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The British film and television industries—decline or opportunity?

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(p) refers to a page of written evidence

SUMMARY

The film and television industries make an important contribution to the British economy. They contribute to national income and employment, and make a net contribution to exports, which has the capacity to grow. Despite the competition from abroad, particularly the US, UK-produced content on film and television has a strong international reputation and makes a major contribution to the entertainment and education of British audiences. This report looks at how these industries have developed, the challenges they are currently facing and what practical help might be provided to enable them to develop further.

Since its inception, the British film industry has experienced periods of boom and bust. From the early years, the Government has recognised its importance and sought to support and protect it, using a variety of tools, including quotas, levies and tax incentives. The industry has been profoundly influenced by the American film industry, built around the major Hollywood studios, which has been at different times an overwhelming competitor and a major investor in filmmaking in the UK. The policy of encouraging American investment has been successful to the point where some two thirds of spending on film production in the UK is on American funded and produced films.

The production arm of the British film industry is its strength. Unfortunately, American companies have always dominated the distribution sector, where much of the profit is to be made. Despite several attempts, no British company has been able to emulate the American model of vertically-integrated companies, which can finance the production of their own films and distribute their own and other companies' productions worldwide. We found this still to be the case, though the coming of digital distribution could offer opportunities for a different distribution model.

Since 2007, the Government has supported the film industry principally through tax relief on film production expenditure. Witnesses from the film industry said the new system had been successful, particularly in attracting big budget films. We recommend some adjustments to the system with the aim of giving more support to smaller films and allowing British films to be partly shot abroad without suffering a financial penalty. Independent filmmakers still face difficulties in financing their films. We recommend that the Government consider ways of encouraging private investment in film production.

The UK Film Council is the UK's strategic agency for film. We found widespread support for its work, but concern that part of its limited budget is being transferred to Olympics funding. We share this concern and question whether the Film Council should be substantially financed through the Lottery. We also question the case for a merger between the Film Council and the British Film Institute, which is currently under discussion.

A number of witnesses saw audiovisual piracy as the main threat to the film industry. We support the Government's decision to introduce measures to combat unlawful file sharing, and welcome the decision of some companies to develop new business models to meet the legitimate demands of their customers. We also recommend new legislation specifically targeted at making the recording of a film in a cinema by camcorder a criminal offence.

The funding of UK-originated content on television is also affected by recent technological and regulatory changes. The last ten years have seen greater competition in the industry, with a proliferation of channels, both subscription and advertising based. Revenue from subscription now exceeds advertising revenue and the competition for the latter now also comes from online.

Despite the increase in the number of channels, the vast majority of UK originated content is produced by the public service broadcasters (PSBs). The spending of the PSBs on UK-originated output fell by 15 per cent in real terms in the five years to 2008. The commercial PSBs are facing serious financial pressures, largely as a result of falling advertising revenue, and this is impacting on their programme budgets, particularly for certain programme genres.

We looked at ways in which this decline in investment could be reversed. We believe the role played by BBC Worldwide in distributing UK content overseas could be expanded, generating more revenue for investment. To this end, we recommend the sale of a part of BBC Worldwide, to create a public private company.

Other ways of encouraging greater production of UK content include a tax credit similar to the film tax credit. We recommend a trial of such a scheme in support of children's programming, which is one of the genres under threat. Other possibilities include the use of the proceeds of spectrum sale and sharing part of the BBC licence fee.

Expansion of online video on demand may provide opportunities for more profit to be made from UK content. One joint venture that would have enabled the PSBs to recoup the online value of their content was Project Kangaroo. This was blocked by the Competition Commission. As a result, American companies may soon take the lion's share of this value. We recommend government intervention in any similar cases in the future, to ensure that the full implications for the television industry are taken into account.

Finally, we looked at training provision across both industries. One of the strengths of the British film and television industries is the highly skilled workforce, both in front of and behind the camera. However, the provision of training is patchy and that there are some specific skills shortages. University courses are not delivering the skills required by the industry. Apprenticeships and internships would improve training in practical skills but are underused. There is also widespread use of unpaid work experience and informal entry routes into the industries, which discriminate against those without connections, while making it unlikely that those recruited are the most able.

The current economic conditions have caused companies in the industry to reduce their in-house training budgets and their contributions to Skillset, the industry training body. We particularly urge the Government to encourage the PSBs to revive their investment in training.

The British film and television industries—decline or opportunity?

INTRODUCTION

1. The creative industries are playing a growing part in the British economy. This report examines two of the most important, film and television—although some of our proposals have implications for other industries like music and videogames. Our aim is to see what practical help we can suggest to enable these two industries to develop further and so benefit employment and overseas earnings as well as adding to our national reputation for excellent and innovative production.

2. The total workforce of the British film and television industries is over 110,000[1]. It is a workforce which takes in actors, directors and producers, reporters and cameramen, animators and make up artists, staff in post-production studios and special effects, and the very many men and women working behind the scenes ranging from electricians and plasterers to sound technicians and researchers. In 2008, British films accounted for around one third of the British cinema box office and generated overseas earnings of over £1 billion. In television, BBC Worldwide, the commercial arm of the corporation, has sales of over £1 billion and few doubt that this figure could be increased.

3. Both industries have won for themselves high reputations. In the last twenty years there have been outstanding British films like *Slumdog Millionaire*, *Four Weddings and a Funeral*, *Shakespeare in Love* and *The English Patient*. British television has also produced a string of award-winning programmes and programme formats, highly popular both in the UK and abroad, such as *Doctor Who*, *The Office, Prime Suspect, Planet Earth, Morse*, and *State of Play*. While in the area of news, British television companies have provided impartial and fair reporting which is respected around the world.

4. Nevertheless both industries now face challenges which have been increased by the global recession. Commercial television supported by advertising has been particularly hit. The problems of the economy have come on top of the structural change caused by the growth of the internet and its success in capturing an increasing share of advertising. One consequence has been that the amount of money devoted to British originated material has reduced and on present trends could reduce further.

5. For many years past, the particular challenge in the film industry has been that the distribution and financing of films has been dominated by the big American studios. The result is that today there is fierce competition around the world to persuade producers to make their films in a particular country. Various financial incentives from tax relief to outright grants are offered to win this inward investment. Producers have no option but to take such incentives into account. If Britain wants to maintain its position as a venue

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[1] The workforce of the film and video industry is over 30,000, and the workforce of the television industry is over 80,000 according to the ONS Annual Business Inquiry 2009. (SIC codes 59.11/3, 59.13/3, 60.2, 59.11/1, 59.12, 59.13/1, 59.14)

for international production there is no alternative but to be competitive in what it can offer.

6. A further threat to both industries is audio visual piracy. Films suffer from both illegal file sharing and camcorder crime when new films are recorded at a cinema by camcorder and then sold as DVDs. The result is that the value of the original work is damaged and the incentive for those who would benefit from subsequent cinema exhibition to invest in new films is reduced. Subscription television faces a similar problem with the illegal transmission of sport.

7. Even more fundamental is the issue of training. Both film and television need skilled workforces. Skills are entirely crucial. They are crucial in bringing overseas producers to Britain to make their films. They are crucial for the making of high quality programmes. Ominously the evidence is that in too many parts of these industries quick economies are being made by cutting training programmes.

8. In spite of these problems we have no doubt that both film and television are capable of achieving more. There are, however, substantial issues to be decided by the policy makers. This report is a contribution to that process.

9. The membership of the Committee is set out in Appendix 1 and the Call for Evidence in Appendix 2. We received 56 written submissions and took oral evidence from 54 witnesses, who are listed in Appendix 3. During the course of the inquiry, we visited Berlin, to look at the ways in which the German authorities support the German film industries. We also visited the film and television studios at Pinewood and Leavesden. We should like to express our thanks to all who have assisted us in our work.

10. Our Specialist Advisers for this inquiry were Professor Steven Barnett, Professor of Communications at the University of Westminster; and Dr Gerben Bakker, Departments of Economic History and Accounting, London School of Economics and Political Science. We have benefited greatly from their expertise.

CHAPTER 1: THE BRITISH FILM INDUSTRY

11. This chapter presents a brief history of the British film industry, focusing on the key issues that have continuing relevance to the success of the industry. It then summarises the current state of the industry, looking in turn at the three distinct but related sectors of the industry: production, distribution and exhibition.

The history of the British film industry

Early history

12. The cinema as an entertainment industry emerged from a series of innovations in the late nineteenth century, mostly in the United States, France and the United Kingdom. In the UK, filmmakers established small studios to produce short films for use by travelling showmen and in music-halls. In the first decade of the twentieth century, more than 30 film studios were established in and around London. British films rapidly established a substantial share of the market at home and abroad, including some 15 per cent of the American market by 1910[2]. This initial success rapidly faded as American production took off, with expensive and heavily marketed feature films. The industry's share of its home market fell from half to less than 10 per cent by 1914[3].

13. At the same time as film production was waning, cinema going flourished as a pastime of the British public. Investment in cinemas surged, with the founding of many new companies and investment of £1.5m (£140m at current prices) in cinemas in 1908 alone[4]. The Government recognised the potential of the film industry, initially as a source of revenue, when it included cinema, together with other entertainments, such as music hall and theatre, in the Entertainment Tax, introduced in 1916. The rate, which was initially set at between 25 and 50 per cent of the price of cinema tickets, was reduced in the 1920s and then raised during the Second World War. It was finally abolished in 1960.

First Government support

14. By 1925, British film production had declined to a point where fewer than 40 feature films a year were being made, compared with over 150 in 1920. The vast majority films shown here were American. In May 1925, Lord Newton raised the issue in the House of Lords, citing "industrial, commercial, educational and Imperial interests" involved, and calling for a Committee of inquiry[5]. In 1927, the Government recognised the importance of film

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2 Analysis of the annual number of British films in American Film Institute, *Catalogue of motion pictures released in the United States. 1893–1910* (New York and London, R. R. Bowker, 1995)

3 Gerben Bakker, 'The Decline and Fall of the European Film Industry: Sunk Costs, Market Size and Market Structure, 1895–1926', in: *Economic History Review* 58, 310–351; 313

4 Rachael Low, *The history of the British film 1906–1914* (London, George Allen & Unwin, 1949).

5 Political and Economic Planning, *The British film industry. A report on its history and present organisation with special reference to the economic problems of British feature film production* (London, Political and Economic Planning, 1952), p 42

production to the British economy and its role in stimulating exports of other goods and services and acted to protect the home market from American domination by means of the Cinematograph Films Act 1927. The Act recognised the interdependency of production, distribution and exhibition, and sought to encourage home production by setting quotas for British-made films[6] to be met by both distributors and exhibitors. The Act was a success, in the sense that production of films in the UK more than doubled by the end of the decade, and resulted in the establishment of several new production companies, including British International Pictures at new studios in Elstree, Warner's studios at Teddington and Fox's studios at Wembley[7]. But it was also blamed for creating a market for poor quality, low cost films, churned out to meet the quota requirements (so called "quota quickies").

The challenge of American film exports

15. While the Government was quick to recognise the domestic importance of the film industry, and particularly film production, the American authorities were even quicker to recognise its importance as an export industry. American missions abroad were reporting on foreign film market opportunities as early as the 1910s. In 1926, Congress appropriated $15,000 to set up the Motion Picture Section within the Bureau of Foreign and Domestic Commerce of the Department of Commerce, which collected market information through 44 foreign offices and 300 consular offices.[8] The Section also appointed a Trade Commissioner in Europe. At the same time, Harvard Business School started to offer seminar series in the business and management of the film industry, and several other American business schools and universities followed. Domestically, the film industry was responsible for about 2 per cent of over-all U.S. GDP-growth and about 3 percent of overall productivity growth between 1900 and 1938.[9] The Hollywood studios generally broke even on the American market and derived their profits from export revenues.

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6 To qualify as British, both the maker (i.e. producer) of the film and the scriptwriter had to be British. The production company had to be legally established in some part of the British Empire, with the majority voting power in the hands of British subjects. Studio scenes had to be shot in a studio in the British Empire and at least 75 per cent of labour costs (excluding copyright payments and the salary of one actor or the producer) had to be paid to Britons or persons living in the British Empire. The quotas started at 5 per cent for exhibitors and 7.5 per cent for distributors in 1928, rising to 20 per cent for both in 1935.

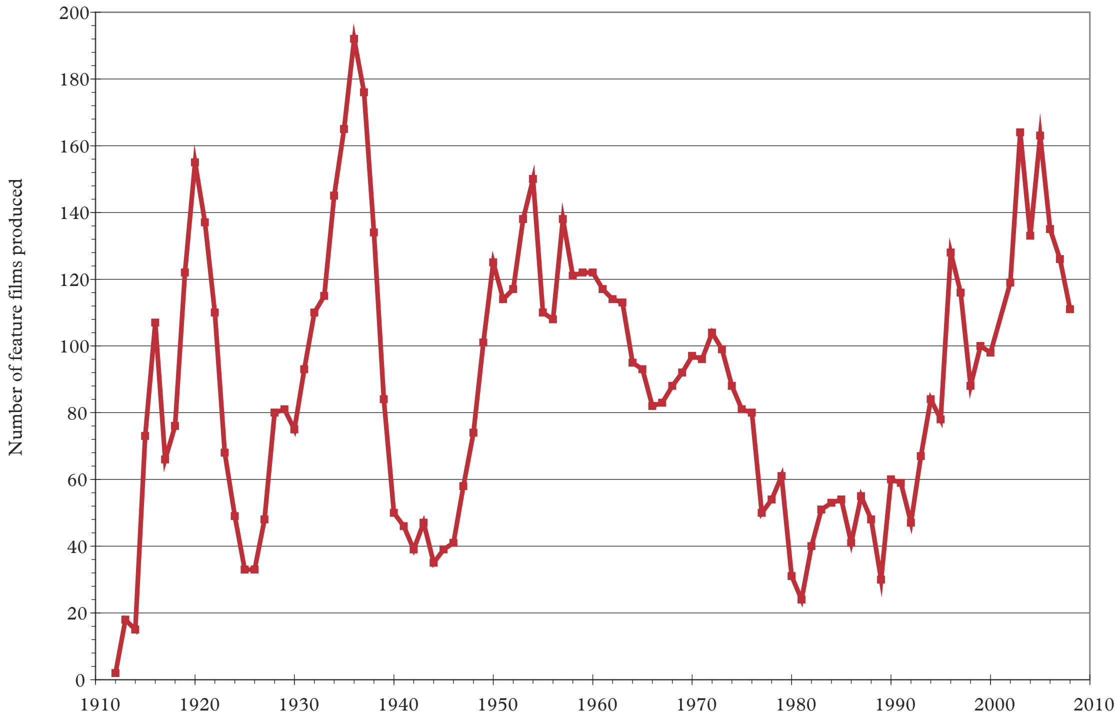
7 Warner and Fox: Margaret Dickinson and Sarah Street, *Cinema and state. The film industry and the British government, 1927–1984* (London, British Film Institute, 1985), p 56

8 Kristin Thompson, *Exporting entertainment. America in the world film market 1907–1934* (London, British Film Institute, 1985), 117–18

9 Gerben Bakker, "Time and Productivity Growth in Services: How Motion Pictures Industrialized Entertainment," *Working Papers in Economic History*, No. 119 (2009), Department of Economic History, London School of Economics, http://www.lse.ac.uk/collections/economicHistory/pdf/WP119.pdf

FIGURE 1

Number of feature films produced in the UK, 1912–2008



Source: 1912–2000: Screen Digest; Screen Finance; British Film Institute. 2001–2008: UK Film Council Statistical Yearbook 2009 (including revised figures for 2002–2007).

Note: The films are all feature films, made in Britain, including co-productions and films made with inward investment.

The 1930s: boom and bust

16. The arrival of "talkies" in 1928 had a positive effect on British film production. Their films were protected in the home market and, unlike the French and German film industries, able to compete with American sound films without the need for dubbing. The result was that the industry experienced a boom. The most successful British film production company was London Film Productions, founded by an immigrant from Hungary, Alexander Korda. The company's breakthrough success was *The Private Life of Henry VIII* (1933). The success of this film in the US helped Korda to establish an alliance with United Artists (the first with a large American studio) who had the commercial muscle to finance his films and ensure American and global distribution. However, by the late 1930s, the boom in British film production came to a sudden end. Over-rapid expansion led to bankruptcies. The number of feature film productions peaked in 1936 at just under 200 and fell by two thirds in the next four years (see figure 1).

17. The quota provisions in the Cinematograph Film Act 1927 had been agreed for ten years and the Act contained a sunset clause. In 1936, the Government set up a Committee chaired by Lord Moyne to investigate what assistance the industry required[10]. Moyne warned of the dangers of foreign (meaning American) control of the industry, particularly the exhibition

10 The remit of the Moyne Committee was "to consider the position of British films, having in mind the approaching expiry of the Cinematographic Films Act 1927, and to advise whether, and if so what, measures are still required in the public interest to promote the production, renting and exhibition of such films".

sector, and recommended both that financial institutions be encouraged to fund film production and that quotas be extended for a further 10 years. It also condemned the "quota quickies" and recommended that the quota rules included a quality test. The Cinematographic Films Act 1938 confirmed the retention of quotas, at 15 per cent for distributors and 12.5 per cent for exhibitors. This was intended to encourage bigger budget films, which could compete internationally. It also encouraged American film companies to make films in the UK, thus getting around the quota restrictions. Warner Bros and Twentieth Century Fox had already established production facilities in the UK. MGM established a British subsidiary, which immediately produced successful films, including *A Yank at Oxford* (1938) and *Goodbye, Mr Chips* (1939).

World War II and the post-war boom

18. The British film industry was still in recession at the beginning of the war but, despite the constraints of the wartime economy, it began to flourish. The number of studios available decreased, but cinema attendance rose from 19m a week in 1938 to 30m a week by 1945[11]. A series of popular films were made which helped to shape the image of a nation at war, including *In Which We Serve* (1942) and *Millions Like Us* (1943). The immediate post-war years saw a surge in British film production to more than 120 films in 1950 (see figure 1). The numbers were matched by outstanding creativity, with films such as David Lean's *Great Expectations* (1946) and Powell and Pressburger's *The Red Shoes* (1948)—the most commercially successful film in the US in its year of release.

19. The 1940s also saw the rise of the first British company to attempt to compete with the Hollywood studios in size and scope. Starting in 1936, J Arthur Rank had built a vertically-integrated film organisation, buying up distributors, cinema chains and production companies. Between 1941 and 1947, The Rank Organisation financed half the films made in the UK, controlled over 600 cinemas and was the largest film distributor. Rank ensured American distribution for their productions and a supply of American films for their cinemas, by securing a 25 per cent stake in Universal film studios through the General Cinema Finance Corporation[12]. Rank provided financial backing to Ealing Studios, which began its series of comedy films in 1948 with *Whisky Galore*.

20. In 1947, the Government, needing to conserve dollars for imports of food and other scarce commodities from the United States, restricted the Hollywood studios to remitting only 25 per cent of their substantial profits. The Hollywood studios responded by refusing to distribute any new films in the UK. The Rank Organisation tried to take advantage of this boycott by producing a series of high-value films but, by the time the films were ready for release, the dispute was resolved and British screens were flooded with a backlog of American films. Rank's production subsidiary lost £3m. During the 1950s, Rank's film production incurred mounting losses and in 1963 the

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11 Office of National Statistics.

12 Geoffrey MacNab, *J Arthur Rank and the British film industry* (London, Routledge, 1992), p. 19–20

management took the decision to diversify out of film production and into other areas, such as the joint venture in photocopying with Xerox[13].

The American threat and further Government intervention

21. In the late 1940s, the Government had become concerned, once again, about Hollywood domination of the film industry and lack of finance for British film production. In 1948, the exhibitors' quota for main feature films was raised to 45 per cent and the Cinematograph Film Production (Special Loans) Act 1949 established the National Film Finance Corporation (NFFC) to distribute loans for film production. In 1950, the Government introduced the Eady Levy, which was a voluntary levy on a proportion of the price of cinema tickets; half retained by the exhibitors and half going to the makers of films made in the UK, in the expectation that it would be used to fund new British film productions. This arrangement was designed so as not to count as a subsidy under the General Agreement on Tariffs and Trade (GATT), to which competitors could have objected. The Eady Levy was made compulsory in 1957 and remained in place until 1985.

22. During the 1950s, despite the support in place, the British film industry came under increasing competition from new technologies. Increasingly, the public turned to home entertainment, as radio listening reached its peak and television developed. By 1958, eight million households had television licences and many of the film studios were closed or sold to broadcasters[14]. The two major British production companies, Rank and the Associated British Picture Corporation, retreated from the ambitious productions of the preceding decade, and concentrated on war dramas and comedies. The turn of the decade saw the appearance of the *Carry On* films and *Hammer Horror* films, which provided low budget work for the British studios for the next 20 years. The *James Bond* films did the same, but at much higher budgets.

American money returns

23. During the 1960s, the availability of Eady funds and American tax legislation encouraged Hollywood studios to shoot more films in the UK. Some American directors, such as Joseph Losey, Richard Lester and Stanley Kubrick based themselves in the UK. The special effects team Kubrick assembled to make *2001, A Space Odyssey* (1968) helped to build the UK's reputation for excellence in this area. The production of American blockbusters, *Star Wars* (1977) at Elstree and *Superman* (1978) at Pinewood, right up to *Moon* (2009) made at Shepperton, demonstrated continuing British expertise in special effects.

US withdrawal in the 1970s and 1980s

24. In the early 1970s, the introduction of an American investment tax credit scheme, new American tax rules on exports and opportunities for Hollywood companies to invest in television led to a severe reduction in American financing of British films. Between 1965 and 1971, annual inflows of American capital for filmmaking averaged £19m. Between 1972 and 1979

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13 Sue Harper and Vincent Porter, *British Cinema of the 1950s: the decline of deference* (Oxford, Oxford University Press, 2003), 35–56, 55

14 B.R.Mitchell, *International Historical Statistics, Europe 1750–2000*

they averaged £6m[15]. British filmmakers increasingly turned to period adaptations, such as *Murder on the Orient Express* (1974), and films based on television programmes, such as *Dad's Army* (1971). The continued availability of the Eady Levy kept up the number of films made, but the drying up of finance was sufficient for the Government to study once again the requirements of a viable and prosperous British film industry.

25. The 1980s began with a serious industry slump, fewer films being made in 1980 and 1981 than in any year since 1914. The incoming Government removed the special support for the industry: tax rules were tightened, the quota system was suspended in 1983 and the Eady Levy and the NFFC were abolished in the Film Act 1985. The Rank Organisation also withdrew from films, which further reduced the funding opportunities. Despite the rise of Goldcrest Pictures, Handmade Films, Merchant and Channel 4 with a surge of high quality and popular films, including *Chariots of Fire* (1981), and *My Beautiful Launderette* (1985), raising British funds was difficult. David Puttnam pointed out to us that he only managed to attract £17,000 of funding for *Chariots of Fire* from UK sources (Q 746). Through the second half of the 1980s, film production declined, with only 30 films produced in 1989. Several filmmakers switched to production of drama for television.

26. Despite the failure of Rank, the Cannon Group took up the challenge of competing directly with the Hollywood studios. Cannon was active not only in film finance but also production, distribution and exhibition. Cannon bought local distributors, smaller production companies, film catalogues and cinema chains in the United States (where it had a distribution deal with MGM), the Netherlands, Italy and Germany as well as the UK, financed by the state-owned French bank, Credit Lyonnais. For a short time Cannon was a major player in the British film industry, but it overextended itself, leading to bankruptcy.

The 1990s: Return of Government support

27. With film production slow to recover from the low point of 1989, the Government took steps to help the industry. In June 1990, the Prime Minister chaired a one-day seminar on the future of the British film industry. The outcome included commitments to a review of policies to stimulate inward investment and promote British films overseas, and the establishment of working parties on the structure of the industry and related fiscal matters[16]. In 1991, the Government established the British Film Commission. In 1992, it introduced tax relief for production expenditure through the Finance Act. In 1995, it decided to allocate lottery money to film production. At the same time, market conditions improved, with cinema audiences recovering from 98m admissions in 1992 to 164m in 2008[17], following the rise of multiplex cinemas (see figure 2). The video market, and subsequently the DVD market, and the proliferation of television channels interested in purchasing films to show, gave films a significant "tail" revenue and added substantially to films' earning potential (see paragraph 33).

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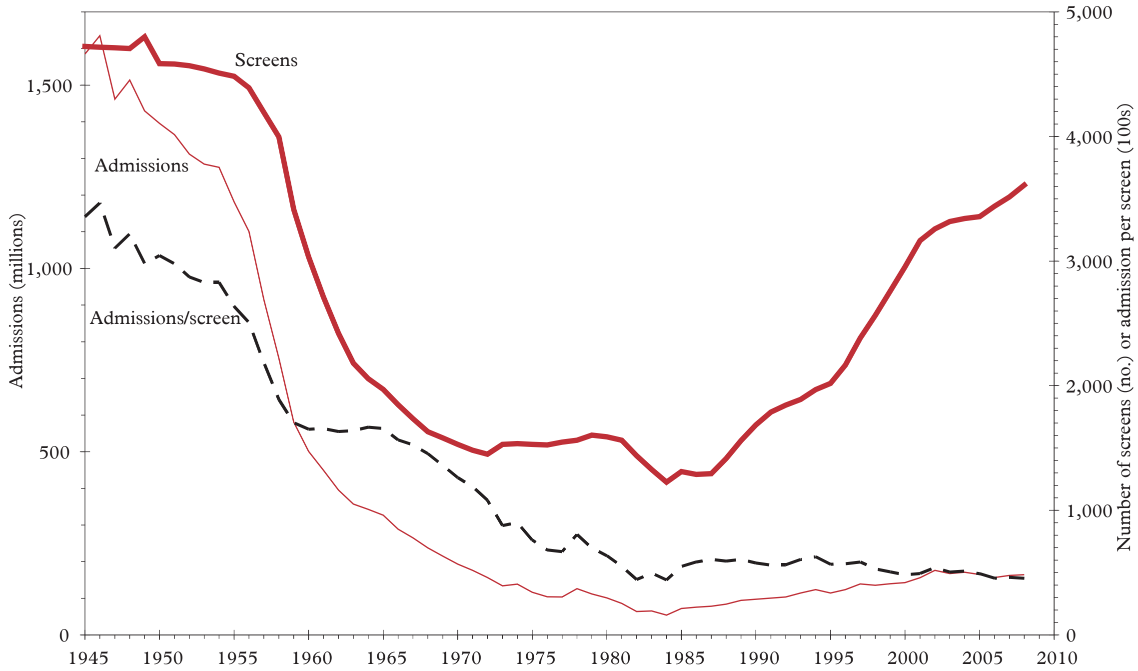
[15] Margaret Dickinson and Sarah Street, *Cinema and state The film industry and the British government, 1927–1984* (London, British Film Institute, 1985), p 240

[16] John Hill, "Government policy and the British film industry 1979–90," *European Journal of Communication*, Vol. 8 (1993), No. 2, p. 203–224; 219–220.

[17] UK Film Council Statistical Year Book, (2002: p 13, 2009: p 7)

FIGURE 2

UK cinema admissions and number of screens, 1945–2008



Source: Gerben Bakker, Entertainment industrialised: The Emergence of the international film industry, 1890–1940 (Cambridge, Cambridge University Press, 2008), p. 408.

28. The early 1990s also saw another UK-based attempt to break into the international film distribution business, when the Dutch-owned music company, PolyGram, diversified into this area and based the headquarters of its film division in London. This distribution network was fed by films from a variety of production companies in the UK, France and the United States. PolyGram's most important British partner was Working Title, which produced *Four Weddings and a Funeral* (1994). After nine years of moderate success, Philips Electronics, PolyGram's owner, decided to sell PolyGram to Universal, and the film division, Europe's only international producer-distributor, was absorbed into Universal films. It remains the case that there is no UK-based international distribution company.

The last ten years

29. The new Government in 1997 took an early interest in the state of the film industry. In the Finance Act 1997 it permitted a hundred per cent tax write-off in the first year for films with budgets of less than £15m, which was intended to help independent filmmakers. In 2000, The UK Film Council was launched, as a non-departmental public body, absorbing a number of public and semi-public bodies involved in supporting the film industry.

30. British film production climbed steadily through the late 1990s to a peak of nearly 180 films in 2002—second only to 1936. This included many accomplished and financially successful films. Working Title, having secured financing and distribution deals with PolyGram and then Universal Pictures, had major international successes, including *Bridget Jones's Diary* (2001), which earned box office receipts of $254m. While the James Bond franchise continued, a major new series of British-made but American

funded films began with *Harry Potter and the Philosopher's Stone* (2001). Aardman Animations, creators of Wallace and Gromit, made their first feature film, *Chicken Run* (2000), which also achieved worldwide success.

