

ITEM FOR FINANCE COMMITTEE

Head 180 – TELEVISION AND ENTERTAINMENT LICENSING AUTHORITY

Subhead 700 General Non-recurrent

Item 480 Film Development Fund

Members are invited to approve a \$300 million increase in the approved commitment for the Film Development Fund with an expanded scope to finance the production of small-to-medium budget films.

PROBLEM

We need to increase the commitment and expand the scope of the Film Development Fund (FDF) to strengthen support for the film industry.

PROPOSAL

2. We propose to increase the commitment of the FDF by \$300 million from \$20 million to \$320 million to –

- (a) provide financial support for the production of small-to-medium budget films; and
- (b) continue to finance projects which are beneficial to the healthy and long-term development of the film industry.

/JUSTIFICATION

JUSTIFICATION

Need to Strengthen Support for the Film Industry

3. The film industry is a flagship of the creative industries in Hong Kong. It significantly contributes to the development of tourism and services industries, and enhances the international and cultural image of Hong Kong. However, there has been a substantial drop in the number of film productions as well as box office revenues in recent years. In 2006, only 51 local films were released with a total box office of \$282 million, as compared with its peak of a production volume of over 300 films a year during the early 1990s and a box office of \$1,240 million in 1992. With a shrinking film market and decreasing number of local productions, the film industry is facing a very difficult time, plagued with talent drought and related problems.

4. Knowledge-based economies such as the UK, France and South Korea generally regard the film industry as an important growth engine that creates job opportunities, vibrant businesses and amiable cultural environment. They also see the need for some form of government support to give an impetus to the industry. For example, the South Korean Government invested a total of KRW130 billion (around HK\$800 million) in 33 film funds between 1999 and 2004, spurring venture capital and other companies to invest in the film industry.

5. Against this background, the Government considers that there is a need to strengthen support for the film industry through a host of measures, assisting it to further develop and compete with overseas counterparts in the globalised environment. One notable measure is to increase the commitment and expand the scope of the FDF.

The Existing FDF

6. The Government first established the FDF for a tenure of five years in April 1999 with an approved commitment of \$100 million¹ to primarily finance projects conducive to the long-term development of the Hong Kong film industry, such as specific training of film personnel, overseas promotion of local films, etc. In March 2005, the Finance Committee approved, among others, to redeploy \$20 million from the Film Guarantee Fund (FGF) (see paragraph 26 below) to revive the FDF so as to sustain the momentum of promoting the film industry.

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¹ Recognising that the film industry had difficulties in obtaining loans from lending institutions to finance film production and there was an uncommitted balance of \$59.3 million, the Finance Committee approved in 2003 to deploy \$50 million from the FDF to launch the Film Guarantee Fund.

7. The FDF is administered by the Film Services Office (FSO) of the Television and Entertainment Licensing Authority (TELA), with the Commissioner for Television and Entertainment Licensing (CTEL) serving as the controlling officer. A project vetting committee chaired by the Permanent Secretary for Commerce, Industry and Technology (Communications and Technology) and comprising members from film industry and other professions has been set up to assess applications and recommend CTETL to approve the applications and disburse funds, prescribe the terms and conditions of funding, and monitor the progress and results of the funding projects. Successful applicants are required to submit reports and audited accounts upon completion of their projects for the project vetting committee's consideration. CTETL cannot approve any project costing more than \$10 million each. For projects that merit funding support but cost more than \$10 million, CTETL would refer the projects to the Finance Committee for approval.

8. From April 1999 to March 2004, the FDF received a total of 155 applications and approved 72 projects with a total funding of \$48.75 million. From April 2005 to February 2007, the revived FDF received a total of 21 applications and approved 13 projects with a total funding of about \$15 million. The remaining balance of the existing FDF stood at about \$5 million as at 31 March 2007. As these projects have helped enhance the competitiveness of the film industry, we consider that the FDF should continue to fund projects of such nature in future (see paragraph 10(b)-(d) below).

Injection of \$300 Million into the FDF

9. The film industry has been suffering from low output of film productions, particularly small-to-medium budget films. This has seriously depleted talents in the industry from screenwriters to directors. There is a genuine need for the Government to continue to assist in the sustainable development of the local film industry through the FDF. In the 2007-08 Budget, the Government has earmarked \$300 million for establishing a fund to help finance film production and overcome the shortage of talents. We propose to inject this sum into the FDF.

