



HM Treasury

## Visual effects:

consultation on providing further  
support to the visual effects industry

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# 1

## Introduction

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**1.1** At Budget 2013, the Chancellor announced that the Government would consult on options to provide further support to the visual effects industry through the tax system.

### Policy context

**1.2** The Government is committed to supporting the creative industries, which were identified in the *Plan for Growth*<sup>1</sup> as having the potential to drive significant growth in the UK. This includes providing targeted support for the creative industries through specific spending and tax measures.

**1.3** Since 2007, the film tax relief has provided more than £800 million of support for over 800 British films with a combined production value of £5.5 billion. With the aim of building on the success of the film tax relief, the Chancellor announced the Government's intention to introduce new corporation tax reliefs for the animation, high-end television and video games industries at Budget 2012. These creative sector tax reliefs aim to promote the sustainable production of culturally relevant productions and to incentivise investment into such productions that might not otherwise be made in the UK.

**1.4** The Government consulted on the design of the new tax reliefs over summer 2012<sup>2</sup> and Budget 2013 confirmed the introduction of the animation and high-end television tax reliefs for 1 April 2013, with the video games tax relief to be introduced following State aid approval.

**1.5** As part of its wider ambition to support technological innovation and to help the digital, creative and other high technology industries grow, the Government is now looking to explore options to further support the visual effects industry through the tax system.

**1.6** Alongside the Budget 2013 announcement that it would consult on tax options to support the visual effects industry, the Government also announced additional funding to support digital media production, including visual effects, through:

- the Technology Strategy Board, which will design and launch a new competition of up to £15 million to support digital content production through partnerships with industry; and
- funding for the Skills Investment Fund, which will be increased from the £3 million to £8 million each year over the next two years, with Government match-funding voluntary industry contributions to support skills development in the UK digital content sectors.

### Aims of the consultation

**1.7** The Government is seeking responses from external stakeholders to inform its decision on providing further support for the visual effects industry through the tax system. To inform this work and to support any subsequent implementation, the Government seeks the input of

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<sup>1</sup> Available for download at: <https://www.gov.uk/government/publications/plan-for-growth--5>

<sup>2</sup> See consultation webpage: <https://www.gov.uk/government/consultations/creative-sector-tax-reliefs>

interested parties to develop a detailed and up-to-date evidence base on the characteristics of the visual effects industry. In particular, information is needed on:

- the current size and composition of the UK visual effects industry;
- details of the economic and cultural contributions of the industry;
- any recent trends within the industry; and
- the factors driving any change within the industry and their likely longer term impacts.

**1.8** In addition, this document presents options to provide further support to the visual effects industry using the film tax relief. Views on these options are invited from a wide range of respondents, including individuals, companies, and representative and professional bodies. The Government especially welcomes comments from individuals, companies, and representative and professional bodies working in the visual effects and wider film production industries.

**1.9** The Government will take account of all responses received to the consultation in determining whether to proceed with any subsequent policy changes.

## **Structure of the document**

**1.10** The remainder of the document is set out as follows:

- Chapter 2 sets out the criteria the Government proposes to use in evaluating whether and how to provide further support through the tax system;
- Chapter 3 requests supporting information on the visual effects industry;
- Chapter 4 presents the Government's proposed option to provide further support by using the film tax relief, and seeks views on alternative approaches to support the visual effects industry; and
- Chapter 5 summarises the consultation questions and explains the consultation process.

## **Stages of consultation**

**1.11** The consultation questions in this document are primarily at stage 1 of the Government's tax consultation framework (setting out objectives and identifying options), with some at stage 2 (determining the best option and developing a framework for implementation including detailed policy design).

## **How to respond**

**1.12** Please send comments by 2 July 2013 to:

Visual Effects Consultation,  
Enterprise and Property Tax Team,  
HM Treasury,  
1 Horse Guards Road, London  
SW1A 2HQ

Email: [vfxtax@hmtreasury.gsi.gov.uk](mailto:vfxtax@hmtreasury.gsi.gov.uk).