31. But in February 2004, the Inland Revenue announced that it was closing a loophole in the tax relief arrangements to prevent tax avoidance schemes. These schemes used the provisions in the Finance Act to encourage the investment of lump sums in the certainty of reducing tax liabilities, regardless of whether the film made a profit. The closing of this and other loopholes in 2004 caused the immediate collapse of a number of film projects in production or pre-production at the time, and the resulting uncertainty contributed to a downturn in film production, with employment dropping by 33 per cent between 2003 and 2008.

32. To end the uncertainty, the Government conducted an urgent review of film tax relief and, in 2006, announced the introduction of a new film tax credit, discussed in Chapter 2, to replace the Finance Act 1997 provisions. In the financial year 2007/08, tax relief granted was worth about £105m, which was about 40 per cent of public funding for film in that year.

The current state of the British film industry[18]

33. The film industry can be divided into three distinct but interdependent sectors—production, distribution and exhibition. The aim of this section is to consider how each of these sectors is currently performing in the UK.

Production

34. The British film industry is production led. In 2008, the UK was the eleventh largest producer of films in the world, by number of films, and fifth largest, after the United States, Japan, France and Germany, by production expenditure[19]. A total of 111 films were made in whole or part in the UK of which 25 were inward investment feature films, which is to say films financed, and on which the decision to make the film is taken, outside the UK. There were 66 domestic productions and 20 were co-productions. The production expenditure on inward investment feature films was £338m, which was 58 per cent of total production expenditure, with an average cost per film of £13.5m.

Inward investment

35. The British industry is heavily dependent on inward investment, almost exclusively from the United States, and the major productions which this brings (see figure 3). In 2006, spend on inward investment features was £558m or 69 per cent of total British production spend and in 2007 £522m or 68 per cent. The UK's ability to attract inward film investment depends on several factors. Stewart Till, then Chairman of the UK Film Council told us that there were three variables on which

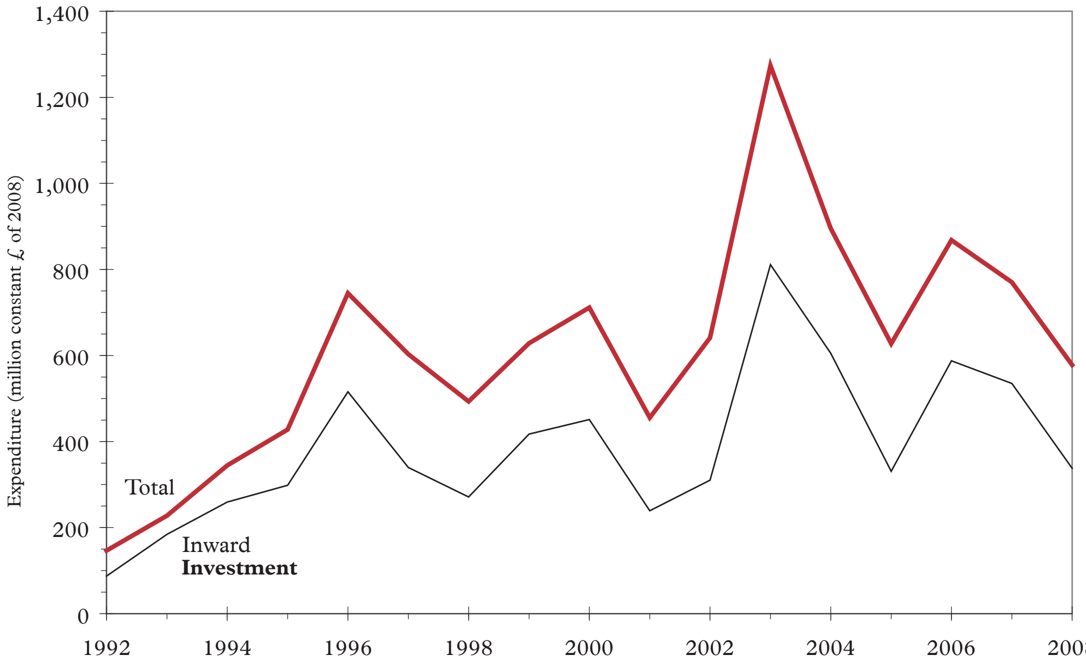
[18] Most of the statistics in this section are taken from the 2009 UK Film Council Statistical Yearbook and "Film in the UK: A Briefing Paper", UK Film Council Research and Statistics Unit, August 2009.

[19] Figures from Screen Digest, quoted in "Film in the UK: A Briefing Paper" by the UK Film Council Research and Statistics Unit, August 2009.

Hollywood studios made decisions on where to make a film. The first was the availability of tax relief. The second, and most important was the high quality of the workforce. Mr Till's third variable was the exchange rate (Q 151). Since American films are budgeted in dollars, when the pound appreciates, the UK becomes a less attractive venue for production.

FIGURE 3

Real film production expenditure in the UK, 1992–2008



Source: UK Film Council Statistical Yearbook; 2009: 138. Values have been corrected for inflation using the UK GDP deflator.

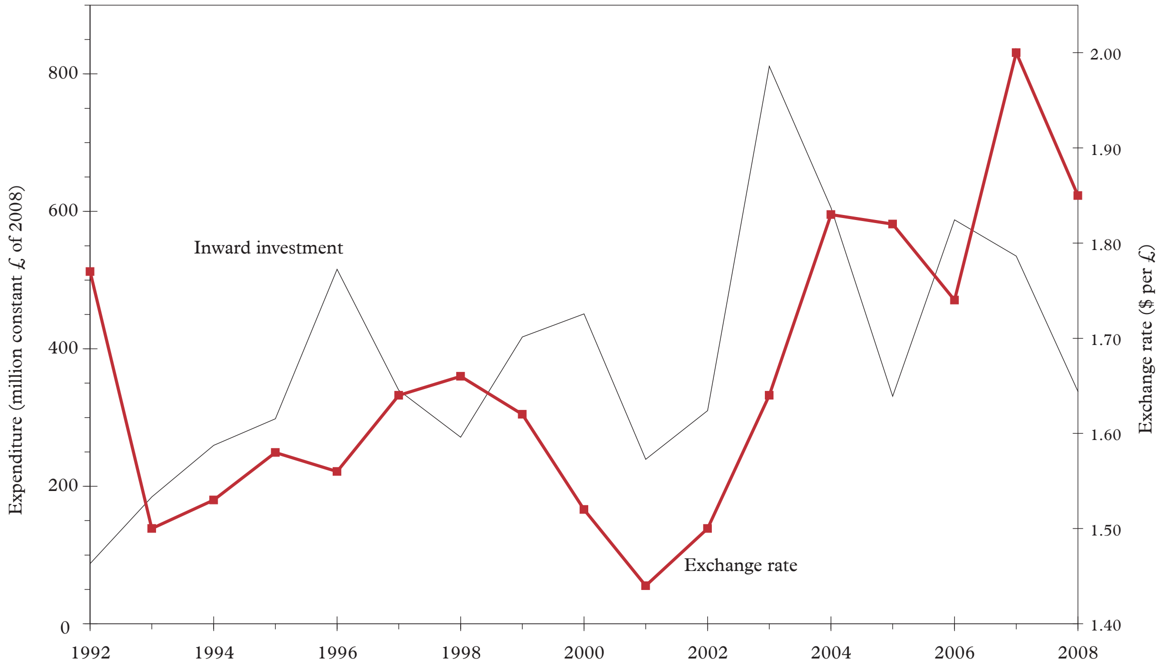
36. The Pound-Dollar exchange rate has had great influence on film production costs and decisions in the last few years (see figure 4). The strength of the UK pound during 2007 was a significant disincentive to American producers. Since lead times for filmmakers are a year or more, this disincentive is reflected in the relatively low figure for inward investment spend in 2008. The subsequent fall in the value of the UK pound has seen a bounce back in inward investment in 2009, with expenditure of £686m in the first three quarters of the year, which is about 20 per cent higher than the entire 2008 expenditure[20].

37. The UK actively encourages inward film investment through the work of the UK Film Commissioner. He seeks to ensure that Britain remains an attractive production base for American films by making American studios aware of the resources available to them, including government financial support and professional talent and expertise. He also works with the screen agencies in the UK to strengthen the production infrastructure here.

20 Other factors, such as the end of the Hollywood writers strike, may also have contributed to the sharp rise in expenditure.

FIGURE 4

Inward investment in UK film production and the average annual dollar/pound exchange rate, 1992–2008



Source: see Fig 3, and Lawrence H Officer, 'Dollar-Pound Exchange Rate From 1791' MeasuringWorth.org.

British film studios

38. The UK has three large film studios, all in the south east of England: Pinewood, Shepperton (which is part of the Pinewood Studios group) and Leavesden. All have world class facilities and are able to accommodate the filming of several large budget films at any one time. Leavesden is currently used exclusively by Warner Brothers, but there are plans to expand the facilities and make them available to other companies. There are a further seven medium-sized studios (all but one in the south east) and 40 smaller studios around the country. These carry out some film work as well as other activities, such as television and advertising.

Production companies

39. In 2008, the UK Film Council's statistics show there were 202 film production companies active in the UK. Of these, two produced four feature films each, five produced three each, ten produced two each and the remaining 185 produced just one feature film each. So the British production sector contains a few large companies making films with substantial budgets and a long tail of small companies producing mainly low budget films[21]. There are currently seven production companies which have long-term agreements with American studios. For example, Aardman Features, has a first-look deal[22] with Sony Pictures Entertainment, and Working Title, is now owned by Universal Studios. There are two production companies which are film-making arms of broadcasters: BBC Films and Film4 Productions. There

21 UK Film Council Statistical Yearbook, 2009 p 145.

22 A first look deal gives a distributor the right of first refusal on new film project that a producer might wish to undertake.

are production companies which are also independent film financiers, such as Ingenious Media Investments, and those which have sales and distribution capability. There are also stand-alone independents, such as Qwerty Films.

Post-production

40. The post-production[23] sector is an integral part of the film production process, though it also serves other industries, notably television and advertising. These companies tend to cluster around centres of production, in this case the south east of England, with 90 per cent of activity in and around London, particularly Soho. A survey[24] in 2005 reported that the British film post-production sector was one of the three largest in world, together with the United States and New Zealand, which benefited from the work generated by the Lord of the Rings trilogy. The survey further found that the British post-production sector was growing rapidly both in absolute terms and as a percentage of film expenditure, where in 2005 it represented a quarter of all film production expenditure. Post-production work is easily tradable: firms in Soho can work for clients anywhere in the world, regardless of distance. So firms that produce high quality work are well placed to compete successfully for export business.

Distribution

41. As the historical section shows, British companies have struggled to make an impact in international film distribution. The distribution sector has always been dominated by the American multi-national film companies. This is a serious issue for the British industry, in that much of the profit earned on films goes to American companies which have part-financed and distributed them. John Woodward, CEO of the UK Film Council, said that the biggest problem of the British film distribution sector was that it lacked scale. "By and large … we are talking about a relatively small number of pretty small companies. What we do not have in the UK is anything approaching the scale of the Hollywood studio, which has the ability … to select the film, finance it, get it made and then distribute it in all markets" (Q 156). Asked whether a British company could ever compete with the American distributors, Danny Perkins, Optimum Releasing, which has two per cent of the UK market, said "There are some very strong independent companies but they have alliances with American companies. That is the key to it really" (Q 1056). He thought the chances of a Warner Bros or a Universal being created in the UK were "not great" (Q 1057).

42. Films are distributed and consumed in a variety of ways—cinema release, retail sales of DVDs, rental of DVDs, films on television and video on demand. The total market for filmed entertainment in the UK was worth more than £3.5bn in 2008, having peaked at just under £4bn in 2004. In 2008, the UK was the third largest filmed entertainment market in the world after the United States and Japan. The first revenue from a film comes from cinema presentation, but this accounts for only 23 per cent of the total. Cinema revenues grew significantly in the late 1990s, but have levelled out

[23] Post-production refers to activities or processes that enhance the visual image or soundtrack of a film. These activities include visual and audio special effects, physical effects, animation, picture and sound editing services and computer generated images.

[24] Oxford Economic Forecasting: The Economic Contribution of the UK Film Post-production Industry, October 2005

since then. Distribution is dominated by the UK-based subsidiaries of the American studios. In 2008, the six American-owned companies between them had 78 per cent of the market, and the top ten distributors had 95 per cent. The largest UK-owned distributor is Entertainment, which in 2008 had eight per cent of the market, with gross box office receipts of £76m.

43. Few if any films make a profit from cinema revenues alone. Instead they rely on the remaining sources, or "tail" revenues, including merchandising, for real returns. This is one of the reasons why audiovisual piracy, discussed later in this report, is such a major issue for the industry. The biggest single revenue source in the British filmed entertainment market is retail sales of DVDs. Revenue from DVDs peaked in 2004, but they were still the most important revenue source for the industry, accounting for 38 per cent of the filmed entertainment market in 2008. Revenues from showing films on television were the second largest contributor, showing slight growth in 2008. The Video on Demand market remains relatively undeveloped in the UK and makes only a small contribution to total revenues, but this is likely to grow.

Exhibition

44. The exhibition sector is similarly dominated by a few large companies, though in this case they are not American-owned. In 2008, there were 3,610 screens (96 more than in 2007) in 726 cinemas in the UK. In 2008, 61 per cent of screens were controlled by three companies: Odeon, Cineworld and Vue. The two largest of these are owned by private equity firms, Terra Firma (Odeon) and the Blackstone Group (Cineworld). Exhibitor revenues, which are made up of box office receipts, concessions and advertising, were just over £1bn in 2008 (three per cent higher than 2007). Although most film are still shown using the standard film print, in 2008, the UK had 310 high-end digital screens, the highest number in Europe, of which 69 were capable of screening digital 3D features.

The economic contribution of the film industry

45. There are various ways of measuring the film industry's contribution to the economy. The basic measure is the gross value added[25] of those companies identified as film companies in the industry statistics of the Office of National Statistics. In 2007, this amounted to £2.5bn, with production accounting for 48 per cent, distribution 36 per cent and exhibition 16 per cent. The 2007 figure was the lowest in real terms since 2003 and a fall of 30 per cent compared to 2006. There are two other estimates, both for 2006, which attempt to take a wider view of the impact of the film industry, and include indirect effects, such as those on tourism. Oxford Economics estimated the "core UK film industry" including flow-on effects to non-film companies (tourism, trade, merchandising), at £4.3bn. By including the business provided to supplier firms, Cambridge Econometrics estimated all film activity in the UK, at £5.3bn.

[25] Gross value added is a measure of an industry's ability to generate income for its employees, owners and investors. Hence it mainly consists of wages and salaries, interest and profits.

Exports

46. The British film industry generates substantial export earnings from film rights and film production services. It also imports in both categories, but the film trade has been in surplus every year since figures were collected (the mid-1960s) and thus the industry has been a significant contributor to the overseas account. In 2007, the latest year for which figures are available, film exports were worth £1,050m, of which £646m was royalties and £403m production services. In the same year, film imports were worth £818m, giving a surplus of £232m.

47. The export of production services occurs when overseas film productions use British studios, locations and services, such as visual effects and post-production. Given the flexibility of the labour market in the film industry, due to the prevalence of freelance and part-time working, export of production services make use of spare capacity. Royalty streams do not use up any current British production capacity and so their full value goes into companies' profits.

Employment

48. According to the Labour Force Survey[26] 2009, there were over 35,000 jobs, full-time or part-time, in the film and video industry. Of these, 60 per cent were in film and video production, eight per cent in distribution and 32 per cent in exhibition. This represents a 13 per cent increase in the workforce since 1996, slightly below the average for the overall British workforce, but a decline of 33 per cent from a peak of nearly 54,000 jobs in 2003. The 2005 study of the film post-production and visual effects sector estimated that it provided 4,400 jobs. Employment in the production and distribution sectors is heavily concentrated in London and the south east. Almost half of those working in the production sector are self-employed: in 2008 it was 46 per cent, compared to 13 per cent for the whole British workforce.

Size of companies

49. The number of companies operating in the film and video industries has grown rapidly in recent years, but this growth is almost exclusively in the production sector. In 2008, there were 7,970 companies working in film and video production, as against 1,745 in 1996: more than a fourfold increase. This reflects a sharp increase in the number of small companies in the production business. The proportion of companies with a turnover of between £1,000 and £99,000 is 57 per cent, which is significantly higher than the average for other industries. While in 1996, the film industry had relatively fewer small companies than the UK as a whole, by 2008 the opposite was the case. In comparison, the distribution and exhibition sectors have seen growth in companies and size of companies more in line with the UK as a whole.

Conclusions

50. There are a number of conclusions that may be drawn from the history and structure of the British film industry, which are discussed in the next chapter.

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26 Conducted by the Office of National Statistics.

51. The government intervened in the film industry, initially to tax the exhibition of films and then subsequently to protect and support the film production industry. It has been a given for almost all of the last hundred years that it is in the interests of the UK—for economic and cultural reasons—to have a healthy and competitive film production industry and that this requires some government support.

52. The film industry has suffered a cycle of boom and bust throughout its existence despite almost constant government intervention. This has contributed to the emergence of a pattern of informal labour practices, including widespread free-lance and part-time work, which is also found in the television industry.

53. The British industry has been profoundly influenced by the American film industry. The shared language and cultural background has helped those working in film to obtain employment in the American industry or American productions in the UK but the output of the American industry has threatened to overwhelm the UK market at various stages. This is particularly true of the distribution sector, where most profits are to be made.

54. In part to counter the American threat, the government has followed a—largely successful—policy of encouraging American companies to make their films in the UK. This has been assisted by the presence of an English-speaking, skilled labour force that can adapt easily to American working practices.

55. The film industry has been a net contributor to UK exports at least since the early 1960s, largely due to the flow of inward investment, which accounts for about two thirds of average British film production expenditure. This is a reversal of the situation in the 1940s, when the industry's large trade deficit was a concern to the Government.

56. The policy of seeking to attract inward investment has had a positive effect on employment and national income. It has had the disadvantage of provoking a slump in production (and employment) when American companies reduce their production budgets or find more attractive opportunities elsewhere.

57. Despite several attempts, no British company has been able to emulate the American model of a vertically-integrated film company, which has interests in production, distribution and exhibition and can finance its own films. Rank, Cannon and PolyGram have tried and had some success, but they were not able to sustain their position in the market.

58. A model which has proved successful for production companies since the 1930s has been to establish a close association with one of the American majors with the finance and distribution muscle. Under this model, financial independence is traded for financial security but with considerable creative freedom.

59. For fully British independent production companies, finance has always been a problem. The government has assisted, either directly or through encouragement and inducements to potential investors, but the problem remains.

CHAPTER 2: A BETTER FUTURE FOR BRITISH FILMS

Financing film production

60. This section looks at the way in which a film may be financed, the financial support provided by the Government and how this might be made more effective.

Film financing models

61. The financing of film production follows two distinct models. The major American studios normally have sufficient financial capacity to fund the making of their films. Much of this capacity derives from their size and range of activities, including distribution. As indicated in the preceding chapter, despite various attempts, the British film industry has not been able to replicate successfully the American model of vertically-integrated companies, involved in production, distribution and exhibition, able to finance their own films. British producers who are not closely allied with an American studio have to follow a different model.

62. An independent British film producer has to build up a patchwork of financing in order for a film to be made. He is likely to be eligible for film tax relief and can approach the UK Film Council, and BBC Film and Film4, the film investment arms of the BBC and Channel 4, who may be prepared to invest in the film. Beyond this, the producer may have to seek equity investment and pre-sale of the film to one or more distributors, against which he can obtain funding. This may still fall short of the finance required. Until the recession, banks might have been prepared to provide "gap funding", but the Committee was told that they had virtually withdrawn from film finance (paragraph 89).

63. Some financing firms offer potential investors a "slate" of films in which to invest, which reduces the risk of investing in one particular film which turns out to be a financial failure, by spreading it over a portfolio, or slate, of productions. Ingenious Media told us that slate financing had become much more difficult to put together since the abolition of the previous system of incentives for film production through tax write-offs (p 190). Michael Kuhn, Qwerty Films, also mentioned the absence in the UK of financing of portfolios of films (Q 776).

64. Charles Sturridge, Chairman, Directors UK, contrasted two films he had made: *Fairytale* and *Lassie*. *Fairytale* was essentially American funded and distributed by Paramount, while *Lassie* "was a classic example of the complexity of creating an independently financed film in the UK". Mr Sturridge said that "at the core contract meeting I sat at a table with eleven lawyers all representing different financiers. That is a sample of the kind of Byzantine complexity one has to go through in order to assemble what was in fact a very low budget, six-week shoot £6 million film" (Q 1437).

65. This model varies from film to film. Tessa Ross, Controller of Films and Drama, and Paul Grindey, Head of Business Affairs, Channel 4, told the Committee that the genesis of *Slumdog Millionaire* involved fewer deals than normal. Film4, having read the book in manuscript and funded the pre-production work, agreed a deal with Celador Productions to co-finance the

production. The fact that they did not require financing from other parties simplified and strengthened their position. Mr Grindey said "We were able to say with a high degree of confidence to the rest of the industry, to the distribution community, that this film was greenlit and going ahead and if you want to join the party then give us your best offer, which … took quite a lot of leverage away from the distribution community because our film was not dependent on any particular negotiation coming good" (Q 11). This demonstrates that it is possible to reduce the financial power of the distributor, but only where a simple and comprehensive deal can be put together.

Government support for the film industry

66. Most Western governments provide financial assistance to their film industries. They are able to support their industries in this way because the World Trade Organisation has, since 2005, recognised a cultural exception to normal trading rules. Reasons for doing so are as much economic as cultural. Governments support the creation of an industry which benefits from economies of scale and, once it reaches a critical mass, can prosper with less need of support.

67. During this inquiry, we visited Germany, where we learned that, in 2008, allocations at the federal and regional level in support of the German film industry amount to €307m (Appendix 6). Government support for the film industry is common across Europe and North America. The largest element within this package of support is normally for film production, either through direct grants or through tax relief. One of the concerns voiced by the film industry is that film production support has become increasingly competitive between Western countries and, in the United States, between individual states, in an effort to attract foreign production. From a British perspective, there is a risk of British support becoming uncompetitive but also of accelerating competition.

Film tax relief

68. In the UK in 2007/08, total public support for the film industry was £261m. The largest single source of public support for production is the film production tax credit, which was estimated to cost £105m in 2007/08, or 40 per cent of total support for the film industry in its first year of operation. The film tax credit was introduced in the Finance Bill 2006. Its key features are that it is provided directly to the film production company—and not to those whose only involvement is providing finance—and it is available to companies making culturally British films, made to be shown in cinemas and where at least 25 per cent of qualifying expenditure will take place within the UK. Whether a film is culturally British is determined by a cultural test[27]. The tax relief is calculated on the amount of the qualifying British expenditure up to a maximum of 80 per cent of total qualifying expenditure, which covers pre-production, principal photography and post-production. Qualifying British expenditure is defined as services performed or goods

[27] In order to obtain the tax credit, film projects need to pass a cultural test, scoring at least 16 points out of a possible 31. They are awarded points for: cultural content (16 points; story in UK, characters British, British novel, English?), cultural contribution (4 points; reflects a diverse British culture, heritage or creativity?), cultural hubs (3 points; studio, filming or postproduction in UK?), and cultural practitioners (8 points; cast, crew and producers British or from EEA?)

supplied in the United Kingdom (known as the "used or consumed" provisions).[28]

69. The current system was supported by most witnesses as essential to the health of the film industry. Tim Bevan, Co-Chairman, Working Title (and now also Chairman of the UK Film Council) said that the film tax credit was "working brilliantly for inward investment in terms of bringing the studios into this country to make big films here" (Q 1404). Michael Kuhn, Qwerty Films described it as "fantastic" and had been designed "very cleverly, very effectively" (Q 763). Lord Puttnam thought that "after three or four false starts … we have a system which seems to be fairly admired, which has been road-tested sufficiently" (Q 763). Gaynor Davenport, CEO, UK Screen Association, thought that, compared to previous film support schemes, the film tax credit is "a much simpler system which is more easily explained and more accessible for people who actually should be legitimately benefiting from the film tax incentive" (Q 930).

70. Several witnesses noted the importance of the tax credit remaining competitive internationally if the UK were to continue to attract inward investment in film. John Woodward, CEO of the UK Film Council said "You need a tax credit frankly to be in the game, because most countries that are serious about their film industry provide one, but the UK tax credit … is worth up to a maximum of 20 per cent of the film's budget. If you go to Australia at the moment, you can get up to 40 per cent of your budget from the Australian government. If you go to Canada, if you use local and federal incentives, you can get up to 60 or 65 per cent of your budget. Ireland in the last week or two has moved its incentive up to be worth around 28 per cent … of the budget. So Britain at 20 [per cent] is at the low end, but we have always maintained the argument that in the UK, the tax credit is there as a cushion and an incentive, but in the end, this is not a Third World economy, we are not going to compete as an industry internationally on price alone" (Q 120).

71. Stewart Till, then Chairman of the UK Film Council, added. "We are at the low end but we are still competitive in terms of tax relief. If our tax relief became very uncompetitive, we would go back to the government and advise them that things had changed; but they have not got to that point yet" (Q 151). He pointed out that, while the rate of tax relief was important, it was one of the three variables on which Hollywood studios made decisions on where to make a fill. He thought that the other two—the Pound/Dollar exchange rate and the quality of the workforce—were more important factors.

72. Industry witnesses broadly supported this view. Roy Button, Managing Director, Warner Brothers Productions, said that his colleagues in Los Angeles and New York would always expect him to compare the government support available when proposing the location for filming a new project, but he acknowledged that there were other important factors (reference). Overall, there was no great pressure from the industry representatives for the tax relief for big budget films to be raised.

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28 Co-productions are treated as national films, and thus qualifying for UK tax relief, where there a co-production agreement in place between the UK government and any other government, international organisation or authority.

73. **We recommend that, given current financial circumstances and the value to the international film industry of a stable tax regime, the Government should keep the rate of the tax credit for big budget films at its current level. At the same time, we recommend that the rate of the tax credit be kept under review by the Government, in consultation with the industry, in order to ensure that the UK does not become uncompetitive as a venue for international filmmaking.**

74. It was suggested, however, that the tax credit be increased as a percentage of the qualifying expenditure for smaller budget films. Tim Bevan said that that the tax credit was working "quite well" for domestic British films, but that it might be improved. He thought that an increase in the tax credit to 30 per cent would make a significant difference to an independent British producer trying to finance a film. "That is because, as an independent producer, I know in my brain if I can get 18 per cent out of the UK that feels like top-up. If I can get 30 per cent that feels like a cornerstone piece of financing and I can go out and raise the rest of the money and I think it will encourage entrepreneurs because producer entrepreneurs are what we need in the business more than anything else"(Q 1405).

75. Mr Bevan argued that this increase would be cost neutral for the Exchequer because "what you would get back in VAT and PAYE and inward investment is probably going to come out cash positive" (Q 1405). There are other, indirect, benefit from films being made in the UK, such as the effect on tourism of the use of British stories and locations. A recent report suggests that the Harry Potter films have led to a 120 per cent rise in visitors to Alnwick Castle in Northumberland and brought £9m worth of tourism to the region[29].

76. The UK Film Council have provided the Committee with the main conclusions of a study, recently carried out by Oxford Economics, on the impact of increasing tax relief on low budget films[30]. The UK Film Council suggest that an increase in the rate of film tax relief on low budget films (which they define as total production costs of £20m or less) would increase the profitability of filmmaking and thus increase the number of films made or increase budgets. Oxford Economics have prepared high and low cases for the likely impact of increases in the net rate of film tax relief to 25 per cent, 30 per cent and 35 per cent. The results suggest that, even on the low case, an increase in the net rate of tax relief would be close to fiscally neutral for the Exchequer, with additional tax receipts covering 90 per cent of the additional cost.

77. In our view, the primary purpose of an increase in the rate of tax relief for lower budget films would be to make it easier for independent producers to finance their projects and thereby to support the making of lower budget films which develop new British talent and tell British stories. It is not easy to define such British films in terms of budget size, but we suggest that, if increased support were available to films with budgets of under £5m, this would catch the sort of projects that we think should be given more support. Of the 66 British domestic feature films made in 2008, 60 had a budget of

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29 "Stately Attraction: How Film and Television Programmes Promote Tourism in the UK", by Olsberg SPI, commissioned by the UK Film Council.