Enlarging the Scope of the FDF

10. Following an injection of \$300 million, we propose that the FDF should fund projects and activities which contribute towards the development of the Hong Kong film industry, including –

- (a) limited funding support for small-to-medium budget film productions;

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- (b) enhanced efforts to promote Hong Kong films in the Mainland and overseas;
- (c) enhanced initiatives to train talents in the various aspects of the film production and distribution; and
- (d) enhancing the interest and appreciation of Hong Kong films by the local audience.

Financing Small-to-medium Budget Film Productions

11. The reduction in film productions, particularly those of small-to-medium budget, is one of the key areas identified by an independent consultant engaged by the former Film Development Committee that require immediate attention and limited financial support from the Government. We therefore propose to finance film productions with a budget not exceeding \$12 million by contributing up to 30% of the production budget, i.e., a maximum of \$3.6 million per film. The funding support proposed is expected to encourage more commercial investment in film productions, especially those of small and medium size, and create a larger mass of film activity and employment opportunities.

Encl. 1

12. When funding small-to-medium budget film productions, we have drawn references from the existing FGF and propose a set of criteria at Enclosure 1. The broad parameters are that only small-to-medium budget productions employing certain number of Hong Kong talents should be funded, and the proposed film production should be up to a standard for commercial theatrical release. There will also be some assessment in relation to commercial viability of the film project (e.g. 50% undertaking of budget by third-party financier(s), objective assessment on whether the film is for mass appeal rather than only niche market), soundness of the applicant (e.g. a company registered in Hong Kong with certain track record) and reasonableness of the proposed budget, etc. There will be no vetting of the content of scripts of the film productions.

13. The film industry, an important and unique industry contributing to Hong Kong significantly in tourism and services industries (see paragraph 3 above), is facing a difficult time. We consider limited government funding support for film production an appropriate measure to assist it to revitalise and further develop. The proposed funding support for film productions would only focus on small-to-medium budget film productions to help create more film productions and job opportunities for film talents. The Government's contribution would be capped at 30% of the production budget, the remaining 70% of which would be funded by private investors. Such limited support strikes a balance between the need

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to revitalise the film industry and the need to keep the Government's assistance to an absolutely necessary level. We will review the effectiveness of the FDF in two years' time (see paragraph 22 below).

Supporting Other Projects

14. The FDF with an increased commitment will continue to adopt the existing eligibility and assessment criteria at Enclosure 2 when funding film-related projects under paragraph 10(b)-(d) above.

Encl. 2

CONTROL MECHANISM

Vetting Committee

15. CTEL will continue to be the controlling officer of the FDF, with the Secretariat of the Film Development Council (FDC) (see paragraphs 23 and 27 below for more details) administering the FDF. CTEL will decide whether to approve the applications and disburse funds based on the recommendations of a reconstituted Vetting Committee, set up under the FDC and comprising some members of the FDC and co-opted members from the film sector and other professions². The new Vetting Committee will be responsible for evaluating the merits of applications for funding from the FDF that falls within its enlarged scope in paragraph 10 above.

16. In respect of film productions under paragraph 10(a) above, as the assessment criteria set out in Enclosure 1 contain certain subjective elements, the Vetting Committee will be assisted by experts drawn from a Panel of Examiners, who are professionals with experience in film production, financing, etc. and who will provide their views for consideration by the Vetting Committee. As for other projects under paragraph 10(b)-(d) above, the Vetting Committee will evaluate them against the criteria in Enclosure 2. The Secretariat of the FDC will ascertain the facts contained in the applications and offer administrative support to the Vetting Committee. Clear guidelines will be set out for the examiners and the Vetting Committee to declare and avoid any possible conflict of interests.

/Disbursement

² Since one of the duties of the new Vetting Committee is to evaluate the commercial viability of applications for film financing, we propose that government officials should not take part in it.

Disbursement of Funds

17. Funds for film productions under paragraph 10(a) above will be disbursed to successful applicants by installments, tying with appropriate milestones or on a pro rata basis with other private investors. Terms and conditions will be specified in the form of undertakings duly signed by successful applicants before the release of the first installment of funds, which would clearly set out the relationship between the successful applicant, third-party financier(s) and the Government, and their respective obligations and liabilities, and that the Government's liability in each film will be capped by the Government's contribution. Final installment of the disbursement of the fund will only be released upon the completion of the production of the film. Successful applicants are required to submit reports and audited accounts within a certain period after the completion of their productions to the Secretariat of the FDC for monitoring and vetting purposes.

18. Funds for projects under paragraph 10(b)-(d) above will also be disbursed in installments and successful applicants must submit reports and audited accounts upon completion of their projects to the Secretariat of the FDC for monitoring and vetting purposes.

19. The Vetting Committee will advise on the uses of the FDF, monitor fund disbursement and evaluate fund expenses upon completion of all film productions and film-related projects under paragraphs 10 (a)-(d).