# 2

## Criteria for assessment

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**2.1** The Government is considering options to provide further support for the visual effects industry through the tax system. The criteria that the Government will use in evaluating proposals to provide such support are set out below. In deciding how to proceed it will be necessary for the Government to consider and balance these sometimes competing factors:

- **effectiveness.** Any proposed policy change must be effective in supporting the visual effects industry to deliver economic and cultural benefits to the UK. Evidence from responses will be used to assess the need for further targeted support through the tax system;
- **affordability.** The proposed change must be affordable, in line with the Government's objective for long term sustainability in the public finances, and represent value for money to the taxpayer;
- **simple and straightforward to administer.** The Government is committed to simplifying the tax system. Any proposed change should not result in unnecessary administrative burdens for businesses or for the administration of the tax system. Any change should be consistent with the low burden approach taken with previously announced creative sector tax reliefs;
- **sustainable and not open to abuse.** Any proposed change must, as far as possible, be designed to fit the way the visual effects industry operates, both now and in the future. Tax reliefs should not create substantial additional avoidance opportunities; and
- **compliance with EU State aid rules.** Any proposed change must be consistent with the principles of the Single Market and will need to gain State aid approval from the European Commission. The State aid guidelines for film and audiovisual works (known as the 'Cinema Communication') set out the parameters for Member States to provide support for the production of film and other audiovisual products with the aim of addressing an identifiable cultural market failure. These guidelines are currently under review<sup>1</sup>. Any proposed changes will need to be achievable in the context of the updated guidelines.

**Question 1:** Do you agree with the proposed criteria for assessing options to provide further support for the visual effects industry through the tax? Please provide any comments as appropriate.

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<sup>1</sup> Further information on the Cinema Communication review is available on European Commission website at: [http://ec.europa.eu/competition/consultations/2012\\_state\\_aid\\_films/](http://ec.europa.eu/competition/consultations/2012_state_aid_films/)



# 3

## Request for supporting evidence

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**3.1** The UK has historically been one of the global centres for visual effects production, and is currently home to a number of world-renowned and award-winning visual effects studios making a significant contribution to British culture. In particular, British studios have a strong reputation for high quality and innovative work and for the existence of a highly skilled workforce. Nevertheless, there have been recent reports of visual effects activity moving overseas, with job losses at a number of UK visual effects companies, and some evidence of UK-based companies looking to open new branches overseas.

**3.2** This chapter request information from stakeholders on the size, composition and characteristics of the visual effects industry, with a particular focus on recent changes and trends within the industry and the factors driving them.

**3.3** This information will feed into the ongoing policy development process, and will also support any subsequent implementation and State aid processes. Previous State aid applications have required a large amount of evidence to be provided to the Commission to gain approval. The Government asks interested parties to provide as much of the evidence requested below as possible.

**Question 2: Please provide information on the current size and composition of the UK visual effects industry.** For example, information on the total number and size of companies, levels of employment, amounts spent on visual effects annually, estimates of total revenues or GDP contribution, and breakdown of activity by market (film, television, video games, advertisements etc.).

**Question 3:** In what ways are visual effects produced in the UK different to visual effects produced in other countries? Please include details of any aspects of UK visual effects that may be identified as culturally distinct to non-UK visual effects.

**3.4** The Government is aware of recent reports of visual effects activity moving overseas, but to date the evidence of any decline within the industry has been largely anecdotal or limited to individual firms. The Government is keen to develop a more detailed, accurate and up-to-date picture of the recent trends within the visual effects industry, and of the factors driving these trends.

**Question 4:** How has the UK visual effects industry performed in recent years, and what have been the main business and wider economic trends? Please provide detailed information or examples, including (but not limited to):

- changes in overall levels of activity and employment within the UK visual effects industry;
- trends in visual effects activity on culturally British films;
- examples of visual effects activity, companies or employment moving overseas, and estimates of the value of this activity; and
- details of British films (particularly large budget films) choosing to spend their visual effects budgets outside the UK.

**Question 5:** What are the three or four main factors that have driven the changes in the visual effects industry that you have identified?

**Question 6:** What impact will these factors have on the UK visual effects industry's ability to contribute to the UK economy and to British culture in the future?