30 The conclusions of this study will be published by the UK Film Council.

less than £5m[31], and would therefore benefit from the proposed change. The work done by Oxford Economics, while based on budgets of £20m or less rather than £5m or less, suggests that the cost to the Exchequer would be small.

78. **Given the problems faced by independent film makers in raising finance for their projects, particularly in the current recession, we recommend that the Government should consider raising the net rate of film tax relief for productions under £5m to 30 per cent.**

79. There were some suggestions for variations to the way in which the tax credit operates. A suggestion we heard was to extend the tax credit for genuine British co-productions to some part of the budget spent offshore. This view was advanced by Tim Bevan and by Roy Button, Warner Bros, who said that "if you have a wonderful film in England and it qualifies and you are doing all the shooting on it, and you have two weeks in France, the money expended on elements of facilities, cameras, lights, people that you have spent in England (so they have paid VAT, tax and everything remains in England) that you take to France does not count in your good spend in England" (Q 1409).

80. Tim Adler, Screen Finance, thought that the "used or consumed" rule should be relaxed, "otherwise we are going to end up with a lot of parochial films" (Q 486). He noted that, as a result of the application of the tax credit, "the amount of UK co-production … has dropped off dramatically. He thought that, £70m of UK co-production expenditure had disappeared, involving British producers (Q 487). Alex Hope, Managing Director, Double Negative (a major visual effects company) also supported a change in the "used or consumed" provisions. He said that, on the film *Hellboy,* he had employed a crew to work in Hungary and "when they were working in Hungary they did not qualify necessarily; but when they came back to the UK they did. That would suggest that it would be better to have more Hungarians working on that production when it was being shot in Hungary rather than UK labour" (Q 932).

81. This extension of the "used or consumed" provisions did not receive universal support. We were told that it could make it more attractive for film producers to use foreign studios, to the detriment of British studios. Michael Grade, Chairman, Pinewood Studios said that it would be using British tax revenue to create economic activity in other countries. He went on to say, "Public intervention in a market of this kind is to encourage spend in the UK … It is the economic activity around a film that is important, and it would be using taxpayers' money to create economic activity in other countries. I cannot see how you can invest taxpayers' money overseas and expect to get a return" (Q 1888).

82. Nevertheless, we understand the wish of filmmakers to be able to keep the same crew on a British film when they do some work abroad without suffering financial penalty. The additional tax relief involved would not be large and would be, to some extent, offset by additional income tax payments by British resident crew members.

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31 UK Film Council Statistical Yearbook, 2009, p 142; UKFC statistics do not record films with budgets of less than £500,000.

83. **We acknowledge that there would be a benefit to producers from a change to the "used or consumed" provisions, to extend the tax credit to production expenditure overseas, and the low cost of this change. We recommend that the salaries of personnel employed on a film should be considered eligible costs whether they are working in the UK or on location overseas so long as the personnel are paid and taxed in the UK.**

The videogames industry

84. The videogames industry is a growing industry that draws upon similar skills to the film industry—particularly in post-production—and has a degree of overlap in content. According to Skillset[32], the British videogames sector in 2008 included 155 companies specialising in developing games, 30 companies which published and produced games and 35 which provided games support. Employment in games development amounted to nearly 9,000 jobs and a turnover of £625m[33]. The market for videogames in the UK has grown rapidly, though with fluctuations, over the last three decades. Software sales grew from £73m in 1980 to £2.1 bn last year[34]. British companies have proved very successful in game development and, according to Richard Wilson, Chief Executive, Tiga (the trade association of videogame developers), the industry generates sales worth £2 bn annually in the UK and the rest of the world (QQ 971 and 972). Mr Wilson also told us that "a typical games development business in the UK earns about 46 per cent of its turnover from export of its product" Q 971).

85. The videogames industry representatives told us that that they were under challenge from subsidised production overseas, and that this was evident in relative growth rates. Richard Wilson said: "Whereas the UK games industry has grown in terms of employees by about eight per cent over the last two years, in Quebec the workforce has grown by about 52 per cent because of the very generous tax breaks. At a federal level, there is a tax break for going into production that amounts to about 37 per cent. In Quebec itself the government, incredibly, will pay the salaries of game developers to the tune of 37.5 per cent of their wage costs" (Q 1015).

86. Richard Wilson drew attention to a support scheme currently in operation in France, which provides a 20 per cent tax break for games production. Mr Wilson went on to say: "It would be fantastic to have the very generous tax breaks for going into production that our compatriots overseas receive for example in Quebec, but at a bare minimum we would like the UK Government to adopt a tax break of 20 per cent for going into production" (Q 1017). Ian Livingstone, Creative Director, Eidos pointed out that, while the film industry benefited from tax credits and the games industry did not.

87. Tiga has lobbied the Government for a tax incentive for videogame development, but the Pre-Budget Report said that it was not persuaded that

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32 Skillset, the Sector Skills Council for Creative Media, "Computer games sector: labour market intelligence digest", 2008, p 1

33 Ibid and Oxford Economics, "The economic contribution of the games development industry", October 2008, p 2

34 The 1980 value is corrected for inflation and expressed in constant 2008 pounds .Estimates from Monopolies and Mergers Commission. Videogames: *A report on the supply of videogames in the UK*, March 1995 and Entertainment Retailers Association, *Statistical Yearbook*, 2008, p 18

the evidence was "sufficiently compelling" to introduce such a tax incentive at this time. The Government did, however, announce plans to invest £3.5m to establish two centres of excellence for the games industry in Dundee and Manchester. [35]

88. **We recognise the claims of the videogames industry for support in the face of foreign government-subsidised competition, and recommend that the Government consider providing tax incentives for videogames production.**

Other issues in film financing

89. Many witnesses drew attention to the difficulties of obtaining funding for British independent film production, particularly following the economic recession and the withdrawal of banks from funding of film production. Tim Adler, Editor Screen Finance, said that "a lot of the banks are now pulling out of film finance because they have had their fingers burnt and they cannot lend in the way that they used to" (Q 469). David Pope, CEO, New Producers' Alliance, told us that "the contribution to the financing of films the banks were making has, to all intents and purposes, gone". He said that banks had provided "gap funding", which is money committed "late in the financing stages and … required to be given back early in the recoupment process, and so that last 20 per cent of the budget has gone" (Q 386).

90. While there was firm support for the film tax credit, some witnesses did point out that the previous system of film support through tax write-offs, though it had been subject to abuse, had attracted equity investment into the film industry. Ingenious Media argued that much of the relative boom in the production of British films after 2003 was due to equity investment. In turn, much of this investment was attracted by accounting rules that embodied the principle that investors' losses could, for accounting purposes, be offset against profits. These rules on "sideways loss relief" (SLR) governing individual partnerships were changed in the Finance Act 2007. In the view of Ingenious Media, the changes were "blunt and indiscriminate … and made no distinction between bona fide investment and tax avoidance" (p 190). Ingenious Media go on to say that their "experience as investors before 2007 was that the availability of SLR was crucial to attracting the large sums involved in putting together production slate financing. There was a vital linkage here: SLR effectively enabled the larger share of funds to be raised from investors—funds which, in turn, made the production tax credit work. In the absence of SLR, or an equivalent form of relief designed to encourage the raising of high risk equity capital, the production tax credit is insufficient in itself to enable films to be made" (p 190).

91. Ingenious Media raised the potential role of Venture Capital Trusts (VCTs) and the Enterprise Investment Scheme (EIS), in attracting risk investment to the audiovisual sectors. James Clayton, Chief Executive, Ingenious Investments said that there were "certain constraints in terms of size imposed by VCT and EIS rules, which made them [currently] not particularly suitable for film investment" (Q 812). We did not receive sufficient evidence in this area to make specific recommendations on particular vehicles for equity investment in film.

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92. Tim Adler suggested that the Export Credit Guarantee Scheme could be extended to foreign pre-sales of British films. British independent producers often depend on pre-sales to foreign distributors to finance their films. It is on the basis of these contracts that banks, or other investors, have provided funds to make the film. Although this source of funding has all but dried up since the onset of recession, if the Government were willing to provide guarantees for these contracts with foreign distributors, investors might be encouraged back into film funding. Mr Adler thought that "if a bank could have the risk underpinned by the Export Credit Guarantee Department it might encourage them to come back in to lend to film and television companies" (Q 469).

93. **Given the difficulties of financing independent British films, particularly following the withdrawal of banks from film financing, we recommend that the Government should look at ways of facilitating greater British private investment in film production. This would need to be done in a way that ensured that the private investment was genuine and not simply a means of tax avoidance.**

Is there support for a film levy?

94. We discussed in Chapter 1 the Eady Levy, a levy on the price of cinema tickets to create a fund which could be used to help finance British films which was in place from 1950 to 1985 (discussed in paragraph 21). We asked a number of witnesses whether they favoured the reintroduction of a levy to help fund British productions. Lord Puttnam stressed the important role that the Eady Levy had played in helping his generation of British filmmakers to make their first commercial films and thus launching their careers. He noted that the Eady Fund "was responsible for 820 films, some very good films. The important point is that Ridley Scott's first film, Alan Parker's first film, my first film, the early work of our entire generation was partially funded out of the Eady Fund; that is not there any more. In every other respect I would say things are better now than they ever have been for people starting out in their career" (Q 748). He did not, however, specifically advocate its reinstatement, suggesting that it was not necessary in current circumstances.

95. The levy continues to be used as a source of film funding in Germany. The German Federal Film Fund's (FFA) budget of nearly €70m a year is raised by a levy on cinema operators, video and DVD retailers, and public and private broadcasters. The Chief Executive, Peter Dinges, told us during our visit to Berlin that the levy system, which has been in place for 40 years, was, in effect, a solidarity fund, raising money and distributing it within the industry. It made the funding of the FFA independent of government, in the sense of not requiring budgetary subventions. It was also self-administering, with members of the industry sitting on the Board. However, he noted that the cinema operators had broken this solidarity by challenging the legality of the levy, on the grounds that the different treatment of broadcasters violates the principle of equal treatment in the German Constitution. A decision on the case is expected later this year (see Appendix 6).

96. Other witnesses, notably the panel of film producers (Roy Button, Tim Bevan and Tracey Scoffield, Director, Rainmark Films) opposed the idea on the grounds that it would muddy the waters of existing government support (Tim Bevan: "I think if we get the tax rebate right that probably does

it.") and suggested that, if it were levied on cinema tickets, could reduce cinema attendances (QQ 1416 and 1417).

97. We were struck by the lack of support for the idea of a levy to create a fund for independent film production, which appeared to us markedly different from the position in the television industry, where we heard calls for the use of a levy to support production of British content (see Chapter 4). We conclude that this is, in part, support for the current film tax relief system, both in terms of the support it delivers and the efficiency of its operation. There is clearly a reluctance to go down the film fund route, perhaps because this might put in jeopardy the preferred means of support.

Role of UK Film Council and the British Film Institute (BFI)

98. The UK Film Council was established in April 2000 as the UK's strategic agency for film, with the overall aim of building a more successful and sustainable British film industry. It is a non-departmental public body reporting to Parliament and the Department of Culture, Media and Sport (DCMS), constituted as a private company limited by guarantee and governed by a board of 15 directors. The UK Film Council offers policy advice to the Government on issues affecting the British film industry and also acts as an advocacy body for the industry. It provides funding to support script development, film production, film export and distribution, film education and film skills training. Its funding comes mainly from Lottery Fund income and the Department of Culture, Media and Sport grant-in-aid. From April 2010 it will be one of a number of organisations to have part of its Lottery funding diverted to the funding of the 2012 Olympics. Within the UK Film Council is the Office of the British Film Commissioner, whose role is to promote the UK as a venue for foreign (almost exclusively American) film production. To this end, he has an office in Los Angeles as well as London.

99. The BFI is the UK's cultural agency for film and guardian of the national film collections. It was founded in 1933 and granted a Royal Charter in 1983. It is grant-in-aid funded by the Department of Culture, Media and Sport through the UK Film Council, with an additional £1m levy from commercial terrestrial broadcasters to fund the television element of the BFI National Archive. A further 55 per cent of its total funding is self-generated income.

100. We sought evidence on the role played by the UK Film Council in supporting the UK film industry and whether this could be improved. Industry witnesses were generally supportive of the work of the UK Film Council and thought it an improvement on the more diffuse arrangements in operation before 2000. However, Michael Kuhn, Qwerty Films, expressed the view that the UK Film Council spread its limited budget too widely and should concentrate its effort on supporting film production (Q 769). Tim Adler, Screen Finance, said that the importance of the Film Council "cannot be overestimated. It is a very important body for the British film industry" (Q 460) but went on to note that it drove a hard bargain—some would say too hard—in its financing terms, achieving the highest rate of return of any film fund in the world.

101. Witnesses also expressed concern that a part of the Lottery funding allocated to the UK Film Council for use in supporting UK film production is to be transferred to the Olympics. The annual transfer of about £5m represents 15

per cent of the UK Film Council's anticipated Lottery income for the years 2010/11 to 2012/13. This is not a huge amount in strictly financial terms but, in our view, it calls into question the practice of supporting an important industry through a source which can be diverted away for reasons unconnected with the film industry.

102. The Secretary of State for Culture, Media and Sport, Ben Bradshaw, told the Committee that the Olympics was a unique event and that the UK Film Council was only one of the recipients of Lottery funding that was being affected by the Olympics. He thought it would have been "difficult … to make a case to uniquely exempt the UK Film Council from taking its share of the burden of the Olympics" (Q 2355). We welcome Mr Bradshaw's assurance that the reduced level "would not represent the new baseline" and that "there is no reason … why it should not be restored afterwards but that will obviously depend on the economic circumstances and on the Government's policy at the time" (Q 2354). We consider this issue further, in Chapter 5.

103. **We question, however, whether an industry body like the UK Film Council should be substantially financed by the Lottery rather than direct Government support. We regret the reduction in funding made because of the demands of the 2012 Olympic Games. We recommend that the funding level should be restored immediately after 2012/13.**

Proposed merger between UK Film Council/British Film Institute

104. Since the Committee took evidence from the UK Film Council and the BFI, the Department of Culture, Media and Sport has initiated merger talks between the two organisations, which are continuing. Concerns have been raised about how a merged organisation might meet the different objectives which the two bodies currently pursue and what its status might be, bearing in mind that the BFI has charitable status and a Royal Charter.

105. We put some of these concerns to the Secretary of State, who said that the Government wanted to ensure that the economic role played by the Film Council and the cultural role played by the BFI were maintained. "We would also have to be very careful about retaining within the new organisation the charitable status of the BFI, but we do think that … it is always worth looking at how organisations can work in a more streamlined way ... We are very well aware of the sensitivities of the BFI in particular, but we hope that we will be able to come up with a model that can preserve the qualities of both organisations and at the same time release money … to maximise the cultural benefits these organisations can bring. If one speaks to people who work day-to-day in the film industry, they often do not quite understand why we need to have these two separate organisations" (Q 2350).

106. At a time when public expenditure is under pressure, the Committee recognises the need for the UK Film Council and the BFI to seek efficiency savings and that a merger may reduce their joint administrative costs. But these are not large organisations and potential savings are limited. The Committee is concerned that this should not be a forced marriage that damages the core functions of the existing organisations.

107. **We do not consider that the small saving, which a merger of the UK Film Council and the BFI would be likely to achieve, would by itself justify an amalgamation.**

108. **If, however, the proposal for the merger of the UK Film Council and the BFI goes ahead, it will be important that any organisational changes neither prejudice nor deter private donations to the BFI's educational and archival work.**

UK Film Council funding priorities

109. In November 2009, the UK Film Council launched a consultation document[36] on its policy and funding priorities for the next three years, when the Council will have a reduced budget due to reduced Lottery funding. The Committee has already expressed its concern above at the loss of Lottery funding for film. In the circumstances, the Committee thinks it is right that the Council should focus on support for film production in the UK, including attraction of inward investment in film production. The UK Film Council is proposing to strengthen the Los Angeles office of the Office of the UK Film Commissioner. The UK Film Council reports that inward investment in the British film industry was at an all-time high in the first nine months of 2009 at £686.4m. The Committee supports the reinforcement of this success.

110. **We welcome the UK Film Council's emphasis in its consultation document on supporting British films and filmmakers as its first core activity, and its proposal to use funds recouped from its investment in film to top up the Film Production Fund's budget.**

111. **We support the UK Film Council's continuing commitment, as part of its first core activity, to the promotion of the UK as an inward investment destination for film production. In this context, we strongly support the proposal to strengthen the Office of the British Film Commissioner.**

Investment in film by the BBC and Channel 4

112. The BBC and Channel 4, through their film arms, BBC Films and Film4, each invest around £10m–£12m a year in new British films. This is spread over five or more films a year and often takes the form of the first investment to get a project moving. The British independent film production sector finds this investment highly valuable and would like to see BBC and Channel 4 put more money into film. Tim Adler, Film Finance, emphasised the high value to the broadcasters of their small investment: "When you consider the paltry amounts of money that British broadcasters, such as Channel 4 and the BBC actually invest in the film business—£10 million pounds each—what they get in terms of the BBC brand around the world being seen on cinema screens is a fantastic deal from the broadcaster's point of view" (Q 494) The BBC invests 0.4 per cent of the licence fee in film; Channel 4 invests 1.8 per cent of its revenue.

113. Mark Thompson, Director General, BBC, said that the BBC had to recognise that it is, fundamentally, a broadcaster and that the public pay the licence fee to receive broadcast services from the BBC. "I believe that at £12 million a year, we are at a level—this is paying, typically, investment in eight to 12 British films, alongside the Film Council, alongside Film4—that feels,

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[36] UK Film: Digital innovation and creative excellence: Policy and funding priorities April 2010 to March 2013.

to me, about right in striking the right balance. The public get from it not just a supply side benefit in terms of a British film industry which is making more feature films than would otherwise be the case, they also get to see these eight to 12 films on the air`"(Q 2087).

114. Andy Duncan, Chief Executive, Channel 4, said that, for Channel 4, film investment was "not a commercial activity; it is ultimately a creative activity. It is about creative endeavour to invest in outstanding film ideas that might otherwise not be made. Crucially, Channel 4 has … first right to show those films on Channel 4 itself". The investment has "a huge knock-on benefit into the wider British film ecology that is wholly helpful" (Q 2160). Mr Duncan said that film investment was "very important as a longstanding part of what Channel 4 has always done. The investment in the sorts of British films that Channel 4 has done has had a real cultural and social value as well as an economic benefit to the British film industry … In balancing it over time, although sometimes commercially it is a cost … there are more successes than failures … Certainly I would hope … there will be the opportunity when the final budgets are decided to put a bit more in next year rather than less" (Q 2220).

115. The Digital Economy Bill, which was introduced on 19 November 2009, proposes that the remit of Channel 4 be amended to include "the making of high quality films intended to be shown to the general public at the cinema in the United Kingdom and the broadcasting and distribution of such content and films".[37]

116. There is clearly a need for the BBC and Channel 4 to keep their investment in film in proportion to their main activities, but this must be balanced against the value to the British film industry, and particularly the encouragement of new talent, which their investment represents.

117. **We welcome the provisions in the Digital Economy Bill, which would bring film production within the public service remit of Channel 4. We encourage the BBC to give greater recognition to the role that BBC Films can play in developing new projects and new talent in the British independent film sector.**

Distribution

118. As highlighted in Chapter 1, the distribution of films in the UK is dominated by American companies. While it may vary from year to year, UK Film Council statistics show that the six Hollywood studios have over 75 per cent of the British market and the British independent distributors share the remainder. Again, as Chapter 1 demonstrates, this is not a new problem, but has been with us for nearly a hundred years. The House of Commons Select Committee on Culture, Media and Sport drew attention to it in their report on the film industry[38]. The report noted[39] that "The nature of the British film industry is perhaps not what we would wish it to be" and this could certainly be said to apply to arrangements for distribution of films.

119. David Kosse, Universal Pictures, suggested that the arrangements were not as detrimental to the distribution of British independent films as might, at

37 Digital Economy Bill [HL], Clause 21 (1)

38 Culture, Media and Sport Committee, Sixth Report (2002–03): The British Film Industry

39 Ibid, page 3

first, appear. While Hollywood companies had 75 per cent of the distribution market in the UK, it did not mean that they were sourcing only Hollywood films. "The studios generally, are a model as to financing on a global scale a slate of movies—15 to 20 movies on a worldwide basis—and source those from around the world" (Q 1051). He pointed out that, despite the dominant position of American distributors, British films still had around 31 per cent of the British market in 2008 (Q 1047). At the same time, the Hollywood studios sometimes fail to see the potential of a film and an independent distributor can pick up a worldwide hit. Danny Perkins, Managing Director, Optimum Releasing, told us that, in the last year, it had proved difficult to finance *The Wrestler*. "We got involved at an early stage, helped to sort [the financing] out and it became a film that resonated around the world and delivered for us really well in this market" (Q 1069).

120. The Government has intervened before in the distribution sector, setting quotas under the Cinematograph Films Act 1927 (though these were aimed at supporting British film production). We did not receive specific suggestions for intervention by Government to try to encourage changes in this structure. But we were told that the arrival of digital distribution could end the dominance of the distribution sector by the American studios. Eric Fellner, Co-Chairman of Working Title and Deputy Chairman, British Film Institute, said that the barrier to entry was the network of physical distribution and the ability to get films into cinemas and do deals with television companies. "Once digital distribution becomes available … where we can go and make a film and we can stick it out there, if we can find a couple of hundred grand or whatever to publicise [it] …, the final barrier to entry to the industry will disappear … That is not more than five or ten years away; I do not know if they fully believe that but a lot of people in the industry believe that" (Q 1179).

Exhibition

121. In his evidence, Professor Ian Christie, speaking on behalf of the Association of Independent Film Exhibitors, expressed concern over the position of smaller distribution and exhibition companies: "a typical small-scale film … gets very brief, fixed runs at a regrettably small number of cinemas around the country" (Q 1689). Professor Christie's specific concern was over the UK Film Council's Digital Screen Network initiative, a £12m investment to equip 240 screens in 210 cinemas in the UK with digital projection technology. He said that the scheme had been successful in putting the UK in the forefront of the new technology, with more digital screens in operation than any other country. But it had created problems. It had proved more expensive than expected and there were insufficient digital projectors to make the miniplexes work. Since the scheme was due to run out in 2011, there were problems of economic sustainability for independent cinemas (Q 1690). In fact, the UK Film Council has confirmed that all of the money allocated to the scheme was committed by May 2007 and there are no plans to extend the scheme.

122. Given the pressures on the UK Film Council's budget, the Committee acknowledges that it is not realistic to call for the Digital Screen Network initiative to be extended.

123. **We urge the Government, the UK Film Council and the organisations representing the exhibition sector to find a way of completing the**

digital equipping of cinemas in the UK which, as necessary, provides help to smaller independent cinemas to purchase or lease digital equipment.

Audiovisual piracy

124. One problem on which there was a wide measure of agreement among witnesses from the film industry was the threat to the industry posed by audiovisual piracy. There are two separate issues: camcorder recordings of films in cinemas and file sharing.

Camcording

125. Camcorders are used to record new films in cinemas for copying and sale as DVDs. This market exists, in part, because there is a time lag between a film's cinema release and its appearance as an officially-sanctioned DVD for rental or sale. The Committee was told that camcorded DVDs can now be of surprisingly high quality.

126. Timothy Richards, Vue Entertainment said "This is sophisticated, organised crime … These are sophisticated recording devices" (Q 1655). Mr Richards went on to explain that, over the last ten years, governments in the United States, Canada, Europe and Australia had passed legislation making camcording in cinemas illegal. The UK was the last of the Western countries that did not have legislation. Phil Clapp, Cinema Exhibitors' Association, said that the problem had migrated to the UK, following the deterrent effect of legislation and its implementation elsewhere.

127. Mr Clapp said that the need for legislation in the UK had been "a long-running discussion and debate with Government. Government officials would maintain that the current Fraud Act 2006 is sufficient to deter and prosecute … The difficulties with that are manifold … I have sat in several meetings with government lawyers where there has been a disagreement among them as to whether it is applicable. So … on a cold Friday night in the Cardiff Cineworld, a policeman turning up is hardly likely to be equipped to understand whether or not something is an offence" (QQ 1665 and 1666).

128. Digital Britain states that, "in relation to rights, the Government believes piracy of intellectual property for profit is theft and will be pursued as such through the criminal law", which appears to support the case for specific legislation, given that there has, as yet, been no successful prosecution under the Fraud Act. But Lord Carter of Barnes stated that "the Government's view is that the Fraud Act 2006 should be fit for purpose, and that should be borne out when there is a suitable test case. But in any event there are other criminal offences which, depending on the specific circumstances, might be used instead or in addition"(p 398). Ben Bradshaw subsequently told us that a suitable test case had been found "and is coming to the courts imminently" (p 527).

129. **Irrespective of the outcome of the test case on camcording of films in cinemas, we remain concerned that the law is unclear and provides insufficient deterrent to abuse. We recommend that the Government reconsider the case for specific legislation to make it a criminal offence to record a film in a cinema by camcorder.**

Illegal file sharing

130. The second issue is audiovisual piracy through illegal file sharing. The case for action was most vividly put by Tim Bevan, Working Title. In describing the problems facing the business model of the film industry, he referred to two major problems: the economic downturn and a second "which is a far more pernicious one, in my opinion, is the digital world" (Q 1375). "Sales of DVD around the world are collapsing and this is because of the internet and basically file-to-file sharing on the internet and internet piracy. If we do not do something about that … then the creative industries broadly are in huge trouble. The creative industries I see as … a bucket of talent, which is fantastic for this country and it is fantastic for any country that has a strong creative industry base, but right now there is a hole in the bottom of that bucket and we need to do something about it" (Q 1376).

131. Digital Britain sets out proposals for legislation to reduce unlawful peer-to-peer file-sharing. The main obligations to be placed on ISPs are to notify infringers that their conduct is unlawful and to collect anonymised information on serious repeat infringers. They may then be required to take technical measures aimed at deterring infringement, such as blocking or bandwidth capping. This is taken forward in the Digital Economy Bill, which sets out measures to tackle copyright infringement, firstly through more effective legal action and the education of consumers and secondly through reserve powers to introduce technical measures such as disconnection of persistent file sharers.[40]

132. **Given the strength of film industry concern about the threat from audiovisual piracy, as reflected in the evidence we received, the Committee supports the Government's decision to introduce regulatory measures to combat unlawful peer-to-peer file sharing.**

133. At the same time, we received evidence from the industry acknowledging that digitisation required changes in the business model by which film and television content is marketed. Charles Sturridge, Chairman of Directors UK, said that there was a revolution taking place in the dissemination of audio-visual work in films and television. "We are now facing a change which, although it is much debated and much discussed, understandably, is still not, I suspect, completely understood. We are in a sense in a generation of cavalry officers trying to work out tank tactics" (Q 1424).

134. Martin Smith, Special Adviser, Ingenious Media told the Committee that the answer to piracy "is not only about changes in the law. It is about new business models, collapsing the windows [of distribution]" (Q 840). Michael Kuhn, Qwerty Films, spelt this out in detail. "The [windows] have been naturally collapsing, partly because of piracy—if you take too long a time before you bring out your DVD the pirates will have it, partly because if you are Sky and you are paying a huge amount of money for the pay-TV rights to a Hollywood studio you do not want to wait a year until it comes on Sky because people have forgotten the marketing campaign for Terminator 7 or whatever it was by then. There is a natural collapsing, therefore, but I would argue that it should not be resisted as it is now by the studios but encouraged, and windows should be differentiated by price. We should be

40 Digital Economy Bill, Clauses 4–17.

saying "You can have whatever you want when you want but it is going to cost you more or less" (Q 772).

135. Tim Bevan, acknowledged that "It is our job as an industry to come together to make a new business model for moving forwards, but then we have to have the backup of extremely forceful measures to stop this piracy because piracy is going to kill us" (Q 1377). "One of the things we have to do as an industry is come up with a business model that makes films available on the internet at a reasonable price and all the rest of it" (Q 1380).

136. **We welcome the decision of some companies in the audiovisual industries to change their business models in order to meet the legitimate demands of their customers while generating a return on their investment in content, and encourage other companies to do the same.**

CHAPTER 3: BRITISH TELEVISION

137. This chapter considers the issues facing the production and distribution of UK-originated content for television. The first part of the chapter outlines a brief history of British television and current viewing patterns; the importance of television in economic and cultural terms; and the regulation of the television industry. The second part of the chapter considers current pressures on the provision of UK content with a focus on specific programming genres; and the independent sector's contribution to UK content production.