Cost Recouping and Profit Sharing for Film Productions

20. When the FDF contributes to a film production under paragraph 10(a) above, the Government will require cost recouping and profit sharing on the film commensurate with the Government's share of contribution in relation to other equity investors on a pari passu, pro rata basis. This will be prescribed in the contract which the Government would enter into with the successful applicant and third-party financier(s) of the film. The contract would specify clearly the Government's contribution, and that the Government would be entitled to the proceeds of the film through a share of all the copyrights underlying the film³. The cost recouped and profit shared will be credited to the General Revenue of the Government. There is a chance of the Government not recouping all or part of the

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³ Revenue-generating avenues of a film are derived from the underlying copyrights of the film. Such avenues include: box office through theatrical release, video release, television broadcasts, spin-off and title rights, etc.

contribution if the proceeds from all revenues for the Government's share of contribution cannot cover the contribution. In cases where there is no real prospect of recouping the contributions, or where further proceeds to be attained from the relevant copyrights are envisaged to be very small and would not justify the administrative costs entailed by continuing to hold on to the copyrights, relinquishing the copyrights by, e.g. selling back to the production company, may be the best option. The Government will therefore have the discretion to relinquish the copyrights, but only upon advice of the Vetting Committee and/or valuation by independent experts some time after the film is commercially released.

21. For effective monitoring, successful applicants for funding film productions are required to set up separate account for all fund of the film, including the Government's contribution and private investment. They are also required to regularly report to the Secretariat of the FDC, which will prepare accounting records and monitoring reports to the Vetting Committee for monitoring the proceeds derived from the films.

REVIEW

22. We propose to review the FDF in consultation with the film industry two years after the injection of \$300 million and enlargement of the scope of FDF as proposed above. We will assess the effectiveness of the expanded FDF in creating a larger mass of film production activities, increasing employment opportunities, nurturing film talents and enhancing Hong Kong's overall image, etc. We will involve the FDC in carrying out the review, and inform the Legislative Council Panel on Information Technology and Broadcasting of the review outcome.

FINANCIAL IMPLICATIONS

23. We propose to increase the commitment of the FDF, with an expanded scope to fund productions and projects in paragraph 10 above, from \$20 million to \$320 million. The administration of the expanded FDF will necessitate enhanced support by the Secretariat of the FDC, which will be transformed from the FSO. In this connection, the Finance Committee will consider the proposal to create the non-civil service position of Secretary-General of the FDC at the equivalent rank of D2 for two years at its meeting on 6 July 2007, to which the Establishment Sub-committee has no objection. The Secretariat of the FDC will also be strengthened by the addition of two permanent civil service posts, namely, one Senior Executive Officer and one Personal Secretary I. The additional staff cost for the increase in manpower is about \$3.4 million per year. We have included sufficient provision in the 2007-08 Estimates under Head 180 – TELA to meet the expenditure.

24. The proposal has no implications for fees and charges for services provided by the TELA.

PUBLIC CONSULTATION

25. We consulted the Legislative Council Panel on Information Technology and Broadcasting on 17 April 2007, which had invited members of the public and the film industry to attend the meeting and give their views on this proposal and the proposed expansion of the FDF. Members raised no objections except they opined that there should be no vetting of scripts when applications for funding the productions of small-to-medium budget films are considered. In view of this, the Administration has removed the requirement of script vetting in the eligibility and assessment criteria.

BACKGROUND

26. Over the years, the Government has been implementing a host of support measures to promote the development of the film industry, including funding support (such as the FDF and FGF⁴), promotion (such as trade fairs) and trade facilitation arrangements (such as the Mainland-Hong Kong Closer Economic Partnership Arrangement) to open up overseas and Mainland markets for Hong Kong films, protection of intellectual property rights, investment in infrastructure in digital technology, etc.

27. The Government will continue with its efforts that are relevant to support the film industry. In April 2007, we established the new high-level FDC, mainly comprising members from the film industry, to advise the Secretary for Commerce, Industry and Technology (the Secretary for Commerce and Economic Development with effect from 1 July 2007) on all matters relating to the

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⁴ FGF aims to facilitate film production companies' access to film financing through the provision of loan guarantee. We will retain the FGF in order to sustain the Government's assistance in developing the local film financing infrastructure for the time being, and the FDC will be invited to conduct a comprehensive review of the long-term need for the FGF. We aim to complete the review in 2008-09. In any event, a production company, producer or director cannot receive financial support both from the FDF and the FGF for the production of a film.

development of the film industry (including nurturing talents, promoting Hong Kong films on the Mainland and overseas, etc.), and will advise the Government on the administration of the FDF as well as implementation of other support measures.