# 4

## Options for support through the tax system

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**4.1** The visual effects sector makes a valuable economic and cultural contribution to the UK, supporting the performance of the wider digital and creative content sectors. This includes the film, animation, high-end television and film industries, which the Government aims to support through its targeted creative sector tax reliefs. This chapter seeks the views of interested parties on an option to provide targeted support via the existing film tax relief.

### **Proposed options: Using the film tax relief to support the visual effects industry**

**4.2** The film tax relief has been highly successful in recent years at supporting investment and production in the UK film sector. In 2011/12 the film tax relief provided more than £200 million of support to over 300 films. It is understood that investment in large budget<sup>1</sup> films has, in particular, had a positive effect on the visual effects industry, with productions such as the *Harry Potter* series and more recently *Inception* providing significant opportunities for UK visual effects companies.

**4.3** However, some industry stakeholders have argued that the current design of the film tax relief places visual effects companies operating in the UK at a disadvantage. They have argued that as a discrete and mobile element of the overall film budget, production companies often choose to shift their visual effects expenditure overseas, or that UK visual effects artists can be placed at a disadvantage due to the structure of film tax relief in the UK. The previous chapter of this document requests further evidence in support of these arguments.

**4.4** Though not committing to introduce any specific change at this stage, the Government is nonetheless keen to receive comments from interested parties on potential options to update the film tax relief with the aim of supporting visual effects works in the UK. These options look to address the structural aspects of the relief.

#### **Proposed film tax relief option 1:**

To offer an enhanced 25 per cent payable credit for large budget films where the vast majority (80 per cent or more) of the film's expenditure on visual effects is qualifying UK expenditure.<sup>2</sup> (See example in Annex A)

**4.5** Currently the maximum payable credit available for large budget films is 20 per cent of qualifying expenditure. Under the proposed option 1, production companies will receive an enhanced rate of relief, worth up to 25 per cent of qualifying expenditure across the whole film budget, where a sufficient proportion of the visual effects budget is qualifying UK expenditure.

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<sup>1</sup> Defined according to the film tax relief definition as films with a production budget of £20 million or more.

<sup>2</sup> Qualifying UK expenditure is defined as 'goods or services which are used or consumed in the United Kingdom'. Further information and guidance on this point is available on the HM Revenue and Customs website at: <http://www.hmrc.gov.uk/films/>

**Proposed film tax relief option 2:**

Decreasing the minimum UK expenditure requirement in Film Tax Relief from 25 per cent to 20 per cent.

**4.6** Currently Film Tax Relief requires that a minimum of 25 per cent of the overall budget of a film is qualifying UK expenditure. Under option 2, this threshold would be reduced potentially allowing more productions to bring qualifying visual effects work to the UK.

**Question 7:** Overall, would pursuing either of these proposed options be an effective way to provide further support for the visual effects industry through the tax system?

**Question 8:** What are the likely economic impacts of introducing either of these options?

**Question 9:** How far would these options support or increase visual effects activity on culturally British films or aspects of films?

**Question 10:** What risks or potential unintended consequences, if any, would the proposed options have for the visual effects or other industries?

**Question 11a:** For large budget films, what proportion of the total production budget is typically spent on visual effects?

**Question 11b:** Are you aware of examples of large budget films that do not include any expenditure on visual effects? If so, please provide details.

**Question 12:** What incentive effect do respondents believe the reduction of UK expenditure requirement will have on visual effect expenditure in the UK?

**4.7** The Government believes that both of these options could represent a potentially effective way to encourage a higher proportion of films benefiting from the film tax relief to carry out their visual effects work in the UK. Nevertheless, further policy development and engagement with businesses and the European Commission will be necessary to establish that this proposal adequately meets the criteria set out in Chapter 2.

**4.8** In meeting the criteria set out in Chapter 2 any potential option must take account of costs to the Exchequer to ensure that the proposal is affordable and represents value for money for the taxpayer. Based on the evidence collated, if the cost of the option proposed were to become disproportionate it could become necessary to consider design options to limit the impact on the Exchequer.

**4.9** One way to do this, under option 1, would be to limit the availability of any enhanced rate to films where the total visual effects budget forms a minimum proportion of the total production budget. This would target the enhanced rate on films containing a minimum amount of visual effects.

**Question 13:** At what level should the minimum proportion of expenditure on visual effects be to qualify for the relief?