A brief history of British television

Television's early days

138. The world's first regular television service was launched by the BBC in November 1936. The Marconi-EMI 405-line "high definition" service transmitted around four hours of programmes each day from Alexandra Palace, available only to owners of sets in the London area.[41] In May the following year, King George VI's Coronation procession became television's first outside broadcast, while the Wimbledon championships became Britain's first televised sporting event. This was, however, still very much a minority interest: when television was suspended on 1 September 1939 because of the war, there were fewer than 20,000 TV sets in operation.

139. BBC television resumed in June 1946, with a combined £2 radio/television licence fee (separate from the pre-existing radio licence) introduced in the same month. Over the next few years, the service was gradually extended outside London, but the watershed broadcast was the televising of the Queen's Coronation in June 1953, covered by 21 cameras and watched live by around 27 million viewers in the UK as well as by viewers in Germany, Netherlands, France, and Belgium. This proved the catalyst for the purchase of television sets, and is generally regarded as the "tipping point" for television in the UK.

The BBC/ITV duopoly and the rise of television

140. In 1954, the Government decided that the second television channel should be operated on commercial lines, albeit regulated by a public body with a statutory responsibility to impose public service requirements. Rather than run by a single network, it was to be organised as a series of separately owned regional franchises, each with a monopoly of television advertising in its own geographical area and collectively known as ITV. The Independent Television Authority (ITA) was inaugurated in July of the same year as the overarching regulatory body, charged amongst its other duties with choosing appropriate ITV contractors among competing bidders. It also decreed that the news should be provided by a separate organisation, Independent Television News, underwritten by the successful ITV contractors. ITV launched in the London area through the contractor Associated-Rediffusion

[41] For the first 3 months, this system alternated with the 240-line John Logie Baird system until it was agreed that the Marconi system afforded better quality reception.

on 22 September 1955[42]. ITV then extended gradually to the Midlands, North and Central Scotland franchises in 1957, Wales, the West and Southern franchises in 1958, the North East and Ulster in 1959. The network was not complete until 1962.

141. By the end of 1958, the number of television households exceeded the number of radio-only households, rising to over 10 million by the end of the 1950s. During the first years of the ITV franchises, as the medium took time to work its way into people's lives and advertisers needed to be wooed away from the familiar territory of newspapers, commercial television struggled to make money. By the beginning of the 1960s, however, on the back of popular shows such as *The Adventures of Robin Hood, Coronation Street, Double Your Money* and *Take Your Pick*—as well as a liberal smattering of American imports such as *Bonanza*, *Rawhide* and *I Love Lucy*—the tide turned and ITV companies' monopoly of television advertising made them exceptionally profitable. Roy Thomson, later Lord Thomson of Fleet and owner of Scottish Television from its inception in 1957, famously described his franchise as "a licence to print money".

142. In 1962, the Pilkington Committee on Broadcasting produced its report, which was critical of the quality of ITV programming, and recommended greater regulatory scrutiny by the ITA. It also recommended that the third television channel should go to the BBC; that the technical standard should move from 405 to 625 lines; and that colour transmission should be expedited. The same year saw the first historic transatlantic satellite transmission, broadcast live via the Telstar satellite. BBC2 went on air in April 1964, and started transmission in colour three years later. A colour television licence was introduced for the first time in 1968[43]. The following year saw a colour service inaugurated on both ITV and BBC1.

143. By the end of the 1960s, television licences had increased from 9 million in 1959 to 16 million and television was being blamed for plummeting cinema audiences: admissions had fallen from 600 to 200 million over the same period, while the number of cinemas had declined from 3,414 to 1,558.[44] The public service philosophy which had become ingrained within the BBC seemed to be mirrored by ITV, which during the course of the 1970s easily matched the BBC's output of original drama, documentary, arts, current affairs and children's programmes.[45]

144. The radio-only licence was abolished in 1971, and the inexorable rise of the television medium was consolidated during the 1970s, a period of unusual stability where the only significant change was a change in the regulator's name as the ITA was rechristened the Independent Broadcasting Authority (to accommodate commercial radio) and technology advances saw the introduction of video cassette recorders in 1974. By the end of the 1970s, the number of colour television licences outnumbered black-and-white.

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42 The BBC responded with the first example of competitive scheduling by killing off Grace Archer in its hugely popular radio series *The Archers*.

43 The same year saw some significant changes in ITV franchises, with London Weekend Television replacing ATV for the London weekend franchise and Thames created by a forced merger of ABC and Rediffusion London for the weekday franchise. Yorkshire TV was given a new franchise out of part of the Granada area, Harlech replaced TWW, ATV took over the all-week Midland franchise and Granada the all-week North-West franchise.

44 Figures from the British Film Institute

45 Appendix seven lists popular British television programmes by decade from the 1950s onwards

Channel 4 and the beginnings of cable and satellite

145. There was a further round of ITV franchise changes in 1982, determined by the IBA on the basis of programme track record and commitments for the future[46]. A more profound change to the television ecology took place in the same year, with the start of Channel 4. The Annan Committee, set up in the 1970s to examine options for a fourth channel, had rejected ITV's calls for a second channel and recommended a wholly new approach to the funding and structure of television. The result was Channel 4, set up as a non-profitable body under the auspices of the IBA, with three very distinctive features.

146. First, rather than a vertically integrated broadcaster which produced programmes in-house, it was created as a publisher-broadcaster with a team of commissioning editors who would commission programmes from outside. Second, although funded commercially through the sale of airtime in the same way as ITV, its advertising sales were conducted by ITV and the revenue then returned to Channel 4. It therefore did not compete directly with ITV for commercial revenue, maintaining ITV's monopoly of television advertising which was felt to have underpinned the quantity and quality of its home-grown content. Third, it was obliged by statute to be innovative and to cater for tastes and interests not generally found on other channels. Experimentation and minority programming were therefore written into the DNA of Channel 4 from its inception, an explicit extension of the public service ethos which still governed British television.

147. Breakfast television started in 1983 on both BBC and ITV (TVam winning the breakfast franchise) and Thames was the first channel to start 24 hour broadcasting in 1987. The 1980s ended with a four-channel all-day schedule on terrestrial television, run on public service lines, which for the vast majority of the audience comprised their total viewing experience. The 1980s also saw the first attempts at cable and satellite delivery systems which were to spawn a plethora of channels over the next 20 years. Europe's first satellite channel, later known as Sky, was launched in 1982. It could be received via the cable systems which were gradually emerging in urban areas after franchises had been awarded by the new Cable Authority (created in 1985).

148. It was, however, advances in direct-to-home satellite broadcasting which were to have a greater impact. In 1986, the domestic franchise for a three-channel domestic satellite service was awarded by the IBA to British Satellite Broadcasting (BSB) which planned to launch its satellite dish-received service in late 1989. It was, however, pre-empted by the Rupert Murdoch-owned Sky four-channel system which launched its service in February 1989. In the event, planning issues and technical problems delayed the launch until April 1990.

The 1990s—a radical shift

149. Two days in November 1990 fundamentally reshaped British television. On 1 November the Broadcasting Act 1990, which aimed significantly to deregulate British television, received royal assent. ITV licences—now to be known as Channel 3 licences—were to be decided by auction rather than subjective "beauty parades", subject to passing a quality threshold. Channel

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46 ATV, Southern and Westward were replaced respectively by Central in the Midlands, TVS in the South and TSW in the South-West.

4 was to be separated from ITV as a stand-alone (though still non-profit) organisation competing with other commercial channels for advertising revenue. The IBA was split into an Independent Television Commission (ITC) and Radio Authority, both with significantly reduced powers over programme output. And all public service broadcasters were now obliged by law to commission a minimum 25 per cent of their non-news programmes from independent producers.

150. The following day, in the wake of substantial losses by both operations, the two satellite companies which had been fighting a bitter war of attrition announced a "merger"—essentially a takeover in which the new operation, British Sky Broadcasting (BSkyB) was controlled and run by Sky. In 1992 BSkyB, despite still being very much a minority broadcaster, acquired the rights to exclusive live coverage of football's newly formed Premier League, a landmark deal which formed the basis of a lucrative subscription service centred around exclusive sports television contracts.

151. Those Channel 3 franchises which had prospered in the new auction process started broadcasting in January 1993[47]. This was followed rapidly by the first wave of consolidations within the ITV system in the wake of relaxations in the 1990 Act and in anticipation of further deregulation, which came in the Broadcasting Act 1996. By 1997, the original 15 franchises had effectively been whittled down to five major companies: Carlton, Granada, United News and Media (owners of Meridian, Anglia and HTV), Ulster Television (UTV) and Scottish Media Group (STV and Grampian). In 2000, Granada took control of the former UNM franchises, leaving Carlton and Granada as the two "big beasts" of ITV in advance of further ownership deregulation in 2003.

152. The Broadcasting Act 1996 also laid the groundwork for digital terrestrial television (DTT), which provided the possibility of multi-channel and interactive television via a terrestrial network Digital "multiplexes" for commercial DTT were awarded by the ITC to the consortium most likely to make the enterprise succeed. The winning group, British Digital Broadcasting, was owned primarily by the two major ITV groups Granada and Carlton, and was renamed ONdigital before launching in 1998. Designed as a subscription service, which required customers to buy set-top boxes to convert digital signals for analogue sets, ONdigital struggled with poor programming, unreliable signals, and a powerful subscription competitor in BSkyB. Despite giving away set-top boxes and being relaunched as ITV Digital in 2001, the enterprise collapsed under the weight of huge debts in 2002.

153. While attempts were being made to kick-start DTT, the final piece of the analogue puzzle was completed in 1997 with the launch of Channel Five as a for profit company (subsequently rebranded as Five). It was initially available to around 70 per cent of television households. Five is now owned by the German conglomerate Bertelsmann.

154. All the public service channels—the BBC and Channel 3 (ITV), Channel 4 and Five—received public support in return for undertaking certain programming commitments, including UK origination quota requirements set by the regulator. For the commercial PSBs, support included free or

[47] Carlton replaced Thames, Westcountry replaced TSW, Meridian replaced TVS and TVam lost out to GMTV for the breakfast franchise.

cheap access to the limited analogue spectrum which reached the great majority of UK households. In addition they benefited from free access to digital capacity as well as prominence on Electronic Programme Guides.

The 2000s—an era of competition, proliferation and new technology

155. With the DTT franchise now vacated, the ITC awarded it in 2002 to a new BBC-led consortium committed to free-to-air broadcasting and subsidised set-top boxes offering 28 channels. Branded as "Freeview", the new service sought to establish itself without monthly payments rather than compete with Sky's subscription model.

156. The Communications Act 2003 continued the deregulatory trend of its predecessor, relaxing content obligations on commercial PSBs and clearing the way for a further consolidation of ITV. This was completed in 2004 when Granada and Carlton merged to become ITV plc, subject to restrictions on the sale of advertising airtime in light of OFT and Competition Commission concerns about its dominance of the television advertising market. The remaining Channel 3 licences, not part of ITV plc are owned by the Scottish Television Group (central and northern Scotland); Ulster Television (Northern Ireland); and the Channel Islands Group (Channel Islands).

157. The Communications Act also heralded the biggest shake-up in broadcasting and telecoms regulation for years as five separate regulators, including the ITC, were brought together to create the Office of Communications (Ofcom) in anticipation of greater technological convergence between screen, print, telephone and computer. The regulation of commercial television passed to Ofcom in December 2003.

158. In September 2005, the government announced a definitive region-by-region rolling programme of switchover from analogue to digital terrestrial television, beginning in 2008 and culminating in London in 2012. The first analogue signals were switched off permanently in Whitehaven, Cumbria in October 2007.

159. Meanwhile, consolidation of media ownership continued. In November 2006, BSkyB acquired a 17.9 per cent stake in ITV to become its largest single shareholder. Following an investigation and ruling by the Competition Commission, the satellite company was ordered to reduce its shareholding to 7.5 per cent, but in 2009 obtained permission from the Court of Appeal to take the matter to the High Court. Its appeal is still pending. In February 2007, the cable company NTL rebranded itself as Virgin Media following Virgin's significant investment in the company.

160. At the same time as ownership trends were shifting in commercial television, satellite and cable, technology was transforming the viewing experience. The 2000s saw VCRs become progressively obsolete as first DVDs and more recently recordable hard drives allowed easier time shifting and non-linear viewing. The Sky+, V+ (for Virgin), Freeview+ BT Vision boxes all now permit consumer-friendly recording as well as, increasingly, catch-up television on all channels. Accessibility of television via live streaming and catch-up programmes on the computer have also brought the convergence of televisions and computers closer, although the vast majority of television viewing remains television-centred.

The importance of the television industry

161. According to the latest ONS data[48], there are around 80,000 jobs in the television industry: in broadcast television, cable and satellite and the independent production sector. This amounts to just over a tenth of the entire workforce in the creative media. The television industry comprises over 1,450 businesses, which are broadly divided up into the following three sub-sectors (p 266):

   (a) 10 (terrestrial) broadcast television companies

   (b) Around 250 cable and satellite broadcasters

   (c) Around 1,100 independent production companies.

162. The industry comprises a small number of large businesses and a large number of small companies. However, there is an increasing trend for the smaller independent production companies merging with others or being bought out to form much larger companies.

163. According to an Ofcom survey[49], British viewers appreciate programmes that reflect UK cultures, values and identities. Over four-fifths of people think it is important for the main television channels to provide programmes that are made in the UK and reflect life in the UK. The importance of locally produced drama was emphasised to us by Peter Grant, an expert in trade law and international cultural policy, who said, "… people appreciate having their own stories told and their own experience reflected on the small screen. So there is a real demand for local programming, whether it is drama or the other categories" (Q 427).

164. In addition, British television companies like the BBC, ITV and Channel 4, also make a significant contribution to our export economy. In 2008, the total revenue from the international sale of UK television programmes and associated activities was £980m[50], which is a 25 per cent increase on 2007. In that year, BBC Worldwide's overseas revenues amounted to around £430m and ITV's overseas revenues around £150m. The industry's main customer abroad is the US, accounting for over a third of total export revenue in 2008. Both UK television programmes and programme formats prove popular with other countries. Examples of popular television programmes include ITV's *Midsomer Murders;* Channel 4's *Ramsay's Kitchen Nightmares;* and the BBC's *Doctor Who.* Examples of popular formats include shows such as the BBC's *Strictly Come Dancing* and ITV's *Who Wants to be a Millionaire?*[51]

Regulations governing UK content on television

165. The BBC was set up by Royal Charter and Channel 4 by Act of Parliament. UK Legislation applies special regulatory provisions to each of the 'Public Service Broadcasters'. The three commercially funded channels are regulated in respect of these statutory requirements by Ofcom while the BBC is regulated both by the BBC Trust and, in certain areas, by Ofcom. Non-PSB

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48 ONS Annual Business Inquiry, November 2009

49 Ofcom PSB Review phase 1 annex 5, quantitative survey 2007

50 PACT Annual TV exports survey. Associated activities include DVD/Video sales, formats and licencing.

51 According to Chris Bonney, Managing Director of Outright Distribution, as cited in the Guardian article, 'British TV exports defy recession', 27 November 2009

television channels broadcast from the UK are also subject to regulation by Ofcom, but to a much lesser extent than the PSBs.

166. All television channels licensed by Ofcom are subject to a range of licensing obligations and conditions, grounded in statute and enforced by Ofcom. Television businesses in the UK are also subject to UK Competition Law which is administered by Ofcom and the Competition Commission. In the case of competition issues with an EU dimension the European Commission can become involved.

167. All channels licensed by Ofcom (like all other channels licensed by any EU Member State) are subject to the provisions of the EU Audiovisual Media Services (AVMS) Directive, which has been transposed into UK Law[52]. The European Union has developed strict rules relating to the permissibility of State Aids, which are widely defined and include support in kind as well as cash—for example, free use of spectrum. The European Commission can and does intervene if it identifies what it considers abuse. Television content is also subject to EU regulations. The AVMS Directive[53] provides that each channel must, where practicable, show a majority of European programmes. Ofcom requires broadcasting licensees to report annually on the proportion of European content included in their transmissions and, if this is less than a majority, to explain why it is not practical to achieve this. This information is then submitted by the Department of Media, Culture and Sport to the European Commission on a bi-annual basis (p 505).

Quotas and the Communications Act 2003

168. All television channels licensed by Ofcom—and in some respects BBC channels too—are subject to a range of regulatory requirements set down by the Communications Act 2003. These are generally recognised as dividing into three levels or "tiers" of regulation:

- Tier 1 sets standards for matters such as harm, offence and political impartiality. These standards apply to all broadcasters including the BBC (although accuracy and impartiality are a matter for the BBC Trust);
- Tier 2 applies only to licensed public service broadcasters. As well as implementing the 25 per cent independent production quota, it requires Ofcom to set quotas for original UK production for each public service channel. It also requires Ofcom to set down minimum requirements for news and current affairs programmes on these channels.
- Tier 3 also applicable only to licensed public service broadcasters, relates to other areas of public service programming where Ofcom can offer guidance but not set quotas.

52 AVMS replaced the Television Without Frontiers (TWF) Directive on 10 December 2007 and was transposed into UK legislation on 10 November 2009

53 The Directive says that television broadcasters shall ensure that, where practicable, and subject to paragraphs 2 and 3:
a) a majority of their Transmission Time is devoted to European programming;
b) at least 10% of their Transmission Time or programming budget is devoted to European programming created by producers who are independent of broadcasters; and
c) at least 50% of programming included in their Transmission Time in accordance with (b) above is created no less than five years earlier by producers who are independent of broadcasters.

169. Original productions are programmes made in the UK and can come from two sources: either commissioned from independent producers, or a broadcaster's own in-house production facilities. The table below shows the quotas currently set by Ofcom for each channel both in peak-time and for the whole day. It demonstrates that all channels comfortably exceeded their original production quotas in 2008. The table covers all UK content, though not necessarily first-run productions since it includes repeats.

TABLE 1

Original production quotas and performance by public service channel 2008

	Quota all day % hours	Achieved all day % hours	Quota peak time % hours	Achieved peak time % hours
BBC 1	70	86	90	99
BBC 2	70	82	80	95
ITV1	65	87	85	96
Channel 4	60	62	70	76
Five	53	59	42	49

Source: Ofcom Communications Market Report 2009

170. Evidence we received suggested the PSB channels broadcast considerably more UK-originated content at peak time than they did 30 years ago. Andy Duncan, outgoing Chief Executive of Channel 4, told us, "One of the rather good things in the UK is that if you look at eight o'clock or nine o'clock in the schedules, typically it is British drama and British programming that dominates the schedules" (Q 2210). This represents a sea-change in the schedules of the 1970s when American imported drama featured heavily in the peak-time schedule. Michael Grade, Executive Director, ITV, said "… if you go back to the so-called golden age of broadcasting, pre-digital, pre-Sky, the BBC1 schedules, the ITV1 schedules, were packed with American material. *Hawaii Five-0*, *Kojak*, *Starsky and Hutch*, *Six Million Dollar Man*, *Dynasty*, *Dallas*, et cetera— … You do not see them on the main channels today, because *Doc Martin*, *Benidorm*, *The Fixer*, *The Bill*—these are programmes that are more popular than American material" (Q 1824).

171. While this dominance of prime-time schedules by UK-produced programmes is to be welcomed, it is the overall level of new original programming that concerns us and which we address below.

UK content

172. Despite two decades of multi-channel broadcasting, the vast majority of UK originated content, (other than in sport), is produced or commissioned by the public service broadcasters. In 2007 (the most recent year for which figures are available), PSBs represented over 90 per cent of all spend on original UK television programming, with cable and satellite channels accounting for the remaining 10 per cent[54].

54 Ofcom Communications Market Report, 2009, p.89

Cable and satellite channels' contribution to UK content

173. The Satellite and Cable Broadcasters' Group (SCBG), who represent the largest satellite and cable channels in the UK (Q 1566), told us that the SCBG members contributed £193m to UK-originated content in 2007 (Q 1581). This contrasts with PSB channels who contributed £2.6bn in UK-originated content in the same year. However, this figure does not include the expenditure of cable and satellite channels on sports programming or the acquisition of sports rights, and the contribution that this makes to sport in the UK.

174. BSkyB is one of the largest providers of satellite television in the UK, with 9.4 million subscribers (Q 1924) and revenue of over £5bn (Q 1919). David Wheeldon, Director of Public Affairs, BSkyB, told us that "we are investing considerably in UK content and that is growing" (Q 1998). However, this is difficult to check. BSkyB is not willing to provide us with detailed figures on its investment in UK content. The Committee is therefore unable to judge BSkyB's claim that their investment in UK content is increasing significantly. We greatly regret the refusal of BSkyB to provide this information. Christine Payne, General Secretary of Equity (the trade union representing performing artists), said that BSkyB's contribution to UK-originated drama is "very, very little, and this is of great concern to us, because as the television landscape is changing, then these channels seem to be taking all the advantages of the work that our members have done, but contributing very little back to it" (Q 254). We note that a recent Culture, Media and Sport Select Committee report[55] also recorded reluctance by the cable and satellite industry to provide figures: "Although the Satellite and Cable Broadcasters' Group originally agreed to provide us with its own estimate of the multi-channel sector's investment in UK-produced children's programming, we note that it has since declined to do so on grounds of commercial confidentiality. We find this failure … very disappointing"

175. There are several types of programming where purely commercial players are unlikely to invest significantly in UK content for television or other platforms, because returns are too low and the commercial risk is too great. Without the PSBs, the UK production of certain programme genres would be likely to decline, which would be a loss for UK audiences, for employment in the industry and for the economy as a whole. Ofcom has identified the programme genres most at risk as children's programmes; regional news; documentaries; drama; and comedy.

The pressures on Public Service Broadcasters

176. Given the important role of PSBs in producing and commissioning UK-originated content, it is of concern that the total value of expenditure on UK-originated output by the five main PSB channels has decreased by £500m in five years, from £3.1 bn in 2004 to £2.6 bn in 2008[56], a fall in real terms of around 15 per cent. The five main PSB channels broadcast 33,177 hours of first-run UK originated programming in 2008, down by 3 per cent (1,099 hours) since 2004[57].

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55 Culture, Media and Sport Committee, First Report (2007–08): Public service content (HC 36)

56 Ofcom Public Service Broadcasting Annual Report 2009, p.33

57 Ibid p.34

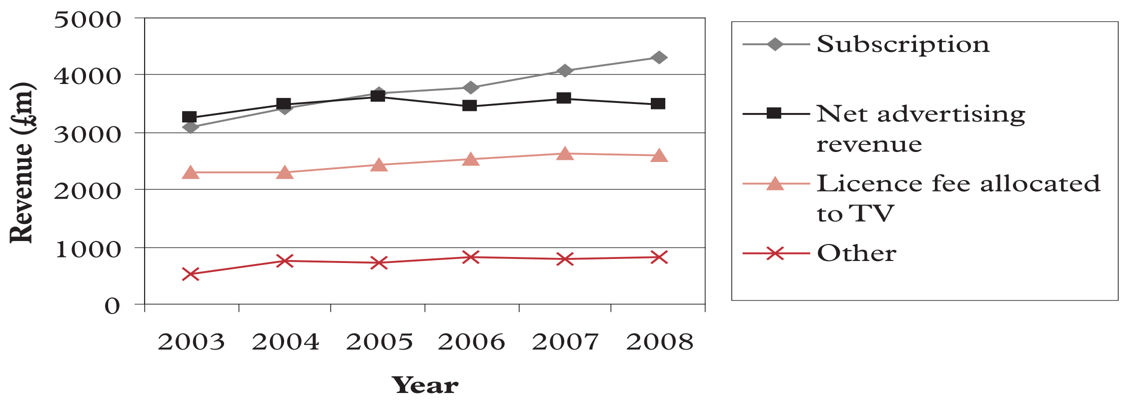
177. Financial pressures on the commercial PSBs, and uncertainties over the future of channels 3, 4 and 5, mean that their commitment to PSB content is now at considerable risk. As outlined in two previous reports by this Committee[58], the PSBs are subject to the following changes in the market:

(a) First, the move from analogue to digital broadcasting. In the analogue broadcasting market, the commercial PSBs benefited from access to limited analogue spectrum—an implied subsidy in return for which the companies undertook certain public service obligations.

(b) Second, falling advertising revenues and fragmenting audiences. A significant proportion of advertising revenue is migrating from television to the internet—in the UK, Google's advertising revenues are greater than ITV1's. The speed and severity of the current economic recession has intensified the fall in advertising revenues[59]. In addition, a system of just two commercial channels and little competition has been transformed into hundreds of competing channels and fragmenting audiences. These challenges exacerbate the tension between a commercially owned public service broadcaster's incentives to maintain a profitable business model and investing in high quality public service content.

FIGURE 5

Total TV industry revenue by source



Source: Ofcom Communications Market Report 2009

178. Whilst the BBC has greater security of funding through the licence fee, they too faced pressures to deliver value for money for audiences, and meet demands for fresh programmes. The BBC has devised an efficiency programme, which started in April 2008, with a target to achieve 3 per cent cumulative savings of £1.9 bn[60]. Mark Thompson, Director-General, BBC said, "… what we are trying to do is to track, to benchmark quality, so you make sure you are maintaining or increasing the public perception of quality while delivering these efficiencies. So far across the piece, that seems to be going well and the public scores we are getting for quality are slightly up over

58 House of Lords Communications Committee—First Report (2007–08): The Ownership of the News (HL 122); and Second Report (2008–09) Public Service Broadcasting (HL 61)

59 Net advertising revenue for ITV1, GMTV1, Channel 4 and Five decreased 8 per cent year on year to £2.1bn (source: Ofcom Communications Market Report, 2009)

60 BBC annual report and accounts, 2008/09. July 2009

this period even though we have already taken 15/20 per cent out of the budgets" (Q 2055).

179. Channel 4's funding problems were addressed in our report on Public Service Broadcasting[61]. These still have not been resolved. Glyn Isherwood, Group Finance Controller, Channel 4, told us "The total programme budget for 2009 is about £530 million, which is £100 million less than the previous year, so there is substantial pressure on that programme budget" (Q 2162), and this is the lowest level since 2002. So, whilst we welcome the wider remit for Channel 4, especially in relation to UK content, which was proposed in the Digital Economy Bill[62] (November 2009), it is still not clear where the funding will come from, to implement this wider remit.

180. The current difficulties of commercial PSBs contrast with the subscription based channels, such as BSkyB, where revenues have risen between 2003 and 2008. These channels have also seen a fall in advertising revenues but have a solid base in subscriptions, as shown by BSkyB whose subscriptions make up almost 80 per cent of their total revenue (Q 1919). These channels generated revenues of £4.3 billion in 2008, a six per cent increase on 2007[63].

Consequences

181. The pressures faced by the PSBs have an adverse impact on UK content both from an economic and quality point of view. Andy Duncan, Chief Executive of Channel 4 said "One of the worries I have for the British system as a whole is the engine of content investment has historically come from the licence fee and from the TV advertising income that ITV, Channel 4 and to a lesser extent Five … have earned, where the majority of that money has been reinvested back into content, and in Channel 4's case all of it has been reinvested back into content. The model that is now growing up is one where if you are a digital channel business you buy other people's used content to repeat and/or you acquire from the States ... The level of content investment in Britain is a worry whether you are looking at it from a cultural/social public value perspective or from a creative economy hardnosed business perspective. On both fronts it is a worry" (Q 2209).

182. An integral part of the public service ethos in the UK has been a recognition that home-grown content and innovation are important ingredients of our television culture. In addition, certain programme genres, which have been identified as being central to public service purposes, have experienced falls in spending. Ofcom's figures show that in the five years leading up to 2008, spending on children's programmes has fallen by 48 per cent; news and current affairs by 14 per cent; factual programmes by four per cent; comedy by nine per cent; and drama by three per cent.

183. The two genres—children's programming; and regional news and current affairs—which have seen the steepest falls in expenditure, are also the areas of UK-generated content that Ofcom believe need to be safeguarded. This was explained by Peter Phillips, Partner for Strategy and Market Developments, Ofcom. He said "What we said in the Public Service

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61 House of Lords Communications Committee—Public Service Broadcasting: Short-Term Crisis,. Long-Term Future? (HL 61). Session 2008–09

62 Clauses 21 and 22

63 Ofcom Communications Market Report, 2009, p.82.

Broadcasting Review was that we felt that news programming should be the highest priority given the feedback that we had from audiences about what mattered to them. The next set of priorities that we set out in addition to that were around children's programming, where we have seen very significant changes in the amount of UK-originated children's programming, particularly for older, school age children, and particularly in the areas of drama and factual programming for those children" (Q 2249).

Children's programmes

184. In the five years leading up to 2008, the volume of first-run originated children's programming fell from 1,887 hours per annum to 919 hours[64]. Reasons include re-focused PSB requirements, increased commercial pressures, greater restrictions on advertising in and around children's programming and significant changes in children's consumption of media[65].