Encl. 3

The terms of reference and membership of the FDC are at Enclosure 3.

Commerce, Industry and Technology Bureau
June 2007

**Proposed Eligibility and Assessment Criteria for Financing Film Productions
under the Expanded Film Development Fund**

It is proposed that the Film Development Fund with an expanded scope should adopt the following eligibility and assessment criteria for financing film productions –

- (a) The applicant should be a film production company formed and registered under the Companies Ordinance (Cap. 32) that should normally have produced at least two films in the past ten years for commercial theatrical release in Hong Kong. For companies without such track record, the producer or director of the film project in question should normally have produced or directed at least two films in the past ten years for commercial theatrical release in Hong Kong;
- (b) Generally, an applicant is allowed to receive funding for not more than two film projects at any one time. For this purpose, if a producer is currently involved in two approved film projects which are under production, any applications involving this producer will not be considered. However, if a film director is currently involved in one approved film project which is under production, any applications involving this director will not be considered;
- (c) The film project must –
 - (i) be in the form of a full script to produce a feature film intended for commercial theatrical exhibition in Hong Kong with a production budget of not more than \$12 million;
 - (ii) be identifiable as commercially viable and have secured some form of third-party financing of , for example, 50% of production budget; and
 - (iii) constitute at least 50% of the main cast and film crew with Hong Kong permanent residents.

Eligibility and Assessment Criteria for Funding Projects under the Existing Film Development Fund

The existing Film Development Fund adopts the following eligibility and assessment criteria for funding projects –

- (a) An applicant should normally be a locally registered institution/organisation engaged in film business or a related body. The Film Services Office (which will be reconstituted as the Secretariat of the Film Development Council) can also apply for funding.
- (b) Projects under application must be beneficial to the overall development of the local film industry, such as enhancing the competitiveness of the local film industry.
- (c) Benefits accrued from the projects must serve the interests of the entire film industry, and not just an individual private company or a consortium of private companies.
- (d) Projects should mainly be non-profit making by nature. Special consideration could be given for projects that can ultimately be self-financing.
- (e) In general, funds approved can only be used for non-recurrent expenditure.
- (f) Funds approved cannot be used to create any civil service posts.
- (g) In examining an application, the following must be taken into consideration –
 - (i) the benefits that a project may bring to the local film industry;
 - (ii) the need for such a project;
 - (iii) the technical and project management capabilities of the applicant institution/organisation;
 - (iv) whether the implementation schedule of the proposed project is well planned and whether the time required for implementation is reasonable;

- (v) whether the proposed budget is reasonable and realistic;
- (vi) whether there is/will be any duplication in terms of the work carried out by other institutions; and
- (vii) for a project involving recurrent expenditures (such as salaries and other administrative expenses), the period required for such expenditures and whether the project can be self-financing after a certain period of time.

Film Development Council

Terms of Reference

To advise the Secretary for Commerce, Industry and Technology (the Secretary for Commerce and Economic Development with effect from 1 July 2007) on –

1. the policy, strategy and institutional arrangement for the promotion and development of the film industry;
2. the use and allocation of public funds in support of the film industry;
3. the planning, co-ordination and implementation of publicly funded activities related to the film industry;
4. the merits of applications for public funding under the relevant funding schemes;
5. the manpower and training needs of the film industry; and
6. the promotion of film literacy in the community.

Membership (for the term from 15 April 2007 to 31 March 2009)

Chairman : Mr. Jack SO Chak-kwong, J.P.

Vice Chairman : Permanent Secretary for Commerce, Industry & Technology (Communications and Technology)
(Permanent Secretary for Commerce and Economic Development (Communications and Technology) with effect from 1 July 2007)

Members : Mr. Gordon CHAN Ka-seung, M.H.
Mr. CHAN Wing-mei
Ms. Mabel CHEUNG Yuen-ting
Mr. Felix FONG Wo, J.P.
Mr. Crucindo HUNG Cho-sing, B.B.S.
Mr. Bill KONG Chi-keung
Ms. Terry LAI Siu-ping
Mr. Peter LAM Kin-ngok
Mr. NG See-yuen, B.B.S., J.P.
Mr. John SHAM Kin-fun
Ms. Nansun SHI
Mr. SUEN Kwok-lam, M.H.
Mr. WONG Chi-keung
Mr. Raymond WONG Pak-ming
Mr. WONG Ying-wai, J.P.
Secretary for Home Affairs or his representative
Executive Director of Hong Kong Trade
Development Council or his representative