**Question 14:** Should there be a minimum visual effects spend threshold and, if so, at what level?

## Identifying visual effects expenditure

**4.10** To ensure the effectiveness of the proposed option 1 outlined above it will be necessary for film production companies to be able to disaggregate expenditure on visual effects from the wider film budget. As it is understood that visual effects represents a relatively discrete part of the post-production budget – which may typically be carried out by a third party – it is expected that this should be relatively straightforward to achieve.

**Question 15:** Is pursuing option 1 likely to introduce any additional administrative burdens for businesses, particularly the need to separate expenditure on visual effects from the wider film budget? If so, please identify and include any cost estimates where possible.

**4.11** Since this consultation is seeking information on the potential effect of such a measure, it is not appropriate to make an assessment of the potential effects of the measure at this stage. If the Government decides to proceed, its assessment of the impacts will be set out alongside the policy proposal.

## Alternative proposals

**4.12** The Government has presented specific options to provide further support for the visual effects industry through the tax system. Nevertheless, the Government would also welcome any alternative proposals, either through the tax system or through non-tax approaches, which stakeholders feel would be of particular benefit to the visual effects industry. Any alternative proposal will need to take account of the assessment criteria set out in Chapter 2. In particular, in addition to delivering economic and cultural benefits, proposals must be simple, affordable and compliant with State aid rules.

**Question 16a:** Are there other areas of the relief that could offer a more appropriate way to provide support, for example should the balance of the cultural test be adjusted to allow more weighting to visual effects? Please describe and explain how this would meet the criteria set out in Chapter 2.

**Question 16b:** What alternative proposals could the Government consider to further support the visual effects industry? Please describe and explain how this would meet the criteria set out in Chapter 2.

**4.13** After the consultation period has closed, the Government will consider the responses to the consultation. In line with the Code of Practice for written consultations the Government will publish a summary of responses to the consultation.



# 5

## Consultation process

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**5.1** The Government welcomes views on the following questions:

**Question 1:** Do you agree with the proposed criteria for assessing options to provide further support for the visual effects industry through the tax? Please provide any comments as appropriate.

**Question 2:** Please provide information on the current size and composition of the UK visual effects industry. For example, information on the total number and size of companies, levels of employment, amounts spent on visual effects annually, estimates of total revenues or GDP contribution, and breakdown of activity by market (film, television, video games, advertisements etc).

**Question 3:** In what ways are visual effects produced in the UK different to visual effects produced in other countries? Please include details of any aspects of UK visual effects that may be identified as culturally distinct to non-UK visual effects.

**Question 4:** How has the UK visual effects industry performed in recent years, and what have been the main business and wider economic trends? Please provide detailed information or examples, including (but not limited to):

- changes in overall levels of activity and employment within the UK visual effects industry;
- trends in visual effects activity on culturally British films;
- examples of visual effects activity, companies or employment moving overseas, and estimates of the value of this activity; and
- details of British films (particularly large budget films) choosing to spend their visual effects budgets outside the UK.

**Question 5:** What are the three or four main factors that have driven the changes in the visual effects industry that you have identified?

**Question 6:** What impact will these factors have on the UK visual effects industry's ability to contribute to the UK economy and to British culture in the future?

**Question 7:** Overall, would pursuing this proposed option be an effective way to provide further support for the visual effects industry through the tax system?

**Question 8:** What are the likely economic impacts of introducing this option?

**Question 9:** How far would this option support or increase visual effects activity on culturally British films?

**Question 10:** What risks or potential unintended consequences, if any, would the proposed option have for the visual effects or other industries?

**Question 11a:** For large budget films, what proportion of the total production budget is typically spent on visual effects?

**Question 11b:** Are you aware of examples of large budget films that do not include any expenditure on visual effects? If so, please provide details.

**Question 12:** What incentive effect do respondents believe the reduction of UK expenditure requirement will have on visual effect expenditure in the UK?

**Question 13:** At what level should the minimum proportion of expenditure on visual effects be to qualify for the relief?

**Question 14:** Should there be a minimum visual effects spend threshold and, if so, at what level?

**Question 15:** Is pursuing this option likely to introduce any additional administrative burdens for businesses, particularly the need to separate expenditure on visual effects from the wider film budget? If so, please identify and include any cost estimates where possible.