185. Ofcom told us that the reduction in the volume of first-run originated children's programming is particularly acute for "older, school age children, and particularly in the areas of drama and factual programming" (Q 2249). The Digital Economy Bill (clause 21) has placed a requirement on Channel 4 to make "relevant media content that appeals to the tastes and interests of older children and young adults". Andy Duncan, told us that Channel 4 "would be very happy and willing to take on additional responsibilities towards the older children's group in particular" (Q 2189)

186. Cuts in funding of children's programming are also affecting UK-originated programmes for younger children. Anne Wood, Creative Director, Ragdoll Productions, said the "Director General of the BBC has cut the children's budget—and many others—to the bone in the interests of saving money. If you have no investment, you have no creative risk taking … It comes down to the funding every single time" (Q 688). Anna Home, Chair, Save Kids' TV argued that "children today see a huge amount of the world, particularly of the American world, and relatively little of their own". She pointed to drama "where children see themselves reflected, their own lives reflected, in a context which they comprehend", which she said was "hugely important, both for their education and for their cultural development as citizens" (Q 1489).

187. The reduction of both output and expenditure in children's programming could have serious consequences, according to Ofcom. In December 2009, Colette Bowe, Chair of Ofcom, told a House of Commons Committee[66] "we are sleepwalking into a situation where we do not have UK-generated content of a high quality for our kids. I believe that would be a very bad outcome".

Regional news

188. News and current affairs shows the second steepest fall in PSB expenditure in the five years to 2008[67]. The BBC is continuing its regional news service,

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64 Ofcom PSB annual report 2009, p.145

65 Digital Britain, 2009, p.147 (box)

66 Joint Culture, Media and Sport; and Business, innovation and Skills Select Committee evidence on Ofcom's 2009–10 Annual Plan, 1 December 2009

67 This includes national news; and local/regional news

though making efficiency savings in this area (Q 2055). In contrast, ITV is withdrawing from regional news. In its written evidence to us, ITV outlined that it currently invests around £55m per annum in regional news but earns insufficient return on that investment. It is aware that a high value is placed on regional news by many viewers, the Government and Ofcom, and believes that a publicly-funded model is the best option to guarantee a secure future for regional news on Channel 3. It supports proposals for an alternative model of regional news provision in which ITV provides the time slots while the service itself is provided by third party news organisations (p 403). The Government agrees and Digital Britain stated that "An early priority is for independently financed news consortia providing an independent stream of multi-media and broadcast news using Channel 3 Licensees' broadcast regional news slots as one means of distribution". Building on Digital Britain's proposal, clause 28 of the Digital Economy Bill (November 2009) includes provision for appointed providers of regional or local news[68], enabling third party organisations to provide news on Channel 3 (ITV).

Documentaries and drama

189. Other programme genres are also under pressure. Roger Graef, documentary maker and CEO, Films of Record, told us that new technology has resulted in financial pressures on makers of factual programmes, "there is the economic reductionist pressure of very tight budgets: because technology allows you to shoot and edit quicker, the accountants who look at the budgets say in that case we must shorten the budget and shorten the schedule. In my experience with documentaries, especially open-ended ones which are not scripted in advance, very often the best things happen on the very last day … That flexibility—the investment and the open-ended process—has really eroded big time" (Q 688).

190. On expenditure on drama, Michael Grade confirmed that current economic conditions had caused ITV to reduce its original drama output from eight to seven hours a week (Q 1838). But there is a more fundamental threat to television drama production from the United States. American imports such as *West Wing* and *The Wire* offer high quality competition. Because US producers are able to recoup their costs from their large domestic market, they can be highly price competitive in overseas markets. Peter Grant told us that the US is "able to sell [televised drama] in other countries at prices that make it almost impossible for other countries to compete in the high value, audiovisual sector without government support" (Q 424). The UK is particularly vulnerable to this competition, compared to other European countries, because of the lack of a language barrier.

The independent sector's contribution to UK content

191. The uncertain future of the PSBs means an uncertain future for another part of the UK television industry: the independent production sector.

192. According to PACT (p 10), the independent sector (comprising production companies that are external to broadcasters) plays an increasingly important

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68 Clause 28, subsection (1) states that "OFCOM may (a) appoint a person to provide relevant media content consisting of regional news or local news (or both) for all or part of a designated Channel 3 area, and (b) pay amounts to the appointed person for use in, or in connection with, the provision of such content.

role in creating UK content. The independent sector has an annual turnover of more than £2 billion, creates around half of all UK television programmes each year across the BBC, ITV1, Channel 4 and Five and provides 21,000 jobs.

193. Historically, the independent production sector has delivered high levels of UK content for the PSBs (p 80). The creation of Channel 4 as a publisher-broadcaster and the formal introduction, through the Broadcasting Act 1990, of a statutory 25 per cent independent quota were the key drivers in opening up a market that previously relied on in-house production at the BBC and ITV.

194. Following an assessment by the Independent Television Commission (ITC) of the independent production sector in 2002, the ITC recommended a radical shift in the relationship between broadcasters (as programme commissioners) and independent producers. Broadcasters were in a strong negotiating position because there was little interest in commissioning from the multichannel sector. The ITC concluded that intervention was required to promote growth in the independent sector.

195. The ITC, and subsequently Ofcom, developed Terms of Trade/Codes of Practice to help independent producers to negotiate a fair deal in the primary rights package, establishing a balance in the relationship between the parties. These terms of trade relate to how rights should be sold and priced. Primary rights are a matter of negotiation between broadcaster and independent producer, subject to Ofcom's approval. The terms of trade introduced in the Communications Act 2003 enabled independent TV producers to retain control of a share of intellectual property rights when they create programmes for broadcasters. The major broadcasters told us that the Terms of Trade put them at a commercial disadvantage. Michael Grade said, "It is a nonsense that there are regulated terms of trade between two commercial organisations. If you are an independent producer, you have plenty of places you can sell your wares to" (Q 1867).

The BBC and the independents

196. As noted, the BBC must commission at least 25 per cent of its qualifying television programme hours from independent producers. However, as noted by the House of Lords Select Committee on the BBC Charter Review in 2005, the BBC did not always succeed in meeting this obligation, and saw it both as a ceiling as well as a floor. Many witnesses who gave evidence to the Committee felt that "an increase in independent commissioning at the BBC would benefit the industry and the quality of programming" (paragraph 225).

197. Following the 2005 Green Paper[69], the BBC, with a view to increasing independent production, put forward a plan to introduce the Window of Creative Competition (WOCC), which identified a further 25 per cent of BBC commissions over and above the 25 per cent minimum quota for which all producers, both in-house and external, can compete.

198. The WOCC began operating in 2007 and has, to date, been successful. According to the BBC[70], in the financial year 2008/9, independent

69 Review of the BBC's Royal Charter: A strong BBC, independent of government

70 http://www.bbc.co.uk/pressoffice/pressreleases/stories/2009/05_may/07/wocc.shtml

production companies won three-quarters and in-house won a quarter of network programme hours available within it. The BBC Trust reviews the operation of the WOCC, and other commissioning arrangements as set out in the BBC Agreement, at least every two years. The BBC Trust said, in a review conducted on the BBC Trust's behalf by PriceWaterhouseCoopers in 2008[71], concluded that "commissioners had clear incentives to pick the best ideas and PwC found no obvious bias towards accepting in-house ideas over independent ones or vice versa".

Conclusions

199. From its inception, British television was governed by a public service ethos which was applied as much to the commercially funded sector as to the publicly funded BBC. For the first 45 years of post-war television, change was incremental and as recently as the early 1990s a four-channel terrestrial service provided the vast majority of television consumption.

200. From the beginning of commercial television, a clear separation of revenue streams (between the licence fee-funded BBC and advertising-funded ITV and Channel 4) provided stability of programme funding, and substantial returns for ITV companies in return for their regional advertising monopolies. However, the major legislative changes of the 1990 Broadcasting Act coupled with the arrival of cable and satellite channels and a fifth terrestrial channel signalled a profound shift in the television market-place in the 1990s, when the "licence to print money" gave way to significant competition for viewers and commercial revenue. The arrival of pay channels, in particular, heralded a new source of television revenue through subscription.

201. The last ten years have seen two major technologically driven changes. First, the shift from analogue to digital transmission in terrestrial, cable and satellite television has spawned a proliferation of channels, both advertising and subscription based. Revenue from subscription channels now exceeds that from both public funding (the licence fee) and advertising. Second, a new generation of hard drive recorders along with catch-up TV (such as the BBC iPlayer) and online viewing through computers provide a number of different approaches to television consumption.

202. The television industry today plays a vital role in the UK economy, providing around 80,000 jobs and contributing about £1 billion to the export economy. In addition to a small number of large terrestrial broadcasters, the industry comprises a large number of small independent production companies which have injected considerable creative and economic dynamism.

203. Television also plays an important cultural role in the life of the nation, and overall levels of TV viewing have remained remarkably consistent, despite the upheavals of the last 20 years, at around 25 hours per week. Both opinion research and viewing figures demonstrate that British audiences place particular value on UK-originated programmes. In recognition of both the economic and cultural importance of original UK content, British legislation has consistently empowered regulatory bodies to set minimum quotas on the

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71 The Operation of the WOCC—First Biennial Review by the BBC Trust, July 2008

levels of UK programming which the PSBs are expected to transmit. For the most part, these have been comfortably exceeded.

204. The exponential growth in the number of channels and the substantial revenues now being earned through subscription and pay per view have not been matched by a proportionate increase in the volume of UK-originated content. Over 90 per cent of UK-originated content on television is therefore still produced by the public service broadcasters—notably the BBC, ITV and Channel 4.

205. Until now, the commercial PSBs have received financial support from their use of the limited analogue spectrum. With completion of the digital switchover programme in 2012, this implied subsidy will disappear. At the same time, an unprecedented cyclical decline in advertising revenue because of the economic downturn has been exacerbated both by fragmenting audiences and by a structural shift of some TV advertising revenue to online.

206. One consequence has been a dramatic fall in overall spending by the PSBs on UK-originated programming, down by around 15 per cent in real terms from £3.1 billion in 2004 to £2.6 billion in 2008. There is a consensus in the industry that this rapid decline is set to fall further if remedial action is not taken.

207. There is a particular risk that the commercial PSBs will be driven towards acquiring more programmes from abroad (especially from the US), which are generally cheaper than equivalent hours of UK-originated output. If unchecked, a continuing reduction in investment in UK television content could have damaging consequences for the economy, for jobs, and for British culture.

CHAPTER 4: PROMOTING BRITISH TELEVISION

208. In this chapter we consider proposals to promote British television. We give particular attention to proposals aimed at supporting UK content and reversing the decline in investment over the last five years. One route to reducing or reversing this trend would be to find alternative sources of funding for UK content. Possible sources include: use of the proceeds of the sale of spectrum; use of the digital switchover portion of the licence fee; and the use of other categories of fees. We outline the arguments that were presented for and against each one. But before considering those arguments, we consider a proposal that does not require legislation or government action but could result in better distribution of UK content, resulting in more money for production.

The future of BBC Worldwide

209. As discussed in Chapter 3, exporting British programmes, and developing media brands around the world brings money back into the country for reinvestment in UK production. This could and should grow further. If this were to happen, it would have a beneficial effect on British made programmes as well as employment in the industry.

210. The BBC, ITV and Channel 4 are all active exporters. By far the biggest British company operating in this area is BBC Worldwide, which in 2009, received the Queen's Award for Enterprise in International Trade.

211. BBC Worldwide is the main commercial arm, and a wholly owned subsidiary, of the BBC. Its mission is to create, acquire, develop and exploit media content and brands beyond the BBC around the world in order to maximise the value of the BBC's assets for the benefit of the UK licence payer. The company has an annual turnover of over £1bn, and profits of £150m. The profits made by BBC Worldwide go to the BBC, and the Corporation has a direct interest in ensuring that the maximum revenue is earned in this way.

212. BBC Worldwide incorporates a number of separate businesses, including DVD sales, licensing of BBC programmes and formats (and also those of UK independent producers'), television channels (such as BBC America) and magazine and book publishing. It jointly owns, with Virgin Media, several television channels, called UKTV. In 2007, BBC Worldwide acquired Lonely Planet, the travel information group, to build a Lonely Planet franchise around the world.

213. The BBC Trust outlined to us the important role that BBC Worldwide plays in supporting the independent production sector. They said "In addition to providing an effective distribution service to independents for their output, BBC Worldwide also offers a variety of ways in which independents can secure up-front investment. These include first-look and development deals and, more recently, "seed-funding" in the form of small equity stakes where this suits the companies concerned … Worldwide allows these smaller independents to gain international exposure which would otherwise not be open to them thanks to the reach BBC Worldwide TV channels provide to almost 300 million homes globally and its role as the largest exporter of TV programmes in Europe … Over the past four years, BBC Worldwide has

generated £200 million for independents from its commercial activities" (p 347).

214. BBC Worldwide could undoubtedly expand further. In an earlier report[72], this Committee drew attention to the scope for BBC Worldwide to become a vigorous and successful acquirer and exploiter of rights, both domestically and globally. This would enable it to generate greater revenue for the copyright holders, provide increased funding for investment in UK content and have a beneficial impact on employment. However, John Smith, Chief Executive of BBC Worldwide said, "All companies grow by a mixture of organic means and acquisition. Apart from a small number of acquisitions which have led us to the debt position we have, I think the feeling is we probably will not have much more, if any more, acquisitions in the future because we cannot take on significant amounts of additional debt. Our growth is limited to organic only" (Q 597). This was confirmed subsequently, when the BBC Trust announced new limits on acquisitions. Mr Smith went on to say that there was an exciting opportunity to grow that might be missed: "I think it is the only chance Britain has ever had and will ever get at having a global media company" (Q 598).

215. We agree that BBC Worldwide is Britain's only really global broadcasting distribution company and that its potential expansion has key implications for UK content. It would be capable of becoming a distributor of UK content on a much greater scale.

216. Digital Britain advocated greater financial and operational separation between the BBC and BBC Worldwide, "… which could include the sale of a part of BBC Worldwide"[73]. In December 2009, the Government announced[74] its desire for the BBC to consider selling off part or all of BBC Worldwide. It said, "The government now expects the BBC to look more widely at the options for greater financial and operational separation, including a sale or partial sale. Alternatives to sale or partial sale might also include other structures that would potentially enable the introduction of external capital, broadening ownership of the asset and yet retaining the link to the BBC."

217. To date, the BBC Trust's attitude has been either dismissive or lukewarm to the idea of a public private partnership. In response to the Government's announcement, a BBC Trust spokesman said "We note the Government's report. Worldwide is not up for sale. The recent commercial review did not set out to consider ownership, but to improve the operation of Worldwide within its current ownership structure. However, any business operates in a dynamic environment. We continue to keep an open mind about the appropriate ownership structure for Worldwide."[75] We do not believe that this recognises the business opportunity that has been presented.

218. We have discussed in this report how the film industry in the UK suffered by being unable to support a successful, sustainable, worldwide distribution company. BBC Worldwide has the potential to fulfil this role for the UK television industry, supporting independent production companies as well as

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72 House of Lords Communications Committee Report on Public Service Broadcasting: Short-Term Crisis, Long-Term Future? (HL 61) Session 2008–09

73 Paragraph 24, p.141

74 HM Government 'Operational Efficiency Programme: Asset Portfolio', 7 December 2009

75 Guardian article, 'Government urges BBC to consider Worldwide sell-off', 8 December 2009

broadcasters. But it is now limited in its activity, earnings and export potential, because of its exclusive ownership by the BBC. Inevitably there is a limit to the licence fee funds that can be applied for developing a commercial business. Private risk capital provides an escape from that straight-jacket; and gives opportunities for other PSBs, besides the BBC to take a stake. We see substantial advantage for the British television industry as a whole in such a step.

219. Despite the BBC Trust's apparent intention to prevent changes in BBC Worldwide ownership structure, we are convinced that the growth of BBC Worldwide through introduction of private capital will benefit UK content producers and UK exports.

220. **We support the Government's intention to sell a part of BBC Worldwide, creating a public private company. We believe that such a company, with a continuing link to the BBC, would be capable of becoming a major global brand for distributing UK content, producing additional profits, employment and opportunities for British production companies.**

221. We believe that the action advocated above for BBC Worldwide will have a beneficial effect, but further action is also necessary. We now review some of the actions that were put to us in the evidence provided to the Committee.

Tax credit for television content

222. In previous chapters, we saw how British films face competition from countries around the world from governments offering financial incentives to producers and how Britain has countered with a tax credit of its own, within WTO and EU rules. No such tax credit exists for television production in the UK, although some other countries do support domestic television production in this way.

223. Miles Bullough, Aardman Animations, explained the impact this has on UK television companies. He said that "colleagues in Canada, France, Belgium, Germany, Australia and Ireland all enjoy a level of tax credit or subsidy that can provide them with anything between 25 and 70 per cent of the budget of their productions. When we as a British producer set out to raise finance for one of our productions, be it *Wallace & Gromit* or *Shaun the Sheep*, we would be looking at getting a maximum of 20 or 25 per cent of the budget out of the UK and that would be from broadcast and up until recently DVD advances, so we start from a position whereby we can sell premium products to the world's leading broadcasters in the UK and still have only raised 25 per cent of the budget. Our Canadian colleagues can do the same and with the tax credits and various subsidies available to them they can raise nearly 70 per cent of the budget" (Q 1427).

224. Mr Bullough added that his business was being "challenged really quite dramatically by subsidised overseas competitors, and this is something that we would like to … see if the Government can help us address, and the tax credit system … we would like to see that extended to animation, especially for kids, which we fear is suffering particularly badly" (Q 1425).

225. We believe there is a strong case for extending the tax credit help to UK content made for television. As we saw in Chapter 3, a number of programming genres are under particular pressure. Among these are children's programmes, including animation. The tax credit could enable

support to be directed not only towards British production but also to particular kinds of production. It would then be possible to target help and to measure how effective that proved to be.

226. **We recommend the extension of the film tax credit, on a pilot basis, to children's programmes and animation productions made for television. This pilot, if successful, might be extended to other genres.**

Regional news

227. In our report on Public Service Broadcasting of April 2009[76], we drew particular attention to the problems facing regional news in the UK and the prospect that ITV would withdraw from regional news production. This was one part of the problems facing public service broadcasting generally. We recommended that "an element of contestable funding should be introduced to fill some of the gaps that might otherwise arise in public service broadcasting. This would entail the setting up of a limited fund, to which broadcasters and programme makers could apply."[77] We proposed that additional funding for public service broadcasting in the advertising-funded television sector should be provided first by the underspend on the digital switchover programme[78].

228. In his Second Reading speech on the Digital Economy Bill, in the House of Lords on 2 December 2009, the Secretary of State for Business, Innovation and Skills, Lord Mandelson, said "Market pressures and structural changes are putting pressure on commercially provided news in the nations, regionally and locally. Some element of public support is needed if this provision is to be preserved."[79] Accordingly, the Bill proposes that Ofcom should support independently funded news consortia to provide regional and local services. This is clearly in line with our recommendation.

229. **We welcome the provisions in the Digital Economy Bill on support for independently funded news consortia to provide regional and local services.**

230. But the use of the underspend on digital switchover will not support additional funding for public service broadcasting indefinitely. The scheme itself is due to come to an end in 2012. Something more will be needed and here there are two main options:-

Proceeds of the sale of spectrum

231. In our report on Public Service Broadcasting[80], we recommended that one way of providing funding for public service broadcasting would be through the use of at least part of the revenue the Government will make from the sale of analogue spectrum after 2012. Part of the receipts which would otherwise go totally to the Treasury could be used for public service broadcasting.

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76 Public Service Broadcasting: short-term crisis, long-term future? Second Report of Session 2008–09, HL Paper 61

77 Ibid, p 17

78 Ibid, p 18

79 House of Lords Official Report, Column 746, 2 December 2009

80 Public Service Broadcasting: short-term crisis, long-term future. Second Report of Session 2008–09, HL Paper 61

232. Ofcom has proposed the introduction in 2014 of a system of charging broadcasters' for the use of digital spectrum, called administered incentive pricing (AIP). AIP would involve charging broadcasters an annual fee that reflects the opportunity cost of holding spectrum. From 2014, Digital Terrestrial Television multiplex licensees, including the BBC, would be asked to pay this annual fee for their use of the spectrum[81], which they have previously been given free. However, as Ofcom has recognised, this represents a transfer of funds from the broadcasting sector to the Exchequer. Further reduction in revenue of broadcasters is likely to lead to a further reduction in potential investment in UK content.

233. A report commissioned by the BBC[82] suggested that Ofcom's existing plans for spectrum pricing for broadcasting could be adapted to deliver funding for UK content. The report proposed that, rather than being diverted from the broadcasting sector, this money could be channelled into a new Public Service Content Fund, which would support the provision of news and other public service content by providers other than the BBC. Funding could be allocated via a contestable process, which would be open to existing commercial broadcasters and to new players. Mark Thompson, Director-General of the BBC said that use of AIP for broadcasting use of spectrum "could, potentially, form the basis of a long-term flow of revenue", and that the use of the sale of spectrum "would not have some of the disadvantages which we believe are associated with top-slicing" (Q 2085).

234. The Secretary of State for Culture, Media and Sport, Ben Bradshaw, argued against the use of spectrum pricing for funding UK content. He said "I think there are a number of potential problems … One is that, if you accept that the whole point of a spectrum tax is to encourage efficient use of the spectrum, the consequence of that is that it raises less and less revenue as that spectrum is used more efficiently. The second problem is that it is a tax. It does not belong to us. It belongs to the Treasury" (Q 2339).

235. We do not believe that the Secretary of State's argument is conclusive. As we have pointed out, the process of spectrum allocation provided support for public service broadcasting. PSB broadcasters benefited from limited competition and from preferential placement on the Electronic Programming Guide. Making funding available from the sale of analogue spectrum would continue a longstanding policy of support.

Use of the BBC licence fee

236. A second possible source of funding is the BBC licence fee. This Committee recommended in April 2009[83] that "Consideration may ultimately need to be given to redirecting an element of the licence fee to support public service content provision outside of the BBC". Digital Britain kept the door open for this to happen. It said that the Government would "consult openly on the option of a Contained Contestable Element of the Television Licence Fee (primarily for news), carrying forward the current ring-fenced element for the Digital Switchover Help Scheme and Marketing (about 3.5 per cent of the

81 Ofcom: Future pricing of spectrum used for terrestrial broadcasting—A Statement, June 2007

82 Paying for Public Service Content—a role for spectrum pricing. A report by Human Capital for the BBC, September 2009

83 House of Lords Communications Committee report, Public service broadcasting: short-term crisis, long-term future? (HL 61) Session 2008–09

Licence Fee) after 2013. This would be independent of the level at which the Licence Fee would be set from 2013" (p 19).

237. Ben Bradshaw told us that, one of the reasons that the Government left open the door to the use of a contained, contestable element of the licence fee was a recognition that there might be justified calls on that support from other public service and publicly-valued areas like children's programming. He said "The reason that we are prioritising regional news … is because we believe that the economics there are really very urgent and that, if we do not do something quite rapidly, the future of a plural provision of high-quality regional news would come under threat. I think that would be something that would be very bad for our democracy" (Q 2317).

238. There is no doubt that real options do exist after 2012 for the support of public service broadcasters, and for particular UK-originated programming. Funding would not come from new taxes or charges but from using some of the proceeds from the sale of analogue spectrum or from a small contribution from the BBC licence fee.

239. **Given the continuing decline in funding for UK content provision, we recommend that the Government should consider use of the proceeds of the sale of spectrum and a part of the BBC licence fee.**

Quotas for UK content

240. Another approach to supporting production of UK content, would be to set quotas for transmission of UK content, in those genres most under threat. This would increase demand and funding for UK content.

241. PSB channels in the UK must currently comply with UK content quotas, in accordance with s.273 of the Communications Act 2003. Beyond news and current affairs, Ofcom has no powers to mandate any other genres, such as children's programming.

242. The genres where gaps are emerging extend beyond news and current affairs. Prior to the Communications Act 2003, the commercial PSBs were required to transmit specific amounts of children's programmes. Some witnesses regretted the current lack of quotas for these programmes.

243. Save Kids' TV's told us (p 335), "In 1996, the then ITC required the commercial PSB broadcasters to transmit a minimum number of hours of original production with quotas for particular genres. So for example ITV had to provide 77 hours per annum of Pre-school, 52 hours per annum of Factual/Information and 70 hours per annum of Drama". It went on to say that, following the introduction of the Communications Act 2003, "With children's television placed in 'tier 3' ... Ofcom's resultant 'light touch' regulation left the broadcasters to their own devices, in terms of hours and content commitments". Save Kids' TV went on to recommend that quotas should be reintroduced for children's programmes.

244. Peter Phillips, Partner for Strategy and Market Developments, Ofcom, said that the Communications Act 2003 had decided that "children's programming is a tier three obligation … where broadcasters have to hear what our advice is but where they can take their own decisions about what level of that programming they choose to put in place. That was a conscious decision that Parliament took, but clearly if you and your colleagues in

Parliament took a different view then, obviously, we would give effect to that" (Q 2250).

245. Other witnesses opposed quotas for specific genres. Michael Grade, Executive Chairman of ITV, said, "There is £3.6 billion of public intervention in the broadcasting market of this country, called the BBC. Channel 4 has a hidden subsidy. It has no cost of capital; it has no shareholders to pay; it does not pay for spectrum; so there is a hidden subsidy at Channel 4. We make a huge contribution as a nation, willingly, into the broadcasting sector. It is the job of the public sector to meet these objectives not the private sector, which can no longer afford to do it" (Q 1875).

246. Luke Crawley, Assistant General Secretary of BECTU, said UK content quotas were difficult to enforce across all channels and were "something that we would support generally, but it is not something that we are prepared to put forward as a solid idea. We think that it is a good idea in principle, but it is not very clear. For example, how would it work with a channel like Nickelodeon? Clearly that is not UK-originated. However, we think it is quite important that there is some kind of encouragement. Whether or not a quota is the right way to encourage broadcasters to carry UK-originated children's programmes, I think it would be one way of putting pressure upon them to do so" (Q 214).

247. As we have made clear, we are anxious to encourage increases in children's programming and UK drama. We believe, however, that the other measures we have proposed are more hopeful than quotas, particularly at a time when the commercially-funded PSBs face particular and practical difficulties.

248. **Given the current financial constraints on the commercially-funded PSBs, we do not think it is realistic to introduce quotas on specific genres of television programming.**

Regulation of EU content

249. As discussed in Chapter 3, television broadcasters (including multichannel) are subject to the obligations of the European Union Audiovisual Media Services Directive (AVMS). The AVMS Directive requires that, "where practicable", more than half of all programming on television channels should consist of content produced in EU countries. In practice, for most UK channels this means UK content. Ofcom provides guidance for broadcasters on implementing articles 4 and 5 of the Directive,

250. It is not clear to what extent channels currently meet the obligations of the Directive. Stewart Purvis, Partner for Content and Standards, Ofcom, told us that, in 2005–2006, about half of the 419 channels that Ofcom regulate met this requirement. He went on to say "That shows that a large number are not but in that you have to fit in all the news channels and the sports channels, all the specialist channels which are not showing European content" (Q 2274).

251. PSB channels comfortably meet this obligation: the issue is for the non-PSBs. Kerry Neilson, Executive Director, Satellite and Cable Broadcasters' Group, said, "All of our members, in conjunction with Ofcom, with whom we work very closely, are very careful to do what the Directive says and to stick to what the rules of the Directive are. You have to remember that some of the wording says "where practicable" (Q 1610).

252. Dr Carole Tongue, Chair of the UK Coalition for Cultural Diversity, suggested that the AVMS Directive was a way of increasing the EU (and thus UK) content of the cable and satellite channels, as it does in countries such as Spain, France and Italy, but went on to say that Ofcom could do more to encourage these channels to comply with the Directive. She said, "So far, Ofcom has not, as it were, engaged with the non-terrestrial broadcasters in this country to encourage them, over time, in a proportional way—for example according to longevity, audience and turnover—to increase the domestic programmes they broadcast" (Q 438).

253. **We recommend that Ofcom should work more closely with cable and satellite channels based in the UK, to explore ways of ensuring that the aim of the rule on European content, as set out in the EU Audiovisual Media Services Directive, is met.**

Potential for funding by fees

254. Four specific types of fees could be considered as a means of raising additional funding for UK content. These are: reuse fees; retransmission fees; search engine fees; and broadband fees derived from Internet Service Providers (ISPs) and phone operators.

255. Reuse fees are a tax on recording devices[84] that are used for recording copyright material. The purchaser pays a small fee for the right to copy and retain a recording of the material, thus allowing some value from the original copyright to flow back to the creators of the material. In other words, copyright holders are compensated for legally made copies of television programmes.

256. The UK Government does not impose reuse fees. Currently, the revenue from the sale or rental of recording devices goes to the manufacturer of the recording device. Although it is the availability of content to record which makes the devices attractive to consumers, no part of the revenue goes to copyright holders. The UK is one of only a handful of EU countries that do not use reuse fees. Steve Morrison, Chief Executive of All3Media, said that, "The only countries that do not do it are Malta, Luxembourg and Cyprus—which I believe are all too small to run such a system—and the UK and Ireland who have not yet seen the need to run such a system" (Q 637).

257. The system of reuse fees that already exists in Europe (across the 22 EU states) generated €568m in 2004, with most of the income being recycled back to copyright holders[85]. Ofcom told us (Q 2272) that they have not done any work on the amount that reuse fees might raise in the UK, but one study[86] estimates that that they could generate around £175m per annum by 2012 in the UK.

258. The Government does not favour the introduction of reuse fees. Digital Britain states that, as broadcasters in the UK already benefit from substantial public intervention, such as the licence fee and spectrum allocation, the Government is not persuaded to introduce such fees, particularly in the current economic climate. However it will keep the situation under review[87].

84 These include: Hard disk recorders; Video Cassette Recorders; blank DVDs; DVD Recorders.

85 Digital Britain, Final Report, June 2009, p.119

86 Ibid, Paragraph 65

87 Ibid, Paragraph 66

259. Ben Bradshaw, Secretary of State for Culture, Media and Sport, told us, "We have left the door open to reuse fees in future. We have asked Ofcom to keep this under review, but we felt that the current time with the state of the market was not the time to think about introducing them now. It is certainly not something that we would rule out in the future. However, … a lot of people who look at other models in other countries and suggest levies sometimes ignore the fact …, that we already have the biggest intervention in the market of any country in Europe through the licence fee" (Q 2344).

260. Lord Carter of Barnes, then Minister for Communications, Technology & Broadcasting, also told us that part of the reason why there is no use of fees and levies in the UK is "because we do have a big intervention in this market. We have £3.6 billion a year of taxpayers' money … and whilst there are countries in Europe which do use such mechanisms for raising money they do not have anything approaching that level of intervention of public funding … It would be quite difficult, I think, to argue the case that we should do both" (Q 1781). However, the argument that the UK has the highest level of public intervention is not supported by Europe-wide data, which show that the UK's licence fee revenue comes seventh out of 13 countries on a per capita basis (behind Germany, Austria and the Scandinavian countries, all of which have reuse fees). Denmark raises the highest revenue per capita from the television licence fee[88].

261. Retransmission fees are paid to the copyright owners by those who own channel distribution systems or "platforms" in return for the right to replay programmes on their systems. These were advocated by BECTU[89] and Steve Morrison, who told us that they are used in 30 countries in Europe (Q 638). Luke Crawley, Assistant General Secretary, BECTU, said that retransmission fees are applied "just about everywhere in Europe and in some ways we are, surprisingly, a rather anomalous country for not doing it. The re-transmission could bring in as much as £63 million a year" (Q 208). In the US, this principle of obtaining "fair compensation" was recently endorsed by News Corporation's chairman Rupert Murdoch in respect of his company's Fox television network: "we will be seeking retransmission dollars from our distributors. Asking cable companies and other distribution partners to pay a small portion of the profits they make by reselling broadcast channels … will help to ensure the health of the over-the-air industry in America."[90]

262. BSkyB, however, argued against, saying "You would be robbing Peter to pay Paul. If you restrict our ability to invest in programming, we will do less of it and that is the effect that a levy would have" (Q 1998). This was also the view of the Satellite and Cable Broadcasters' Group (Q 1601). Digital Britain stated that the Government "remains unconvinced" that such a fee would "generate the necessary future revenues to fund content creation in the UK, without unacceptably adverse consequences"[91].

263. Ben Bradshaw, Secretary of State for Culture, Media and Sport, told us that the Government does not favour retransmission fees (Q 2345). He said, "The work we did during the preparation of the White Paper showed that the

88 European Audiovisual Observatory Yearbook Online Premium Service 2008

89 Broadcasting, Entertainment, Cinematograph and Theatre Union

90 The Times, 17 October 2009, http://business.timesonline.co.uk/tol/business/industry_sectors/media/article6878611.ece

91 Digital Britain, Final Report, June 2009, Paragraph 61

current arrangements on satellite transfer no value to PSBs, because the retransmission fees are offset by the carriage fee. This might be different from other European countries" (p 528).

264. Search Engine Fees. Another possible funding mechanism would be a fee on search engines such as Google and Yahoo! which routinely use copyright material from other organisations and content creators to drive their own page impressions and thus generate significant advertising revenue. A recent proposal along these lines in France estimated that such a levy would raise €10–20 million a year.[92]

265. Broadband/mobile fees. A final suggestion was fees derived from ISPs and mobile phone operators which increasingly benefit from the use of third party creative content but pay nothing towards it. Both France and Spain have recently decided to impose such levies, which can work either as a small annual fee paid by each subscriber or as a percentage tax of annual revenue. These have not been employed in many countries because most governments are, as in the UK, keen to encourage broadband take-up.

266. Dr Carole Tongue, Chair of the UK Coalition for Cultural Diversity, said that "The report by the NUJ and BECTU, written by the IPPR[93], says that if you levied one per cent on mobile phone operators or internet service providers, that would produce a revenue to drama/film/documentary, depending on where you directed it, of £210m. If you levied one per cent on video-on-demand providers/Virgin Media and BSkyB, that would produce £70m" (Q 438).

267. Commenting on the general applicability of fees, Luke Crawley, Assistant General Secretary of BECTU, said, "There is no doubt that these are used as mechanisms for raising funds in other countries, which are then used to subsidise one form or another of public service broadcasting, and we think they could be used here and could produce the kind of money that is necessary" (Q 208). Jocelyn Hay, Honorary President, Voice of the Listener and Viewer, agreed, "We, again, were very disappointed last year when Ofcom produced its review of public service broadcasting that it did not take more notice of a suggestion put forward particularly by Steve Morrison from All3Media, that levies on a range of different providers—hardware, software, equipment manufacturers, all kinds of things—should be looked at as an alternative source of funding". (Q 1533)

268. **Although we do not favour the introduction of industry fees in the current economic climate, we believe that the Government should ask Ofcom to assess research already done on possible use of fees in the UK, and commission them to conduct further research to reach firm conclusions on the likely costs and benefits of such fees. This would provide a firm basis on which Parliament might make any future decisions.**

Independent Production Companies and UK content—Terms of Trade

269. The Terms of Trade enable independents to retain control of a share of intellectual property rights when they create programmes for broadcasters—

92 Guardian 8 January 2010, http://www.guardian.co.uk/technology/2010/jan/08/google-tax-ad-revenue-france

93 Mind the Funding Gap: The potential of industry levies for continued funding of public service broadcasting, An IPPR report for BECTU and the NUJ, March 2009

discussed in Chapter 3. Following their introduction, the sale of primary TV rights continues to be the main source of revenue for the independent sector. This income grew both absolutely and as a proportion of the independent sector's total television income.[94] Independents used the resulting revenues to contribute £126m in UK content in 2008, to the overall £3.5bn UK television content sector (p 78). Recent estimates[95] indicate that the independent production sector creates 49 per cent of all new UK television programmes each year across the PSB channels.

270. Digital Britain[96] states that "The Terms of Trade have benefited both broadcaster and producer: they recognise the producer's ownership of the creative property but also oblige the broadcaster to pay only for that element they actually wish to use—a feature that has reduced by more than a quarter the previous production costs to broadcasters". This point was made to us by John McVay, Chief Executive, PACT who said that the Terms of Trade "created a more shared risk and more shared value and reward for the investment and the exploitation of British content. So, I would not say that either party is dominant". He added that the Communications Act introduced codes of practice which "do not dictate the terms that are subsequently negotiated. Those terms are negotiated between ourselves and the four regulated broadcaster concerned—BBC, Channel 4, ITV and Five. So, it is a market negotiation and that market negotiation reflects the differences/changes in the market. I would say that, like any negotiation, you win something out of that and you lose something out of that but, at the end of the negotiation, by and large, most people have walked away reasonably satisfied that the terms they achieved were equitable" (Q 335).

271. However, some broadcasters thought that the pendulum had swung too far. Since 2006, when the television industry felt the effects of worsening economic conditions and falling advertising revenues, the situation has changed appreciably. Andy Duncan, Chief Executive, Channel 4, said, "Broadcast terms of trade have been incredibly helpful for the independent sector and many companies have benefited enormously from that. They came from a time when the broadcasters were in a much more dominant position than arguably they are today. The Channel 4 position is broadly supportive, that they should sustain at least for the foreseeable future. My own personal view … is that when you take a step back now it is rather bizarre that the four or five big super indie groups who now represent some 70 per cent of the market, and some bigger than Channel 4, have intervention to help them" (Q 2223).

272. Digital Britain[97] concludes that the Terms of Trade have worked well but, as there have been changes such as new entrants to the market and the evolution of large independent producers, it proposes a review of the relationship between independent producers and broadcasters.

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94 TV rights income grew from £1.1 bn in 2004 to £1.4 bn in 2008, while total indie income grew from £1.5 bn in 2004 to £1.9 bn in 2008. 2009 PACT census

95 Ofcom Communications Market Report 2008

96 Paragraph 99, Digital Britain, Final Report, June 2009

97 Action 15—In light of new entrants to the market, new business models and new distribution channels, it makes sense to have a forward look at how the relationship between independent producers and those who commission their ideas could evolve.

273. **We welcome the positive impact that the Terms of Trade have had on the growth of the independent production sector, and the benefits this has had on the sector's contribution to UK content. We support the Government's proposal to review the Terms of Trade, in the light of changes in the independent production sector and the impact they can have on the commercial PSBs.**

'Project Kangaroo' and its implications

274. A further way of British television companies generating additional revenue—to the potential benefit of investment in UK content—is through the development of online video on demand.

275. 'Project Kangaroo' was a proposed video on demand joint venture between BBC Worldwide, ITV and Channel 4. It was originally devised as a joint operation amongst the PSBs to enable the UK to recoup the online value of its content. This would have been supported by advertising, but with the potential of payment for downloads of older material. It would have owned its own material, and derived revenue (and profits) from making that material available via the Kangaroo platform.

276. The project was blocked by the Competition Commission in 2009, as it felt it would be too much of a threat to competition in a developing market. In a joint statement, the partners in the project said that the decision was "an unwelcome finding for the shareholders" and that "the real losers from this decision are British consumers"[98].

277. A number of other witnesses, including the Voice of the Listener and Viewer, also regretted the Competition Commission's decision to prevent Kangaroo from proceeding, as they all felt that the outcome was against the public interest. Andy Duncan, Chief Executive, Channel 4, said, "… the Kangaroo decision is a big mistake in defining markets so narrowly. In my view, they did not see the bigger picture" (Q 2226). The only witness who was in favour of the Competition Commission's decision was BskyB, because they felt that the involvement of the BBC, with its dominant position in terms of content production, would be problematic (Q 2009).

278. Whilst it is rare for the Competition Commission to consider the public interest in most investigations, the Enterprise Act 2002 provides a mechanism for the Secretary of State to intervene where he considers there may be public interest issues relating to media ownership, in order, amongst other things, to protect the availability of a wide range of high quality broadcasting[99]. However, in this case the Secretary of State did not intervene as "it was judged at the time that there was no evidence that the projected joint venture would give rise to serious public interest concerns" (p 528). Therefore, the Competition Commission was only able to assess it on competition grounds and did not consider the public interest.

279. In our view, the decision to block Kangaroo will inhibit the opportunity for UK content producers to create a stream of revenue, which might have been

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98 Guardian article, "Project Kangaroo blocked by Competition Commission", 4 February 2009

99 There has only been one use of the Public Interest Test by the Competition Commission since the Enterprise Act 2002 came into force—*Acquisition by British Sky Broadcasting Group plc of 17.9 per cent of the shares of ITV plc,* Competition Commission report, December 2007.This case was referred to in the House of Lords Communications Committee report, *The Ownership of the News,* HL 122, 2007–08

used for investment in UK content[100]. The specific risk is that the market is now open to US video on demand ventures such as Hulu[101]. Michael Grade, Chairman of ITV told the Committee that he guaranteed "that the net result of that Competition Commission decision—which in their own terms I am sure was the correct decision from the way they look at it—will be that the Americans will take the lion's share of the internet value in our content in this country very soon" (Q 1856). It appears to us likely that the Government did not understand the full implications of the failure to intervene in the Competition Commission's investigation.

280. **There is a serious risk that the UK will lose out by the decision to block Project Kangaroo and we strongly regret the Government's failure to intervene in the Competition Commission's investigation. We urge that, if other similar UK-based video on demand projects are proposed, the Government will ensure that the implications for the British television industry are properly taken into account.**

[100] Another joint venture currently under consideration is Project Canvas, an example of internet protocol television (IPTV), in which the BBC, ITV and BT (and more partners to be included) are developing a broadband Freeview service that could see on-demand programming, made available via television sets. Project Canvas is not of direct relevance to our inquiry, as it would not generate a stream of revenue which might be invested in UK content.

[101] Hulu offers a mix of advertising-funded British and American programmes

CHAPTER 5: SKILLS AND TRAINING

281. Throughout this inquiry, we were told that one of the strengths of the UK film and television industries is the highly skilled workforce. The quality of British actors is immediately apparent in the succession of Oscars and other awards won, and in the regular demand for British performers in leading roles in Hollywood. This high quality is also to be found in behind-the-camera roles of writing, directing and the range of craft and technical skills required for production and post-production. But we were struck by the views of some of our witnesses that there were skill shortages in some areas and that training was not as well linked to the needs of the industries as it might be. We also heard that the changing structure of the industry and the current economic climate were limiting the availability of funding for training.

282. We heard that training across the film and television industries is patchy, with considerable variation in the extent to which organisations contribute towards both funding and provision of training. The BBC is heavily involved in training, spending £43m on training in 2007/08. On the other hand, small companies are more limited by resources, and so can only provide limited training opportunities (Q 1393). Dinah Caine, Chief Executive, Skillset, told us that, in 2008, 78 per cent of broadcast television employees have received some formal training, whereas only 36 per cent had in the independent production sector (Q 1216).

283. There are a variety of funding and training organisations within the film and television industries, but Skillset is the main organisation through which funding is channelled. Skillset is the Sector Skills Council for Creative Media[102], which covers training in both the film and television industries, and describes itself as "an independent, industry-led organisation; jointly funded by industry and government, our job is to make sure that the UK creative media industries have the right people, with the right skills, in the right place, at the right time, so that our industries remain competitive" (p 262).

284. This chapter outlines what the training landscape looks like and ways in which links can be forged between education and industry to help plug the skills gaps. We also consider the role and funding of Skillset. In this discussion, we go beyond the question of skills and training as they affect the production of UK content, and comment on how training could be developed to improve the general health of the film and television industries.

Education and industry

285. High proportions of the workforce in both the television and film industries are graduates. According to Skillset (p 266), around two-thirds of the workforce in the television industry is made up of graduates, which is a higher proportion than the creative media sector overall. Nearly half of those hold a media-related degree, and the percentage of entrants choosing media-related degrees is growing. In the film industry, there is also a high percentage of graduates—58 per cent in film production out of which 21 per cent hold postgraduate degrees and 38 per cent are media related (p 266).

[102] Skillset subdivides the Creative industries into 10 sectors: animation, computer games, facilities, film, interactive media, other content creation, photo imaging, publishing, radio and television

Universities therefore play an important role in training provision. However, many of our witnesses from the industries were concerned that universities do not offer the specialist training needed by students who want to go on to work in the film and television industries.

286. We heard from a number of witnesses including those from the animation industry, visual effects sector, and cable and satellite companies that even graduates with a vocational element in their media studies degree, still require another one or two years of training once they enter the industry. Sophie Turner Laing, BSkyB, criticised the quality of media studies courses, saying students "are not particularly brilliantly taught and then we have to retrain them as soon as they come out" (Q 2019). On the other hand, Kate O'Connor, Executive Director, Policy and Development, Skillset, argued that media courses are not aimed at developing technical skills. She explained "some of those courses at degree level are not intended to be about training for work in the media industry; they are disciplines, like any other arts discipline, that students study for the love of the subject" (Q 2094).

287. Whatever point of view you take on university courses, it remains the case that there are several specific skills gaps or shortages at the higher or postgraduate level that are not being addressed. These are predominantly in visual effects (anything that you see in a film that you cannot shoot with a film camera and is then created in post-production); animation skills and multimedia skills. Also, at the secondary school level, Skillset agreed (Q 1222) that it needs to be made clearer to pupils that studying science subjects like mathematics and physics, can lead to a career in the animation, computer games and post-production sectors.

Post-production

288. On visual effects, Roy Button, Warner Bros, told us that UK universities are not offering the necessary grounding in digital skills, compared with France and Germany; hence the Computer-Generated Imagery (CGI) sector had to bring in foreign trained students. This view was supported by Colin Brown, UK Film Commissioner, who said that the UK visual effects specialist companies (which are largely based in London's Soho), work extremely well together and produce very high quality output. But he added that the UK was not training enough visual effects artists. Many more people with mathematics and computer science skills need to be trained, and there were gaps in the provision of training for these skills (Appendix 5).

289. Alex Hope, Managing Director, Double Negative, emphasised the importance to the UK economy, of pursuing the development of higher-level skills in visual effects, in order to bring about a global competitive advantage. He said "currently the significant challenges come from the States and from Australia and New Zealand—there are some companies in Canada as well … increasingly we will see competition from Southeast Asia, India and China" (Q 942).

290. Mr Hope identified "two kinds of visual effects work—what might be referred to as commodity work, which might be painting out the wires on a stunt man … [and] the higher end work of creating a digital character. I would suggest that that lower end work will be very price sensitive and that for the higher end work, which is the more skilled work, there are significant barriers to entry. So a policy that focuses skills at that very top end is policy that is going to see a sustainable British visual effects industry". He thought

that this required that "companies, both small and large, understand where there are R & D grants and things like that available to them, of which a lot of smaller companies in my sector are not necessarily aware. And seeing policy that is joined up between universities, the film visual effects industry and the games industry is what I would strongly recommend" (Q 942).

291. Other representatives from the visual effects and videogames industry advocated closer links between higher education institutions and industry. Alex Hope said, "I would favour a move to bringing industry and higher education closer together, incentivising in-house training at larger companies; incentivise the training of those people giving training in higher education, so that people who are teaching a course in computer graphics have the opportunity to spend some time in a company like ours to learn what current best practice is" (Q 956).

Animation

292. Skillset report that a quarter of animation companies report a skills gap. Miles Bullough, Head of Broadcast, Aardman Animations[103], said, "In our sector we feel that the education system is not delivering to us the graduates that we need for our business" (Q 1458). According to Aardman, there are around 250 media courses containing an animation module in the UK, but UK employers still have to recruit graduates from France and Germany. Aardman tried to set up an academy themselves, in partnership with local universities, to try and plug the skills gap but said that, because of the structure of higher education funding in the UK, they were unable to develop it. Skillset told us that the Government skills agenda and budget focuses on lower-level skills, and that the budget for specialist skills is channelled through higher education funding bodies.

Multimedia

293. We were told that lack of flexibility within universities made it more difficult to train in multimedia skills, such as computer studies/graphic design. Peter Dale, Chair, Television Skills Council, Skillset, said that a problem with the structure of higher education was that "very good organisations and universities still operate in silos of creative work. So, for example, in games, in a university the computer science department will have nothing whatsoever to do with the graphic design department, and there will be competition between them" (Q 2100).

294. Skillset told us that targeted funding would be required in order to tackle the skills gaps in the areas of visual effects/post-production/animation, but that this would only involve training about 300 individuals a year. They suggested that, the Department for Business, Innovation and Skills (BIS) might hold some of the Higher Education Funding Council money in a specific fund for high-level training, which could be accessed by Skillset (Q 2122).

295. **We recommend that the Department for Business, Innovation and Skills should encourage the Higher Education Funding Council to**

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[103] Aardman Animations, Ltd., also known as Aardman Studios, is a privately owned British animation studio based in Bristol, United Kingdom. The studio is famous for its stop-frame, clay animation productions.The same technology is used for all productions. Aardman is well known for its plasticine duo, Wallace and Gromit.

deploy some of its funding to support high-level, post-graduate training in the post-production and animation sectors.

296. As with other industries, reducing skills shortages in the creative sector would be helped by closer links between education and industry. Skillset has attempted to do this by setting up a network of "academies, media academies and screen academies, and it is those particular higher education institutions and FE colleges who are now working with the industry"[104] (Q 2094). These academies run courses with a significant vocational element which meet standards laid down by Skillset, and which "can start to build the kind of curriculum and the kind of programmes that are needed by the industry" (Q 2103). Skillset told us that examples of highly successful academies include the NFTS; Teesside University; and Bournemouth University (Q 2095).

297. Lord Carter of Barnes, then Minister for Communications, Technology & Broadcasting, told us that in his view the links between the creative industries and universities were growing. He said there was "increasing and in-depth engagement between industry, commerce and the major educational institutions" (Q 1786). We would like to see these links developed further, to enable students in the creative industries to spend a significant part of their courses with a company.

298. Skillset emphasised that industry dialogue with the higher education sector is a two-way process and that industry needs to be clearer about its needs. Peter Dale, Skillset, said, "Certainly one of the structural problems we have been having with the media academies is getting the industry to make recognition of what they might contribute. They tend to take the old view, which is that: "The academies or colleges will turn out people with some ability and we will pick ones we like the look of", rather than saying, actually: "This is a process of dialogue we ought to be having where we are identifying the skills that we anticipate needing and match that with the curriculum that these places are offering". That dialogue is not happening, at the moment. We are making a great effort to make sure that happens, but it has to be a two-way thing" (Q 2105).

299. It is apparent that, in order to realise the full benefits of, for example, academies, in enabling greater connections between education and industry, that the industries must be willing to engage in greater dialogue with the education/training providers.

300. **We support Skillset's efforts to promote dialogue between the education and training providers and the film, television and videogames industries. We recommend that the Higher Education and Funding Council should encourage closer relationships between universities and the creative industries, including the introduction of sandwich courses for media studies degrees enabling students to spend part or all of the penultimate year of their degree working in the industry.**

[104] The **Skillset Media Academies** form a network of colleges and universities across the UK which are centres of excellence in **television** and **interactive media.**

Apprenticeships and internships

301. Historically, apprenticeships have been used in industries of all kinds to address skill gaps. But partly because of the unusually high proportion of graduates and postgraduates coming into the creative sector, there is limited use of apprenticeships in the film and television industries. As Dinah Caine, Skillset, noted, "… there is a tendency to recruit people with higher education qualifications, which immediately rules out the normal old-style apprenticeship recruits" (Q 1233). She considered this to be largely due to the culture of the industry, "because a lot of roles in the industry could be open to apprenticeships" (Q 1233). She said that Skillset is trying to address this problem. For example, it is considering the development of a digital media apprenticeship which might "get the industry to see that they do not always have to recruit at HE level" (Q 1233).

302. Additionally, the prevalence of freelance employment, in both film and television, makes apprenticeship schemes difficult to operate. Kate O'Connor, Skillset, said that "there is huge scope for apprenticeships in the film industry, but because of the nature of employment in the film industry people are not employed, apart from on the films and projects. There does need to be this brokerage system, so that we can sort out training providers … to help organise those apprentices" (Q 1231).

303. While they are not widespread, apprenticeships are provided by some companies. Eric Fellner, Deputy Chairman, British Film Institute, and Co-Chairman of Working Title productions, told us that Working Title had decided to set up their own scheme. "We finance it fully ourselves, it costs us a couple of hundred grand a year and we just think it is worth putting that kind of money in. We can give three places and we train people right across the board. All of the people that we have trained have since gone on to work in the industry and are starting to develop business skills and creative skills to take them into, hopefully, being the leaders of the future" (Q 1157).

304. Other companies have used work placements as well as full apprenticeships. Roy Button, Warner Bros, thought that it was essential to bring students into the studios on work placements. He said that "we always avail ourselves of any trainees or training opportunities or apprenticeships for as long as we can on a film. Certainly in some of the craft grades that I am interested in, scenic artists, painters, plasterers, all that sort of thing, less so for the more mechanical stuff like electricians and props because that is somewhat simpler because it is less talent driven" (Q 1391).

305. In our view, apprenticeships and internships in the film and television industries are under-used and uncoordinated. We believe there is scope for increasing their use, to the benefit of the industries but also as a step to providing more structured careers for film and television industry staff.

306. In addition to the issues already discussed, there seem to us to be three further training issues to be addressed in these industries. First, the entry routes into the industries are still fairly informal, which perpetuates the "who you know" culture in some pockets of the industries. Second, the industries are characterised by widespread use of unpaid work experience, which while developing skills, discriminates against those who cannot afford to work unpaid. Third, unequal attention is paid to training by different organisations within the industries.

307. According to Skillset, 47 per cent of the television workforce has undertaken unpaid working at some point in their careers (p 12). In a 2008 survey, nearly 40 per cent of the film production workforce had done some unpaid work experience in the film industry before getting a paid job[105]. Skillset emphasised the absence of clear entry routes into the industry and that progression routes are not supported by proper organisational structures (p 7).

308. The use of foot-in-the-door work experience would probably be reduced if our recommendations on apprenticeships, internships and sandwich courses are adopted. This was a point made by Peter Dale, Chair, Television Skills Council, Skillset, who said, "I think this goes back [to] … education and access to courses, because, clearly, if you turn out with the right skills, that is more qualifiable than having your father know someone who runs a television company. I think unpaid work is endemic; it is undesirable, but I think the figures speak for themselves. A very, very large proportion of freelancers will have undertaken unpaid work at some point, and companies with their backs against the wall trying to make a programme on a reduced budget will be even more tempted to take those people on" (Q 2129).

309. Skillset along with the industry is trying to address the issue of informal work experience. Kate O'Connor, Skillset, said, "We have just recently finalised a code of conduct for what are called graduate internships, because this is the area that seems to be most confusing—what constitutes work experience, legitimately unpaid, and what constitutes working for nothing to get a foot in the door to get that first range of contacts" (Q 2132).

310. Within the television industry, there are initiatives such as in-house training, and work experience. In addition to or in lieu of Skillset's funded schemes, these are run and, where applicable, funded by organisations including the BBC, and major independent production companies.

311. Looking across the television industry, and the variation in provision of training between cable and satellite providers, the PSBs and the independent production sector, it is clear that there is unequal access to the industry as a whole, with the risk of exploitation of staff through unpaid work, as well as unequal access to training.

312. **We welcome the work that Skillset is doing on codes of conduct for internships, and encourage them to play a greater role in the coordination of apprenticeships and other on-the-job training**.

313. **We urge the film and television industries to provide more equal access to training and skills-based career development through greater use of apprenticeships and graduate internships.**

The BBC

314. As we have mentioned, the BBC is a key provider of training within the creative industries. Its training budget was £43m in 2007/08—although, in the run up to the 2005 Charter Review, it was around £57m a year (Q 1250). The budget cuts have led to a reduction in, for example, general traineeships, which were only reintroduced in 2009 (Q 568). Despite the reduction in the training budget, the BBC does still play a significant role in

105 Skillset/UK Film Council Film Production Workforce Survey (2008)

training both for its own staff and more widely. Tim Bevan, Working Title Productions, said, "a lot of our crews who would be working on *Harry Potter* movies have probably been trained at the BBC" (Q 1386).

315. The BBC outlined to us its role in both training its own staff and the wider industry. Jana Bennett, Director BBC Vision said, "Overall, last year we had 57,000 days' worth of face to face training of staff, so there are very many other different types of training we do as well. 5,000 days of training were also delivered to individuals and organisations in the wider industry" (Q 568).

316. Given the pressure on training budgets in the television industry, the BBC could make its training provisions more widely available. Peter Dale, Chair, Television Skills Council, Skillset, said, "One of the things we are really trying to do is to ensure that organisations that have substantial training capacity, like the BBC, can make that more available. Of course, it is in the BBC's interests to spread its public service contribution as widely as it can. So we are in very good dialogue with the BBC about using its training for freelancers and repurposing it for people who do not belong to the BBC" (Q 2138). In response to this suggestion, Jana Bennett, Director of BBC Vision said, "We understand that our role in training becomes more important with the structural pressures that the industry is under. I do not think we can be the sole provider of everything but we want to be more porous and open" (Q 569). In December 2009, the BBC launched the BBC Academy—a dedicated centre of excellence for training in journalism, production, leadership and technology, giving wider access to the BBC's training resources and skills to support the wider UK media industry.