**Question 16a:** Are there other areas of the relief that could offer a more appropriate way to provide support, for example should the balance of the cultural test be adjusted to allow more weighting to visual effects? Please describe and explain how this would meet the criteria set out in Chapter 2.

**Question 16b:** What alternative proposals could the Government consider to further support the visual effects industry? Please describe and explain how this would meet the criteria set out in Chapter 2.

## Submitting responses

**5.2** Please send comments by 2 July 2013 to [vfxtax@hmtreasury.gsi.gov.uk](mailto:vfxtax@hmtreasury.gsi.gov.uk) (specifying in the subject line whether your email is an enquiry or a formal consultation response).

**5.3** Alternatively, address responses to:

Visual Effects Consultation,  
Enterprise and Property Tax Team,  
HM Treasury,  
1 Horse Guards Road,  
London  
SW1A 2HQ

**5.4** The Government will also be meeting with stakeholders during the consultation period to discuss their views on the questions set out in this document.

**5.5** When responding please say if you are a business, private individual or representative body. In the case of representative bodies please provide information on the number and nature of people or businesses you represent.

**5.6** Please be aware that all responses may be shared with HM Revenue and Customs and the Department for Culture, Media and Sport.

## Confidentiality

**5.7** Information provided in response to this consultation, including personal information, may be published or disclosed in accordance with the access to information regimes. These are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004.

**5.8** If you want the information that you provide to be treated as confidential, please be aware that, under FOIA, there is a statutory Code of Practice with which public authorities must comply

and which deals with, amongst other things, obligations of confidence. In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on HM Treasury.

**5.9** HM Treasury will process your personal data in accordance with the DPA and in the majority of circumstances this will mean that your personal data will not be disclosed to third parties.

## **Consultation Principles**

**5.10** This consultation is being run in accordance with the Government's Consultation Principles. The Consultation Principles are available on the government website:  
<https://www.gov.uk/government/publications/consultation-principles-guidance>

**5.11** The Government's Consultation Principles state that "timeframes for consultation should be proportionate and realistic". This consultation will run for six weeks, which should be sufficient time for stakeholders to consider and respond. A longer consultation is not considered necessary given the scope of the issues the Government is looking to explore with interested parties.

**5.12** If you have any comments or complaints about the consultation process please contact:

Amy Burgess,  
Consultation Coordinator,  
Budget Team,  
HM Revenue and Customs,  
100 Parliament Street,  
London  
SW1A 2BQ

Email: [hmrc-consultation.co-ordinator@hmrc.gsi.gov.uk](mailto:hmrc-consultation.co-ordinator@hmrc.gsi.gov.uk)

**5.13** Please do not send responses to the consultation to this address.



# A

## Illustrative example of an enhanced payable credit

### Illustrative example of how the proposed enhanced 25 per cent payable credit could work

The following is a simple worked example to illustrate how the film tax credit could be calculated for a film production company qualifying for enhanced relief under the proposed option.

A film production company makes a film with a core expenditure of £100 million, all of which is UK expenditure. The film was commissioned by an unrelated distributor which pays £85 million for it.

The visual effects budget for the film is £15 million, all of which is spent in the UK. All of the UK expenditure therefore qualifies for the enhanced 25 per cent tax credit:

Total income	£85m	
Total expenditure	(£100m)	
<b>Pre-tax relief profit/ (loss)</b>		<b>(£15m)</b>
Enhance-able expenditure	£80m	
(core expenditure of £100m x 80%)		
Additional deduction		(£80m)
(100% rate of enhancement x £80m)		
<b>Post-tax relief profit/ (loss)</b>		<b>(£95m)</b>

The surrender-able loss is the lesser of:

- the post-tax relief trading loss of £95 million; and
- the enhance-able expenditure of £80 million.

The film production company can surrender any amount up to £80 million of losses. The amount of credit due based on a payable credit rate of 25 per cent multiplied by the loss surrendered (assuming the maximum of £80 million is surrendered) is  $25\% \times £80m = \mathbf{£20m}$ .

This compares with **£15.8 million** that would otherwise be available.





### **HM Treasury contacts**

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