317. **In the light of the variability of training across the sector, we welcome the continuing role played by the BBC and the BBC's willingness to make its training more widely available through the launch of the BBC Academy.**

Funding of Skillset

318. Contributors to Skillset's training have included BBC, ITV, Channel 4, five, the Indie Training Fund[106] and S4C (Channel 4 Wales). The BBC is the largest contributor. Two of the funds Skillset uses to support the film and television industries are the Film Skills Fund, and the TV Freelance Fund. The Film Skills Fund is the largest fund in the UK dedicated to training in the film industry with funds provided by the UK Film Council, of £6.5m per annum over the last five years. The TV Freelance Fund invests in training for the freelance television workforce, and invested £1.5m in 2007–08. It was introduced because the television industry is characterised by high levels of freelancing, a mobile workforce, and the high cost of training.

319. Other organisations providing formal training include the National Film and Television School (NFTS) and the Film Business Academy. The NFTS has 13 core funders and receives just over 50 per cent of its funding via the Department for Culture, Media and Sport and Skillset. A further 20 per cent is received from broadcasters, and the remaining 30 per cent through fees and fundraising. Funding provision to Skillset and the NFTS has fallen

[106] ITF is a registered charity that aims to improve the competitiveness of UK independent television and digital media production companies, by collecting funds from their productions to invest strategically in appropriate training and development initiatives

within the last few years. The implications of this are considered in paragraphs 324 to 331.

320. The Film Business Academy, which is supported by Skillset and the UK Film Council, was launched in 2005, in order to provide courses in business skills for the film industry. According to Terry Ilott, Director, Film Business Academy, there was the perception that there was a "huge dearth of business skills in the industry" (Q 1276). This was a view supported by Martin Smith, Special Adviser, Ingenious Media, who said, "We have the best technical skills and we have the greatest talent, but we do not capture the commercial upside in this country. We must raise our sights higher" (Q 852). According to Mr Ilott, 80 per cent of what is taught is generic to business (Q 1314), but the Film and Business Academy has film-specific modules within their MBA and MSc business and management programmes.

321. In emphasising the importance of training within the film and television industries and how delivery might be improved, we recognise that there has been a large reduction in the funding available to Skillset, through which public funding for training is channelled, and a significant reduction of funding to the NFTS, one of the key deliverers of training. During 2009, NFTS has lost its funding from ITV, Channel 5 and Discovery. Sky and Channel 4 have also had reduced their funding. In total cuts have amounted to over £500,000 (p 285), around 6.5 per cent of the NFTS total budget of £7.7m[107].

322. As Skillset is the main organisation through which funding is distributed, reductions in funding to Skillset effectively mean reductions in funding available to the film and television industries overall. We recognise that there are excellent private providers of training to the industries, but the sector as a whole relies heavily on the contribution of Skillset.

Reductions in television industry financial contributions to Skillset

323. Skillset told us that, over the past two years, broadcasters have reduced their investment in training and skills. Kate O'Connor told us that as of 2009, out of all the PSBs, ITV reduced its funding to Skillset the most, withdrawing funding totally from the freelance training fund, and "substantially" from the core fund (Q 2144). She went on to say, "It does concern us that, overall … we have now 50 per cent of the fund that we had last year, with a growing list of skill requirements and a real need to prepare for the future upturn, hopefully, of content development and the skills associated with that" (Q 2147). Furthermore according to Skillset, in 2009, the independent production sector has only contributed 20 per cent of what they normally provide (Q 1216).

324. Asked about ITV's reduction of funding to Skillset, Michael Grade said, "We have made the decision that whatever resources we have we need to spend on internal training and development of our own people first … We have had to cut the investment. It is not in our long-term interests for there to be an even greater skill shortage in the sector, not in our interests at all, and we have to get back to our previous levels of investment as fast as we can—as fast as the economy will allow (Q 1879). He went on to say, "Sadly, when you lose 15 per cent of your revenue overnight, you have to make some

107 NFTS Management accounts for year ending 31 December 2009, to be published in May 2010

very fast, short-term decisions. You do not want to make them but you have to; you have no choice” (Q 1880).

325. John McVay, PACT, felt that ITV’s decision was short-sighted, and that an obligation should be placed on PSBs to contribute to organisations such as Skillset, as they are subsidised by public money (Q 361). Michael Kuhn in his capacity as Chairman of the National Film and Television School, agreed with PACT’s view (Q 1296 and 1324).

326. The Communications Act 2003, does not oblige PSBs to contribute to organisations such as Skillset or the NFTS. Asked if such obligations should be placed on PSBs, Stewart Purvis, Partner for Content and Standards, Ofcom said that there had been discussion about a more interventionist approach, “about requiring specific funding from specific broadcasters for the training, for instance, of freelancers” but added that there has not always been agreement on that and Ofcom has not necessarily always agreed with Skillset’s interpretation of our options”. He went on to say, “as yet we have not thought it one of our regulatory duties to insist that broadcasters contribute to, for instance, freelance training” (Q 2281).

327. We regret that funding contributions from the television industry (including the PSBs, satellite and cable sector, and independent production sector) to the key training providers, have been reduced or withdrawn. Training is critical to the long term health of the television industry. We are particularly concerned that the PSBs, which continue to receive some privileges from their status as PSBs, are withdrawing from the funding of training. Lord Puttnam told us that to allow a situation to occur “whereby ITV, on the same day that it is released from £20 million worth of PSB obligations, cuts its external training budget completely is lunacy” (Q 779). We believe that training should be a priority obligation of PSBs and that, if necessary, the regulatory framework might be reviewed to ensure that the PSBs continue to fund training.

328. **We understand the current pressures on the budgets of UK commercial public service broadcasters but believe that the reduction in training budgets threatens the future competitiveness of the UK television industry. We urge the Government to encourage PSBs to revive their investment in training.**

Reductions in the UK Film Council’s financial contributions to Skillset

329. The UK Film Council has been a major contributor to Skillset, but its contributions are likely to be lower over the next few years. Stewart Till, then Chairman of the UK Film Council, told us in March 2009, “I think it is vital that the Film Council continues to invest in the training and education of that workforce. We have spent £6.5 million a year over the last five years; so a very large slice of our budget. What I often think the Film Council does best is to do what the industry, because it is a very fragmented industry, does not do. The industry historically has not been good on training and education because it is so fragmented. These very small companies or freelance workers do not invest in it” (Q 151). Despite the importance placed on the UK Film Council’s contribution to training, the allocation to Skillset’s Film Skills Fund has fallen to £5.4m in the current financial year and, under

the Council's plans[108] will fall to £3.25m for the three years to March 2013. While we understand the pressure on the Council's budget, which has come about through a reduction in lottery funding as we outlined in Chapter 2, we regret that, despite the importance given in the UK Film Council's plans to nurturing skills and creative talent as a core task, it is prepared to see a 50 per cent fall in its funding of training, compared to the allocation for the past five years.

330. **We regret that, because of budgetary constraints, the UK Film Council should be forced to reduce significantly its funding for training for the next three years, at a time when training should be a priority. We urge the Government to ensure that the UK Film Council is adequately funded to allow it at least to restore its former level of support for training.**

The current regulatory framework for training in the television industry

331. The current regulatory framework for training in the television industry is set out in the Communications Act 2003. In accordance with section 6 of the Act, Ofcom set up a system of co-regulation for training, and established, in 2005, The Broadcast Training and Skills Regulator (BTSR), as a co-regulatory body between Ofcom, Skillset and the industry[109]. The purpose of such a system is to ensure an industry-led method of planning, organising and measuring the delivery of training in the sector; and gives responsibility to broadcasters for setting objectives and standards for training both individually and collectively through Skillset.

332. There is, however, some confusion, between Ofcom and Skillset, about the co-regulatory arrangements. Skillset said in its written evidence (p 21) that "current powers have not been sufficient to allow for meaningful dialogue". When pressed on this, neither Skillset nor Ofcom were able to clarify the issue for us, and suggested that we talk to the other bodies in the co-regulatory relationship. There appears to be a disagreement between Ofcom and Skillset around Ofcom's obligations regarding freelance training. In an industry which is so dependent on freelance working and informal training, this uncertainty around statutory definitions of training is unhelpful and needs to be clarified as a matter of urgency. Given the inevitable temptation within the private sector to take short-term cost-cutting decisions, the industry is reliant on the industry regulator to take a longer view and safeguard the nation's long-term talent and skills base.

333. Ofcom told us (p 508) that it has "put proposals to both BTSR and Skillset for rationalising the current framework and developing co-operation in information collection and will be working with both organisations on the way forward".

334. **We welcome Ofcom's proposals to develop co-operation within the regulatory framework for training in the television industry and recommend that Ofcom should publish guidance to clarify the roles of the organisations involved.**

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108 UK Film Council Plan. *UK Film: Digital innovation and creative excellence—Policy and funding priorities April 2010 to March 2013*

109 BTSR's prime purpose is to work with its co-regulatory partners to ensure that the relevant broadcasters comply with Sections 27 & 337 of the Communications Act 2003. (BTSR annual report 2008)

CHAPTER 6: SUMMARY OF RECOMMENDATIONS

335. We recommend that, given current financial circumstances and the value to the international film industry of a stable tax regime, the Government should keep the rate of the tax credit for big budget films at its current level. At the same time, we recommend that the rate of the tax credit be kept under review by the Government, in consultation with the industry, in order to ensure that the UK does not become uncompetitive as a venue for international filmmaking. (para 73)

336. Given the problems faced by independent film makers in raising finance for their projects, particularly in the current recession, we recommend that the Government should consider raising the net rate of film tax relief for productions under £5m to 30 per cent. (para 78)

337. We acknowledge that there would be a benefit to producers from a change to the "used or consumed" provisions, to extend the tax credit to production expenditure overseas, and the low cost of this change. We recommend that the salaries of personnel employed on a film should be considered eligible costs whether they are working in the UK or on location overseas so long as the personnel are paid and taxed in the UK. (para 83)

338. We recognise the claims of the videogames industry for support in the face of foreign government-subsidised competition, and recommend that the Government consider providing tax incentives for videogames production. (para 88)

339. Given the difficulties of financing independent British films, particularly following the withdrawal of banks from film financing, we recommend that the Government should look at ways of facilitating greater British private investment in film production. This would need to be done in a way that ensured that the private investment was genuine and not simply a means of tax avoidance. (para 93)

340. We question, however, whether an industry body like the UK Film Council should be substantially financed by the Lottery rather than direct Government support. We regret the reduction in funding made because of the demands of the 2012 Olympic Games. We recommend that the funding level should be restored immediately after 2012/13. (para 103)

341. We do not consider that the small saving, which a merger of the UK Film Council and the BFI would be likely to achieve, would by itself justify an amalgamation. (para 107)

342. If, however, the proposal for the merger of the UK Film Council and the BFI goes ahead, it will be important that any organisational changes neither prejudice nor deter private donations to the BFI's educational and archival work. (para 108)

343. We welcome the UK Film Council's emphasis in its consultation document on supporting British films and filmmakers as its first core activity, and its proposal to use funds recouped from its investment in film to top up the Film Production Fund's budget. (para 110)

344. We support the UK Film Council's continuing commitment, as part of its first core activity, to the promotion of the UK as an inward investment destination for film production. In this context, we strongly support the proposal to strengthen the Office of the British Film Commissioner. (para 111)

345. We welcome the provisions in the Digital Economy Bill, which would bring film production within the public service remit of Channel 4. We encourage the BBC to give greater recognition to the role that BBC Films can play in developing new projects and new talent in the British independent film sector. (para 117)

346. We urge the Government, the UK Film Council and the organisations representing the exhibition sector to find a way of completing the digital equipping of cinemas in the UK which, as necessary, provides help to smaller independent cinemas to purchase or lease digital equipment. (para 123)

347. Irrespective of the outcome of the test case on camcording of films in cinemas, we remain concerned that the law is unclear and provides insufficient deterrent to abuse. We recommend that the Government reconsider the case for specific legislation to make it a criminal offence to record a film in a cinema by camcorder. (para 129)

348. Given the strength of film industry concern about the threat from audiovisual piracy, as reflected in the evidence we received, the Committee supports the Government's decision to introduce regulatory measures to combat unlawful peer-to-peer file sharing. (para 132)

349. We welcome the decision of some companies in the audiovisual industries to change their business models in order to meet the legitimate demands of their customers while generating a return on their investment in content, and encourage other companies to do the same. (para 136)

350. We support the Government's intention to sell a part of BBC Worldwide, creating a public private company. We believe that such a company, with a continuing link to the BBC, would be capable of becoming a major global brand for distributing UK content, producing additional profits, employment and opportunities for British production companies. (para 220)

351. We recommend the extension of the film tax credit, on a pilot basis, to children's programmes and animation productions made for television. This pilot, if successful, might be extended to other genres. (para 226)

352. We welcome the provisions in the Digital Economy Bill on support for independently funded news consortia to provide regional and local services. (para 229)

353. Given the continuing decline in funding for UK content provision, we recommend that the Government should consider use of the proceeds of the sale of spectrum and a part of the BBC licence fee. (para 239)

354. Given the current financial constraints on the commercially-funded PSBs, we do not think it is realistic to introduce quotas on specific genres of television programming. (para 248)

355. We recommend that Ofcom should work more closely with cable and satellite channels based in the UK, to explore ways of ensuring that the aim of the rule on European content, as set out in the EU Audiovisual Media Services Directive, is met. (para 253)

356. Although we do not favour the introduction of industry fees in the current economic climate, we believe that the Government should ask Ofcom to assess research already done on possible use of fees in the UK, and commission them to conduct further research to reach firm conclusions on

the likely costs and benefits of such fees. This would provide a firm basis on which Parliament might make any future decisions. (para 268)

357. We welcome the positive impact that the Terms of Trade have had on the growth of the independent production sector, and the benefits this has had on the sector's contribution to UK content. We support the Government's proposal to review the Terms of Trade, in the light of changes in the independent production sector and the impact they can have on the commercial PSBs. (para 273)

358. There is a serious risk that the UK will lose out by the decision to block Project Kangaroo and we strongly regret the Government's failure to intervene in the Competition Commission's investigation. We urge that, if other similar UK-based video on demand projects are proposed, the Government will ensure that the implications for the British television industry are properly taken into account. (para 280)

359. We recommend that the Department for Business, Innovation and Skills should encourage the Higher Education Funding Council to deploy some of its funding to support high-level, post-graduate training in the post-production and animation sectors. (para 295)

360. We support Skillset's efforts to promote dialogue between the education and training providers and the film, television and videogames industries. We recommend that the Higher Education and Funding Council should encourage closer relationships between universities and the creative industries, including the introduction of sandwich courses for media studies degrees enabling students to spend part or all of the penultimate year of their degree working in the industry. (para 300)

361. We welcome the work that Skillset is doing on codes of conduct for internships, and encourage them to play a greater role in the coordination of apprenticeships and other on-the-job training. (para 312)

362. We urge the film and television industries to provide more equal access to training and skills-based career development through greater use of apprenticeships and graduate internships. (para 313)

363. In the light of the variability of training across the sector, we welcome the continuing role played by the BBC and the BBC's willingness to make its training more widely available through the launch of the BBC Academy. (para 317)

364. We understand the current pressures on the budgets of UK commercial public service broadcasters but believe that the reduction in training budgets threatens the future competitiveness of the UK television industry. We urge the Government to encourage PSBs to revive their investment in training. (para 328)

365. We regret that, because of budgetary constraints, the UK Film Council should be forced to reduce significantly its funding for training for the next three years, at a time when training should be a priority. We urge the Government to ensure that the UK Film Council is adequately funded to allow it at least to restore its former level of support for training. (para 330)

366. We welcome Ofcom's proposals to develop co-operation within the regulatory framework for training in the television industry and recommend that Ofcom should publish guidance to clarify the roles of the organisations involved. (para 334)

APPENDIX 1: SELECT COMMITTEE ON COMMUNICATIONS

The Members of the Committee which conducted this inquiry were:

Baroness Bonham-Carter of Yarnbury
Baroness Eccles of Moulton
Rt Hon the Lord Fowler (Chairman)
Lord Gordon of Strathblane (appointed April 2009)
Lord Hastings of Scarisbrick (resigned November 2009)
Baroness Howe of Idlicote
Lord Inglewood
Rt Hon Lord King of Bridgwater
Rt Hon Lord Macdonald of Tradeston
Baroness McIntosh of Hudnall
Rt Rev Lord Bishop of Manchester
Lord Maxton
Baroness Scott of Needham Market

Lord Corbett of Castle Vale resigned from the Committee in March 2009 and did not take part in this inquiry.

Lord St John of Bletso was appointed to the Committee in December 2009 and did not take part in this inquiry.

Declarations of Interest

BONHAM-CARTER, Baroness

12(f) Regular remunerated employment
Television Executive, Brook Lapping Productions, a subsidiary of Ten Alps Communications plc
**12(i) Visits*
Visit to Guardian Hay Festival of Literature, Hay-on-Wye (22–24 May 2009) sponsored by skyARTS—accommodation and meals provided by Sky
**13(c) Financial interests of spouse or relative or friend*
I also disclose the interests disclosed by Lord Razzall
16(b) Voluntary organisations
RAPT—Rehabilitation of Addicted Prisoners Trust

ECCLES OF MOULTON, Baroness

**12(e) Remunerated directorships*
Independent National Director, Times Newspapers Holdings Ltd
15(b) Trusteeships of cultural bodies
Director, Opera North, company limited by guarantee ***(unpaid)***

FOWLER, Lord

**12(e) Remunerated directorships*
Non executive Director, Holcim Ltd
Non executive Director, ABTA
Chairman, Thomson Foundation
15(d) Office-holder in voluntary organisations
Vice Chairman, All-party Group on AIDS
16(a) Trusteeships
Trustee, Terrence Higgins Trust

GORDON OF STRATHBLANE, Lord

**12(e) Remunerated directorships*
Chairman, Radio Clyde
15(d) Office-holder in voluntary organisations
Hon President, Glasgow and West of Scotland Family History Association

HASTINGS OF SCARISBRICK, Lord

**12(e) Remunerated directorships*
British Telecom PLC
**12(f) Regular remunerated employment*
KPMG
Former BBC employee (1994–2006) in receipt of BBC Pension
15(d) Office-holder in voluntary organisations
Vice President, Crime Concern
Patron, Springboard for Children
Patron, Zane
Patron, Toy Box
Trustee, International Business Leaders Forum
Trustee, Vodafone Group Foundation

HOWE OF IDLICOTE, Baroness

15(a) Membership of public bodies
President, National Governors Association (NGA)
15(b) Trusteeships of cultural bodies
Trustee, Architectural Association School of Architecture
15(d) Office-holder in voluntary organisations
Member, Council of the Institute of Business Ethics
Member of the NCVO Advisory Council
Patron, Institute of Business Ethics
President, The Peckham Settlement
Board Member, Veolia Environmental Trust plc (formerly Onyx)
16(a) Trusteeships
Trustee, Ann Driver Trust

INGLEWOOD, Lord

**12(c) Remunerated services*
Political Adviser, House of Lords ***(unpaid)*** *for the Estates Business Group*
**12(e) Remunerated directorships*
Chairman, CN Group (Media)
Chairman, Carr's Milling Industries plc (food and agriculture)
Director, Pheasant Inn (Bassenthwaite Lake) Ltd (hotel)
**12(f) Regular remunerated employment*
Farmer
Chairman of a colloquium on two pictures by the Indonesian artist Raden Saleh
**13(a) Significant shareholdings*
Pheasant Inn (Bassenthwaite Lake) Ltd (hotel)
**13(b) Landholdings*
Hutton-in-the-Forest Estate (farmland including residential property in Cumbria)
Wythop Estate (farmland including residential property in Cumbria)
Owner Hutton-in-the-Forest (historic house open to the public)
**13(d) Hospitality or gifts*
20 November 2007: The costs of the plaintiffs in the case of Lord Alton and others v. The Secretary of State for the Home Department of which I was one, were met by contributions from Iranian residents in the UK through the National Council of Resistance of Iran

15(a) Membership of public bodies
Chairman, Reviewing Committee on the Export of Works of Art
Governor of Skinner's Academy Hackney (from February 2008) (20 January 2009)
15(c) Office-holder in pressure groups or trade unions
Friends of the Lake District (nominated by the Committee for the National Consultative Council)
President, Cumbria Tourist Board
Member, Historic Houses Association Finance & Policy Committee
15(d) Office-holder in voluntary organisations
Chairman of the Carlisle Cathedral Development Trust Project
President, Cumbria Wildlife Trust (from May 2008)
16(a) Trusteeships
Trustee, Elton Estate, Cambridgeshire
Trustee, Raby Estates, Co Durham and Shropshire
Trustee, Thoresby Estate, Nottinghamshire
Trustee, Calvert Trust
Trustee, Settle-Carlisle Railway Trust
Trustee, Whitehaven Community Trust Ltd
16(b) Voluntary organisations
Member, Bar
Member, Royal Institution of Chartered Surveyors
Fellow, Society of Antiquaries of London
Chairman, Westmorland & Lonsdale Conservative Association

KING OF BRIDGWATER, Lord
**12(e) Remunerated directorships*
Non-executive Director, London International Exhibition Centre plc and London International Exhibition Centre (Holdings) Ltd
**13(b) Landholdings*
Minority partner in family farm in Wiltshire (including cottages)
Partner in woodlands in Wiltshire
15(d) Office-holder in voluntary organisations
Patron, UK Defence Forum
Trustee Friends of Wiltshire Churches
Vice President, Royal Bath and West Society
Vice President of Brainwave (a charity for handicapped children) (5 February 2009)

MACDONALD OF TRADESTON, Lord
**12(e) Remunerated directorships*
Scottish Power Ltd
**12(f) Regular remunerated employment*
In an advisory capacity, Chairman—Macquarie Capital, Europe
Member of the Advisory Committee on Business Appointments (an Advisory Non-Departmental Public Body sponsored by the Cabinet Office)
15(a) Membership of public bodies
Chancellor of Glasgow Caledonian University
16(b) Voluntary organisations
Member, Fabian Society
Patron, Brighton & Hove Philharmonic Society
Patron, Dystonia Society

McINTOSH OF HUDNALL, Baroness
**12(e) Remunerated directorships*
Non-executive Director, Artis Education ***(unpaid)***
15(b) Trusteeships of cultural bodies

Board Member, Roundhouse Trust
Board Member, Royal Academy of Dramatic Art (RADA)
Board Member, National Opera Studio
Trustee, South Bank Sinfonia
15(d) Office-holder in voluntary organisations
Trustee, Art Inter-Romania
Trustee, Theatres Trust
Trustee, Foundation for Sport and the Arts
16(a) Trusteeships
Trustee, Thaxted Church Trust

MANCHESTER, Lord Bishop of
**12(f) Regular remunerated employment*
In receipt of episcopal stipend
15(a) Membership of public bodies
Chair, Sandford St Martin (Religious Broadcasting Awards) Trust
General Synod of the Church of England
Manchester Diocesan Board of Finance
Manchester Church House Co
Manchester Diocesan Council of Education
Manchester Diocesan Association of Church Schools
Life Governor, Liverpool College
Governor, Hulme Hall
15(d) Office-holder in voluntary organisations
Lord High Almoner to HM The Queen
National Chaplain, Royal British Legion
Chairman, Council of Christians and Jews
16(b) Voluntary organisations
Manchester Diocese Mothers' Union
Arches Housing
Disabled Living
Hulme Hall Trust
Wigan & Leigh Hospice
St Ann's Hospice
Manchester University of Change Ringers

MAXTON, Lord
**13(b) Landholdings*
Holiday home in the Isle of Arran
A London flat

SCOTT OF NEEDHAM MARKET, Baroness
**12(d) Non-parliamentary consultant*
Centre for Transport Studies (judging and presentation of transport awards)
Advisory Board, Centre for Parliamentary Studies
**12(e) Remunerated directorships*
Member, Lloyd's Register ***(unpaid)***
**12(f) Regular remunerated employment*
Education Cultural Exchanges—lecturing to visiting students (29 January 2009)
**12(i) Visits*
Visit to Taiwan (28 July–3 August 2007) meeting with the Ministers, members of the People's Democratic Party (fellow members of Liberal International), the British Trade and Cultural Office, parliamentarians and others. Travel and hotel costs paid by the Taipei office in the UK. Courtesy gifts received and given

APPENDIX 2: LIST OF WITNESSES

The following witnesses presented evidence. Those marked * gave oral evidence.

*	Aardman Animations
*	All3Media
*	Angst Productions
	Artists Studio
*	Association of Independent Film Exhibitors
	Barzo Productions
*	BBC
*	BBC Worldwide
	British Entertainment Industry Radio Group
*	British Film Institute
	British Screen Advisory Council
*	Broadcast, Entertainment, Cinematograph and Theatre Union
*	BSkyB
*	Channel 4
	Children's Film and Television Foundation
*	Cinema Exhibitors' Association
	City of London Corporation
*	City Screen
*	Climax Studios
*	Department for Culture, Media and Sport
*	Directors UK
*	Disney UK
*	Double Negative
	Ealing Studios
*	Eidos
*	ELSPA
*	Eon Productions
*	Equity
*	Escape Studios
*	Evolutions
	Film Agency for Wales
*	Film Business Academy
*	Film Distributors' Association
	Film London

Film and Music Entertainment
* Film and Television Freelance Training
* Films of Record
Future Films
Mr Jonathan Gems
* Mr Peter Grant, McCarthy Tétrault
Guild of Television Cameramen
* Ingenious Media
* ITV
International Broadcasting Trust
Isle of Man Government
MG Alba
* National Film and Television School
Netribution
* New Producers' Alliance
* Nickelodeon UK
Northern Film and Media
Northwest Vision and Media
* Ofcom
Olswang
* Optimum Releasing
Pinewood Studios Group
* Producers' Alliance for Cinema and Television
* Lord Puttnam
* Qwerty Films
Radio Independents Group
* Ragdoll Productions
* Rainmark Films
* Satellite and Cable Broadcasters' Group
* Save Kids' TV
Scottish Screen
* Screen Finance
Screen South
Screen West Midlands
* Skillset
South West Screen
* Tiga

* Dr Carole Tongue
* TT Games
* UK Film Council
* UK Screen Association
* Universal Pictures
* Voice of the Listener and Viewer
* Vue Entertainment
* Warner Bros Productions

  Mr Jonathan Williams
* Working Title Films

  World Cinema Alliance

APPENDIX 3: CALL FOR EVIDENCE

HOUSE OF LORDS

SELECT COMMITTEE ON COMMUNICATIONS

CALL FOR EVIDENCE

The British film and television industries

The House of Lords Select Committee on Communications is announcing today an inquiry into UK originated content in film and television.

The inquiry will focus on how the film and broadcasting industries are supporting the UK economy, including jobs, and promoting UK culture and talent and whether there is scope for them to make a greater contribution. It will examine trends in UK film production and the commissioning of UK content by broadcasters. It will assess how the current tax regime for films and, in the case of broadcasting, regulatory intervention by the Office of Communications (Ofcom), are supporting UK investment and jobs in these industries. The inquiry will also examine how related and growing parts of the creative industries sector, are contributing to the economy, and the benefits they offer to, and derive from, the film and television sectors.

In 2006, changes were made to the tax credit system for the British film industry. The new tax credit is available only for films which meet the qualifying conditions of "Britishness", which relate to the location of production and filming, the nationality of those involved and the cultural content of the film. The inquiry will examine the effectiveness of this regime and the appropriateness of the criteria used.

The inquiry will also consider the role of the Government's strategic agency for film, the UK Film Council. It will examine how the Film Council is meeting its objectives, particularly in the areas of direct financial support for production, export and distribution; encouraging investment in UK film and support for international co-production; and support for UK film culture.

The vast majority of UK originated content on UK television is produced or commissioned by the public service broadcasters (BBC, ITV, Channel 4 and Five). They are subject to requirements to broadcast minimum levels of original content. The inquiry will examine how well the regulatory framework is supporting UK originated content and whether the current arrangements are adequate for the digital age. It will also examine the implications for UK originated content of the current financial pressures on public service broadcasters, and the extent to which other broadcasters can be expected or encouraged to deliver original UK content.

The Committee would, in particular, welcome evidence on the following questions:

1. What do the UK film and television industries currently contribute to the UK economy and British culture? In what ways might this contribution be enhanced?

2. How do the current UK arrangements for distribution and exhibition of films affect the commercial success of the film industry? How might long run changes in international film production and distribution affect the UK film industry and its export potential over the next decade? To what extent is the raising of finance an inhibiting factor in UK film projects?

3. Have the 2006 changes to the tax credit system been of benefit to the UK film industry? Have they had a perceptible effect on UK film production? Are the qualifying conditions, including the "Britishness" test, for the tax credit appropriate? Are any types of film or types of commercial arrangement unreasonably excluded?
4. Is the UK Film Council meeting its objectives of giving support to production and export of British films? Could it do more to assist the UK film industry's contribution to the UK economy?
5. Is the current business infrastructure in the UK conducive to the acquisition of the managerial and technical skills required by the film and television industries? Is the business environment conducive to the emergence of entrepreneurial talent, which can take advantage of opportunities in the creative industries?
6. How successful has the regulatory system been in supporting UK content in television? Are there particular types of programming, such as drama, children's or factual programming, for which more support is needed? Could more be done through regulation or incentives, for example, to encourage non-public service broadcasters to commission original UK content? Might financial measures, such as industry levies, be feasible and effective?
7. How will the structural changes facing the UK television industry, and particularly the public service broadcasting component, affect UK originated television content? To what extent are these effects irreversible? To what extent are they being offset by changes elsewhere in the creative industries sector? What are the implications for television content creation of digital switchover and widespread broadband availability?

GUIDANCE FOR THOSE SUBMITTING WRITTEN EVIDENCE

Submissions should be sent to:
Ralph Publicover
Select Committee on Communications
House of Lords
London SW1A 0PW

Tel 020 7219 8662
Fax 020 7219 4931

and preferably also as an email attachment to: holcommunications@parliament.uk

The deadline for submitting written evidence was 23 March 2009. This has now been extended to 30 April 2009.

Please ensure that you include relevant contact details. Evidence should be attributed and dated, with a note of your name and position, and should state whether it is submitted on an individual or corporate basis.

Short submissions of 6 pages or fewer are preferred; longer submissions should include a summary. Evidence sent as hard copy should be clearly printed or typed on single sides of A4 paper, unstapled. Paragraphs should be numbered. If drawings or charts are included, we ask that these are black-and-white and of camera-ready quality.

Evidence becomes the property of the Committee, and may be printed or circulated by the Committee. You may publish your evidence yourself, but in doing so you should indicate that it was prepared for the Committee. The Committee may invite some of those who submit written evidence to give oral evidence, usually in public at Westminster. Transcripts will be published.

You can follow the inquiry via the Committee web pages, accessed from

http://www.parliament.uk/parliamentary_committees/communications.cfm

This is a public call for evidence. Please bring it to the attention of other groups and individuals who may not have received a copy direct.

APPENDIX 4: COMMITTEE VISIT TO PINEWOOD STUDIOS, 6 MAY 2009

The Committee was received by Ivan Dunleavy, Chief Executive, and Andrew Smith, Group Director Corporate Affairs, Pinewood Shepperton plc, who briefed the members on the work and business model of Pinewood studios. The Committee were then given a tour of the facilities, including film stages and television studios, the underwater stage and the sound studio. The visit finished with lunch, hosted by Mr Dunleavy and attended by a number of producers and commercial directors of companies currently working at Pinewood, at which there was general discussion of issues facing the film and television industries.

Pinewood studios

Pinewood is a full-service studio. It is a "four walls" facility, used by producers bringing their own staff. Pinewood plc is a landlord which provides services to producers.

Pinewood has 50 acres of studios, with a range of film stages, including Europe's largest. It can offer facilities to any type of production, the small budget film (£2m–£10m; one or two weeks of filming) to the major production (over $100m; 6–7 months of filming). It has two television studios, recently refurbished and growing in usage. Pinewood Group has planning permission to double the working space. It is also home to 310 businesses that support the film and television industries. It is a key part of the Pinewood business plan to build up a cluster of creative industries to attract users to the facility. There are no videogames producers at present, but Pinewood is trying to encourage them to come for the synergies and efficiencies.

A key business challenge is to maintain a consistent flow of projects. Firm commitments from film producers tend to come only 3–6 months in advance of shooting. Pinewood therefore needs to maintain contact with producers in the development stage in order to assess likely demands and maintain a flow of smaller projects to plug the gaps between the major projects. Pinewood's target utilisation rate is 75 per cent, but actual rates can vary from 50 per cent to 93 per cent. Pinewood's income is split roughly 50 per cent from film, 30 per cent from television and 20 per cent rents (from other businesses on site).

Mr Dunleavy described film making as a "very financially focused industry". There was strong competition from other studios worldwide as well as non-bespoke facilities. The recession has not had much impact on the film industry so far, except for the greater difficulty of raising finance, especially for smaller producers. In fact, cinema box office receipts tend to be robust in difficult economic times. Technical advances in filmmaking have not reduced the requirements on film studios. Digital technology means that sets need to be bigger and better. The aspirations of filmmakers have grown, leading to greater rather than lesser demand for facilities.

About 70 per cent of the projects filmed at Pinewood are American, with the remainder from the UK (which matches the balance of English language film production worldwide). US producers are attracted to film at Pinewood by the scale of the facilities, the skills of the workforce and the cost-effectiveness of production.

In the view of Pinewood Group, there is currently a shortage of skills required by the film industry. Pinewood is working with a range of organisations to rectify this. As part of Project Pinewood, it proposes to set up a Screen Craft Academy with Skillset and the National Film and Television School. It is also involved in a joint venture with Skillset which will hold courses on site.

Lunch discussion

During a round table discussion over lunch, the following views were expressed:

Contribution of the film industry

The film industry contributes about £4 billion to the UK economy. It is an economic force and a pump primer for the creative industries as a whole. There are 160 craft skills required to make a film.

Government support

The government needs to appreciate the scale of contribution of the industry. It also needs to recognise the risks that filmmakers are required to take and provide a consistent policy framework. The film tax credit system is working well. It gives confidence and benefits the industry. It might be possible to make marginal improvements, but it was essential not to jeopardise the system.

The television industry is in turmoil. This has an effect on the film industry because they have a common skills base. High end television drama, which is under pressure, is similar to filmmaking. There is a case for supporting it with a similar tax credit system.

Competition to UK film studios

The main competition for UK studios comes from Australia, Canada, Hungary, the Czech Republic and Germany. Much depends on the script and the requirements for exterior filming.

In general, the UK studios offer the best set up. Companies can be encouraged to do interiors in the UK even when exteriors have been shot elsewhere. The UK scores highly in post-production. For example, visual effects are better in the UK than in Hollywood. There are six companies providing visual effects, each of which can manage a major film.

The UK can offer the necessary "creative cluster". It has the knowledge, experience and expertise. Studio facilities, visual effects, craft skills and capacity are all available within 20 miles of London. Other locations can appear attractive for cost or other reasons, but cannot provide the infrastructure. Also, while the UK may not always be the cheapest location, it offers certainty and reliability. Producers may be prepared to pay a premium for this.

Television

A number of speakers emphasised the synergies between film and television and the value to the UK of keeping both internationally competitive. It was suggested that it might even be possible to attract filming of television shows for US networks in the UK, if tax breaks were available for television productions.

Piracy

There was agreement that pirating of the digital image was a serious problem that takes investment out of the industry. There was a need to police service providers. Recent technological developments meant that the major studios were losing control of distribution, which opened up opportunities for piracy. Also, viewers were not naturally sympathetic to anti-piracy measures: they expected to see audiovisual product free within a certain period of time.

Skills and training

The smaller size of production companies had reduced the emphasis on skills and training—at a time when technological change meant that new skills were needed. Skillset was the main gateway to improving the situation. Skillset had a scheme whereby trainees spend time with productions, receiving practical experience. The requirement is for practical skills, which are acquired on the job, but this requires continuity of film productions.

APPENDIX 5: COMMITTEE VISIT TO LEAVESDEN STUDIOS, 16 JULY 2009

The Committee was received by Roy Button, Managing Director, Warner Bros, and Colin Brown, British Film Commissioner, who briefed them on the work and business model of Leavesden Studios. The Committee were then given a tour of the facilities, including the Harry Potter sets. The visit finished with lunch, hosted by Mr Button, at which the British Film Commissioner (BFC) provided more information about his role, and the key drivers behind inward investment in the UK film industry.

Leavesden Studios

Leavesden Film Studios, located in west Hertfordshire is a film and media complex situated on the site of the former Rolls-Royce factory at Leavesden Aerodrome, which was an important centre of aircraft production during World War II. Leavesden Studios is one of only a few places in the UK where large scale productions can be made. The studios contain approximately 500,000 sq ft (50,000 m2) of flexible space which includes stage space, production office space and support buildings, along with an extensive 80 acre backlot which offers a 180 degree uninterrupted horizon which can be used for exterior sets. At any one time, 700–800 people could be working at the site, but this very much varies with the films under production.

Warner Bros. UK has had a permanent base at the studios since the first Harry Potter film was made here in 2000. They have so far made six Harry Potter films, box office receipts for which already exceed the 22 Bond films. Warner Bros. are embarked on a 254 day schedule to film the seventh and eighth Harry Potter films, which will be released in November 2009 and July 2010. Numerous commercials and music videos, and other feature films have been made at the studios. The films include Bond films, Star Wars and The Legend of Sleepy Hollow. There are currently five films shooting at Leavesden.

Warner Bros. have been active in the UK, initially as a distributor, since 1923. They started production in 1972. Since 1992, they have produced about 40 films in the UK at a cost of about US Dollars 11 billion. Warner Bros. UK's current lease expires in 2010. After that, Warner Bros. have plans to renovate and develop the studios further, but these plans are yet to be finalised and approved. The development would require planning permission from two local authorities, Watford and Three Rivers. Mr Button said that they were receiving good cooperation from both. This expansion would increase UK studio facilities by one third. The studios would operate commercially, for other companies to hire, and would become a competitor to Pinewood. As part of their development plans, Warner Bros. propose to create a Harry Potter museum as a tourist attraction, which they expect to lead to 2–300 permanent jobs on site.

Views on skills and training

Mr Button said that the UK had a very good skills base. He added that it was a good base for production of a film because it was easy to move equipment etc in and out of the UK and because UK film crews are internationally mobile. He thought that the UK film academies were providing a good grounding in skills, though it was essential to bring students into the studios on work placements. However, he considered that the universities were not offering the necessary grounding in digital skills, compared with France and Germany; hence the CGI sector had to bring in foreign trained students.

This view was supported by the Mr Brown, who said that the UK visual effects specialist companies (which are all based in Soho), work extremely well together and produce very high quality output. But the UK was not training enough visual effects artists—many more people with mathematics and computer science skills need to be trained, but there are gaps in the provision of training for these skills. Mr Brown raised the funding rules under which Skillset operated, and questioned whether the UK Film Council's training money, channelled through Skillset, reached the right targets. He thought that the UK was still "unjoined-up" on training.

Views on UK tax credit scheme

Mr Button strongly supported the current tax credit scheme. He noted that it was available for above the line costs (salaries of actors, director, etc) as well as below the line costs. He said that the UK Film Council was very helpful in operating the scheme. The documentation was straightforward and the turnaround time was good. Also, the fact that the rebate was government guaranteed gave film producers and financiers "comfort and confidence". In this context, he added that he did not expect any change in the scheme in the event of a change of government.

The one area in which he would welcome change would be the "use and consume" provisions. This led to a loss in the continuity of crew. UK studios' concerns about allowing shooting abroad to qualify could be met by putting a cap on qualifying shooting in foreign studios.

Finally, Mr Button stressed the importance of a attractive tax break scheme, given that so many countries and US states are competing for film business. He said that his board would consider it "fiscally irresponsible" to make a film in a country/state without a tax break.

The British Film Commissioner

The main role of the British Film Commissioner is to persuade American producers to make films in the UK. This includes major Hollywood producers as well as independent film companies. The Office of the British Film Commissioner consists of the Commissioner himself, plus four staff in the London office, and one member of staff based in Los Angeles. Mr Brown said he would find it very helpful to have one extra member of staff based in LA to help get more inward investment. Mr Brown noted, by way of example, that the Australian Film Commission, invested more money than the UK in events to try to stimulate US inward investment.

The figures for inward investment in 2009 are encouraging. In July 2009, the UK Film Council published the UK film production statistics for the first half of 2009. The numbers first half year (H1) production in the UK are the best since 2004. The total UK spend value in H1 2009 was £535.1m, compared with £363 million in H1 2008. Of the £535.1m total, £436.2m was accounted for by inward investment films such as Harry Potter and the Deathly Hallows Part 1, Clash of the Titans and Gulliver's Travels. Mr Brown said that the low figure for 2008 was a blip, caused by the writers' strike and actors' renegotiation in Hollywood—leading to uncertainty over production plans—and the high £/$ exchange rate. He expected 2010 to be even better than 2009.

According to the Mr Brown, the key drivers for success in inward investment are: the exchange rate; and the tax relief system for UK films. His Office had commissioned research which compared costs of making films in ten countries, and the UK came out second cheapest. Hungary was the cheapest. The two areas which drove up costs in the UK were construction costs and stage space.

APPENDIX 6: COMMITTEE VISIT TO BERLIN, 2 NOVEMBER 2009

As part of its inquiry into the film and television industries, the Select Committee undertook a visit to Berlin, 1–3 November 2009.

This document provides a minute of the meetings held.

Meeting with Kirsten Niehuus, Managing Director Film Funding, Medienboard Berlin-Brandenburg

1. Medienboard Berlin-Brandenburg (MBB) is one of the three largest of the seven regional organisations providing film financing, spending around €30m a year. The financing is provided in the form of soft loans (repayment rate around 5 per cent). About three quarters of the funding comes from the regional budget and the remaining quarter from voluntary payments by television companies.

2. The Medienboard provides funding for script development, project development, production and distribution. Only producers and distributors are eligible to apply for support and they must normally have an operation in Berlin-Brandenburg. 100 per cent of the funding provided by the MBB must be spent in the region. They will support films shot abroad if the post-production is carried out in Berlin-Brandenburg.

3. Ms Niehuus emphasised the importance of co-productions, particularly with France, where they had support at the political level. UK/German co-productions had been active until the previous UK film support system (sale and leaseback) came to an end. Under the current tax credit scheme, co-productions were very difficult. Ms Niehuus thought this was a real loss, creative and commercial, and thought UK producers felt the same.

4. Ms Niehuus said that the MBB sought to achieve a balance between support for films likely to be economically successful, those likely to be critically successful and those which nurtured new talent. She noted that enticing foreign filmmakers to make their films in Germany gave benefits to German actors (improving their international recognition) and technicians (improving their skill level). Overall, she thought the benefits of supporting filmmaking in Berlin-Brandenburg were the strengthening of the film industry itself in the region (skill levels, reputation) and secondary benefits to the local economy (catering, hotels, cars, etc). She thought additional direct employment was not a strong argument and was not convinced that it helped tourism.

5. In general, Ms Niehuus thought the German film industry had made great strides over the last ten years, increasing it local market share from around 15 per cent to 20–30 per cent. This was partly due to attracting an older cinema-going public through the development of "arthouse lite" films which appealed to this segment: films which were more complex but not disturbing.

Meeting with Dr Carl Woebcken, CEO Babelsberg Film Studios

6. Films have been made at Babelsberg since 1912. The current owners took over the studio in 2004, without incurring debt, and doubled the studio space available. Dr Woebcken said that activity at Babelsberg had exploded in 2007, with 11 films being made there and up to 2,500 people being employed on site (n.b. this was partly due to productions being put on hold until the DFFF was introduced—see below).

7. Dr Woebcken noted that the balance of filmmaking was different as between Germany and the United Kingdom. The UK was more successful in attracting Hollywood productions to be filmed or part-filmed locally than was Germany. But the number of German domestic productions was much higher than those of the UK. German producers found it easier to raise the public subsidy up to the maximum of 50 per cent. With pre-sale and equity, this was normally enough to see the film made

8. Dr Woebcken said that there were a number of reasons for foreign filmmakers to choose Germany to make their films. Firstly, the German Federal Film Fund (DFFF—see below) was internationally competitive. Foreign films could receive up to 20 per cent support (*Speed Racer* received 19.6 per cent). Germany offered good studio facilities, but also both city and country shooting locations. It had a talent pool, including experienced crews used to Hollywood methods, but also actors (43 of the 60 actors in *Inglourious Basterds* were German). It had a track record of films made in Germany. Finally, it had excellent, but affordable, infrastructure.

9. He said that, at €60m a year, the DFFF was not large enough. Germany needed to put more money into bigger films which could be exploited outside the country. He saw finance as a major problem for the industry and said he was looking to develop European finance partners.

10. He mentioned the arrangement which Babelsberg Studios has with producer Joel Silver to take an equity stake in his forthcoming productions made at the studio. He saw this as a way to ensure a continuous flow of work for the studio, but acknowledged that the equity investment constituted a risk.

11. On employment, Dr Woebcken said that he had reduced the number of permanent staff at the studio from 250 to about 85 in order to "stay lean". The company employed about 30 tradesmen (carpenters, plasterers, painters, etc), but could increase this to 300–400 as necessary. He saw this flexibility as essential. He said that Babelsberg employed a number of apprentices in the trades. The government paid for their courses and the studio paid their salaries, which increased over the three year training period.

Meeting with Ulrike Schauz, Head of Division for Film Affairs, Federal Government Commission for Culture and Media Affairs (BKM)

12. The Commission for Culture and Media Affairs is the federal authority responsible for promotion of cultural issues and the development of the general framework for art and culture at the national level. (Under the German Constitution, education and culture policy is the responsibility of the Laender.) In the area of film, the Commission is responsible for developing the policy framework and for the three main federal film funding streams: BKM funding (mostly culturally directed), the Federal Film Board (FFA) funds and the Federal Film Fund (DFFF), on which see below.

13. Ms Schauz said that the main objectives of the BKM's Film Affairs Division were to create the right legal environment for film support, to improve the economic performance of German film, to improve the artistic standing of German film, to strengthen the position of German films abroad and to promote the attractiveness of film production in Germany.

14. She said that the BKM had undertaken a policy review of film support in 2005–06. They abolished their previous tax credit system, which had not been achieving its objectives, and in 2007 established the DFFF. The Fund was

allocated €180m from the federal budget for the three year period 2007–09 for supporting film production through grants. The decision to move to grants was influenced by the need to put a system in place quickly to meet a political promise without having to bring in new legislation. Hungary, the Czech Republic and Austria had followed the DFFF model of providing direct grants.

15. The initial evidence from the scheme was encouraging. The BKM estimated that, for every Euro given in grants, about six euros were invested in the German economy, which was more than they had expected. Bigger projects had produced better results in terms of the positive effect on ancillary industries. There was evidence of increasing know-how transfer, leading to more postproduction work staying in Germany. Babelsberg Studios had been the main beneficiary of the Fund.

16. The DFFF is to be extended for a further three years, 2010–12, at the same rate of €60m a year. There were a few changes to the scheme, but the Cultural Test was unchanged, so they did not expect any problems obtaining agreement from Brussels. There had been discussion of extending the limit on funding per film (€4m) and extending the overall funding to €100m per year. Both were proposed by Babelsberg Studios but rejected. Ms Schauz explained that the limit per film can be extended up to €10m, but only on a decision of the board (viz Speed Racer). Asked how *Speed Racer*, which is based on an American graphic novel, passed the Cultural Test, she mentioned the scene at the Brandenburg Gate and the contribution to employment, but admitted that she was surprised by its score.

17. Ms Schauz mentioned the current legal challenge to the Federal Film Board (FAA)'s levy funding (discussed in detail below). She commented that the challenge to the constitutionality of the levy had been made by the owners of the multiplex cinema chains. This reflected dissatisfaction within the exhibition sector that small cinemas were exempt from the levy but still benefited from the FFA's funding.

18. She said that the impact of the court case had been to delay payments to producers, meaning that some productions had been postponed or abandoned. She hoped the situation would improve in 2010, but the German film industry would continue to be affected by global problems related to the recession. No German banks were currently providing film funding, but the federal government had agreed to facilitate access to finance through the state-owned KfW bank.

19. Ms Schauz said that the shortage of funding increased the importance of co-productions: larger budgets generally meant higher quality films. It was difficult to do co-productions with the UK because the support systems did not match.

Meeting with Peter Dinges, Chief Executive, German Federal Film Board and Constanze Hellmich, Funding Consultant, German Federal Film Fund

20. The Federal Film Board (FAA) was established in 1968 in response to the decline of the Germany film industry in that decade, and following the example of France and Italy, which had introduced film support systems. The role of the FFA is to promote the film industry and the quality of German films to help them achieve success domestically and internationally. The FFA is responsible for administering the FFA fund and the BKM film funds. In addition, the German Federal Film Fund (DFFF) functions as a subsidiary of the FFA.

FFA funds

21. The FFA has a budget of nearly €70m a year. This is raised by a levy on cinema operators, video/DVD retailers and public and private broadcasters. The first two are levied at fixed rates according to turnover, while the broadcasters negotiate individual agreements with the FFA.

22. Mr Dinges said that the benefits of this system were that it was, in effect, a solidarity fund, raising money and distributing it within the industry. It made the funding independent of government, in the sense of not requiring budgetary subventions. It was also self-administering, with members of the industry sitting on the Board.

23. However, the exhibitors had broken this solidarity by challenging the legality of the levy, on the grounds that the different treatment of broadcasters violates the principle of equal treatment in the German Constitution. On 25 February 2009, the highest Administrative court referred the case to the constitutional Court, which is expected to pronounce on the case by mid 2010. In the meantime, the exhibitors have stopped levy payments.

24. Mr Dinges said that the principle of the levy had been accepted by the parties 40 years ago. A deal had been done, whereby the exhibitors accepted the levy and in return had their VAT liability reduced to 7 per cent. They now say that the levy is too high, having apparently forgotten the deal. It has been suggested that, if the exhibitors refuse to pay the levy, they should pay VAT at the full rate of 19 per cent. The exhibitors say that the government would never dare to impose this. So far, they have been proved correct.

25. The FFA's main expenditure is on funding film production in the form of grants and conditionally repayable loans. About half of this is automatic, in the sense that any producer who meets the criteria is entitled. The other half is a rebate to producers, which rewards success. Based on audience figures and awards, money is held on account for producers and can be drawn on to fund their next films. Under the new law, this selective fund will fall from €15m to 10m a year.

26. The FFA also gives financial support for distribution, promotion and marketing, the building and refurbishment of cinemas and film appreciation education for children. The FFA is keen to launch support for digital conversion of cinemas (along the lines of the UKFC's Digital Screen Fund but as a PPP project), but this is difficult at present because the FFA's relationship with the exhibitors is not good.

DFFF

27. The DFFF is the largest provider of film production support, with an annual budget of €60m. It was introduced in 2007, to replace the tax credit system which had ended up financing films made in Hollywood (the so-called "Silly German money) It was initially set to run for three years and is being extended for a further three years.

28. The DFFF supports production of full-length films intended for cinematic release. It provides up to 20 per cent of (accepted) German production expenditure up to a maximum of 80 per cent of the total budget in the form of a grant. There is a cap of €4m per film, though this can be extended to €10m on the decision of the Advisory Board, who consider issues such as skills transfer. Grants are approved on a first come first served basis up to the €60m limit, though this

has not yet been tested in fact. Applicants must be German residents or have a place of business and their project must pass a Cultural Test (similar to the UK tax relief test).

29. Producers may apply for financial support from both the FFA fund and the DFFF (and the Lander) up to a total of 50 per cent of the budget permitted under EU rules. (There is even the possibility of up to 80 per cent funding for projects that are "small and difficult"—not further defined by Brussels.) Average funding intensity of German films is 48–49 per cent.

30. Mr Dinges said that the German Government had made a calculation that, by establishing a fund of €60m and offering grants of 20 per cent, they would attract annual film production expenditure in Germany of around €300m. Of this, they expected €200m to be German films and €100m international films. This had turned out to be a largely accurate calculation, since they had given out €118.5m in the first two years. There had been calls for an increase in the budget for the next three years, but there was no justification for this. If anything, they expect film production expenditure to fall due to wider budgetary constraints brought about by the difficult economic conditions.

31. Overall, he acknowledged that the German film production support system was not the most attractive for big foreign productions. It was simple, transparent and predictable, but it was a compromise. Domestic productions and co-productions were also important. This was particularly so for the FFA funding, which had no requirements about the territory of spend. Last year, 57 of the 180 films supported by the FFA were co-productions.

32. He reiterated the difficulty of doing co-productions with the UK and the loss this represented. He added that co-productions had a psychological effect and said that the cancellation of the UK/Germany Co-production Agreement in 2004 had been a bad sign.

Training

33. Mr Dinges said that there were good film schools in all regions of Germany, covering all areas including special effects. The film industry was involved with the schools and offered positions to their graduates. He said that the main complaint of German companies was that they took graduates of these schools, trained them up (through apprenticeship and other schemes) and then one year later they left Germany to earn more money abroad. Canada was the destination of choice. This trend was not harming Germany's skills base at present, but the next generation of qualified film technicians were in Canada.

34. Mr Dinges commented that this was another outcome of the international competition in subsidies. The UK and Germany had to abide by EU rules on support for their film industries. Canada had no such constraints. He suggested that there was a process underway by which the DFFF grants attracted foreign filmmakers to Germany, leading to a transfer of know how to German technicians, which in turn led them to leave Germany.

The Committee adjourned.

APPENDIX 7: SIX DECADES OF BRITISH TELEVISION HIGHLIGHTS

1950s:

Panorama; Dixon of Dock Green; Quatermass; What's My Line?; The Coronation; Muffin The Mule; The Potter's Wheel; Emergency Ward 10; This is Your Life; The Benny Hill Show; The Army Game; Zoo Quest; Sunday Night at the London Palladium; Hancock's Half Hour; Watch with Mother; Crackerjack; Juke Box Jury; Blue Peter; The Adventures of Robin Hood; Take Your Pick.

1960s:

Maigret; Cathy Come Home; World in Action: 7-Up; Civilisation; The Prisoner; Doctor Who; Coronation Street; Monty Python; That Was The Week That Was; The Forsythe Saga; Man Alive; Culloden; Z-Cars; The Morecambe and Wise Show; Steptoe and Son—(NB also ran 1970–74); Dad's Army; Top of The Pops; Ready Steady Go!; The Likely Lads; Till Death Us Do Part; The Avengers; Danger Man; The Saint; The Magic Roundabout; Thunderbirds; University Challenge; Juke Box Jury (started 1959); Thank Your Lucky Stars; Double Your Money.

1970s:

Fawlty Towers; The Ascent of Man; The Sweeney; Play for Today: Abigail's Party; Law and Order; Not The Nine O'Clock News; Life on Earth; Tiswas; Pennies From Heaven; The Naked Civil Servant; I, Claudius; The World At War; The Family; Monty Python (started 1969, finished 1974); Dad's Army (1968–77); Porridge; Bar Mitzvah Boy; The Knowledge; Grange Hill; Yesterdays Men; Rock Follies; The Old Grey Whistle Test; The Generation Game; Call My Bluff.

1980s:

Brideshead Revisited; Jewel in the Crown; The Young Ones; Screen Two: Caught on A Train; Boys From The Black Stuff; Auf Wiedersehen Pet; Live Aid; Spitting Image; The Edge of Darkness; The Singing Detective; Blackadder; Only Fools and Horses; Arena: The Life and Times of the Ford Cortina; Inspector Morse; EastEnders; Brookside; Yes Minister/Prime Minister; Tumbledown; Real Lives—At the Edge of the Union; Death on the Rock (This Week); A Very British Coup; The South Bank Show; Blind Date; GBH.

1990s:

Absolutely Fabulous; Have I Got News For You; Driving School; Who Wants to Be A Millionaire?; The Royle Family; Video Diaries; The Wrong Trousers; Our Friends in the North; I'm Alan Partridge; Walking With Dinosaurs; Grand Designs; Father Ted; One Foot in the Grave; Hillsborough; Scum; Cracker; Prime Suspect; The Death of Yugoslavia; The Borrowers; Teletubbies; The Word.

2000s:

A History of Britain; The Blue Planet; The Office; State of Play; The Secret Policeman's Ball; Big Brother; I'm A Celebrity Get Me Out of Here!; Hustle; Spooks; Operatunity; Wife Swap; Milkshake; Ant and Dec's Saturday Night Takeaway; Faking it; Mock the Week; X Factor; Britain's Got Talent; The Making of Modern Britain; Top Gear; The Thick of It; Shameless; Life on Mars; Strictly Come Dancing; Footballers' Wives; My Family; Gavin and Stacey; Extras; Skins; Outnumbered; QI; Springwatch; Peep Show; The Weakest Link; Cranford; Little Britain; The Apprentice; Doctor Who; Planet Earth.