



HM Treasury

Consultation on additional tax relief for visual effects costs

Summary of responses

October 2024

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Foreword

The Creative Industries play a key role in driving economic growth, generating £124.6 billion in gross value added in 2022 and supporting over 2 million jobs. They offer a distinct cultural contribution to the UK, represent our values globally and help foster connections between communities.

The Government is dedicated to supporting the sector and will introduce a Creative Industries sector plan as part of its Industrial Strategy. This will help to generate high-quality jobs and boost growth in film, music, gaming, and other creative fields.

The UK is a world-leading centre for visual effects production in film and TV. Our industry is exceptionally innovative and dynamic, with cutting edge visual effects techniques increasingly used in gaming, advertising and other sectors. The Government is proud of the growth and global acclaim the industry has achieved since Film Tax Relief was introduced by the Labour Government in 2007.

In March 2024, it was announced that from 1 April 2025, film and high-end TV programmes will be able to claim an enhanced Audio-Visual Expenditure Credit (AVEC) rate of 39% on their UK visual effects costs. AVEC's 80% cap on qualifying costs will also be lifted for UK visual effects costs.

This Government will legislate to introduce these changes. This will address a longstanding concern from the industry that AVEC's 80% cap drives visual effects work away from the UK, and these changes will boost the UK's offer for visual effects in a competitive international environment.

I am grateful to the visual effects industry and wider film and TV sector for the constructive engagement they have provided on the design of the additional tax relief.

James Murray MP

Exchequer Secretary to the Treasury

Chapter 1

Introduction

Background

1.1 Visual Effects or “VFX” is the digital manipulation of images to enhance, augment or replace elements of live-action shots in films and TV. It is an intrinsic part of many feature films and many TV dramas.

1.2 The UK has historically been a strong performer in visual effects production and is home to several Oscar-winning visual effects studios. British studios are world-renowned for their high quality, innovative work, as well as their highly skilled and talented workforce.

1.3 Nevertheless, there have been reports of visual effects activity moving overseas. To provide the government with a better understanding of the strengths and challenges facing the UK visual effects sector, a call for evidence was launched on 22 November 2023 and closed on 10 January 2024.

1.4 Respondents agreed the UK visual effects sector is highly successful and has experienced steady growth in recent years. Many respondents highlighted the UK’s strong reputation for excellent skills and deep expertise in visual effects.

1.5 However, many respondents also highlighted increasing competition from other countries for visual effects work and noted that the UK’s film and high-end TV tax relief regime has become less attractive to production companies since some jurisdictions have introduced visual effects-specific tax incentives. Respondents highlighted the visual effects tax incentives offered by Canada, France and Australia as being particularly attractive to production companies considering where to place visual effects activity.

1.6 In March 2024 it was announced that from 1 April 2025, film and high-end TV programmes will be able to claim an enhanced Audio-Visual Expenditure Credit (AVEC) rate of 39% on their UK visual effects costs. It was also announced that AVEC’s 80% cap on qualifying costs will also be lifted for UK visual effects costs.

1.7 A consultation of the design of the additional tax relief ran from 27 March 2024 to 22 May 2024. The objectives of the consultation were to set out how the additional tax relief for visual effects will work and the types of costs that would be in scope. The government sought views on whether there were any unintended consequences in the policy design so that these may be resolved before the policy was legislated.

Next steps

1.8 These changes will be legislated in the next Finance Bill. The government expects the next Finance Bill will be published in full following the introduction of the Bill and will contain proposed legislation for the additional tax relief.

1.9 This document summarises the main issues raised by stakeholders in their consultation responses and the policy design that the government plans to take forward.

1.10 The government would like to thank respondents for their helpful and constructive feedback and active engagement throughout the consultation, which has helped to inform the policy design.

1.11 The government will continue to work with industry and provide guidance and education about how the additional tax relief will operate.

Commencement of the additional tax relief for visual effects

1.12 Visual effects costs incurred from 1 January 2025 will be eligible for the additional tax relief.

1.13 Companies will be able to claim the additional tax relief from 1 April 2025.

Chapter 2

Key policy decisions

Eligibility requirements

2.1 Film and high-end TV productions claiming the Audio-Visual Expenditure Credit will be eligible for the additional relief. This means film and high-end TV productions will be required to meet the existing eligibility criteria of AVEC, in order to qualify for the additional visual effects tax relief.

2.2 Productions that claim the enhanced 39% rate of AVEC for animated productions and for children's TV productions will not also be able to claim the additional tax relief for visual effects. If they are eligible for both, then they must choose which one they want to claim.

2.3 Productions that claim the Independent Film Tax Credit (IFTC) are not eligible for the additional tax relief for visual effects. If they are eligible for both, then they must choose which one they want to claim. This is because films that qualify for the IFTC will receive generous support for their visual effects costs. All eligible production costs, including visual effects costs, will receive AVEC at the enhanced IFTC rate of 53%, capped at 80% of the production's total qualifying expenditure.

Visual effects costs in scope of the additional tax relief

2.4 The government will legislate the following definition of visual effects for the purpose of the additional tax relief: *visual effects is work consisting of the use of computer technology to create or alter images for the inclusion in the film or programme.*

2.5 This definition is in line with the approach taken by other jurisdictions that offer visual effects tax incentives and with the recommendations of visual effects and the film and TV companies that responded to the consultation.

2.6 Costs associated with the use of artificial intelligence (AI) in the visual effects process will be eligible for the additional tax relief.

2.7 Costs associated with special effects (which are created physically rather than using computer technology) will not be eligible for the additional tax relief.

2.8 Visual effects costs incurred in virtual production will be eligible for the additional tax relief. Other costs incurred in virtual production, such as filming in front of an LED screen, will not be eligible. The

government expects companies to apportion virtual production expenditure so that relief is only given on visual effects costs.

2.9 The government will provide further guidance on the definition in due course.

Administration of the additional tax relief for visual effects

2.10 The additional tax relief will be delivered through the Audio-Visual Expenditure Credit (AVEC). The following steps will be used to calculate the additional tax relief.

2.11 To qualify for the removal of the 80% cap and the 5 percentage point uplift in the credit rate, HM Revenue and Customs (HMRC) will verify that the claimant's visual effects costs are genuine and incurred in the UK.

2.12 When making a claim for the additional tax relief, companies will need to provide HMRC with evidence of the visual effects costs they wish to claim relief on and details of the company that carried out the work. The rest of the claim process is expected to be unchanged from the process for AVEC.

2.13 If a company makes a claim for the relief with an interim certificate from the British Film Institute (BFI), they will receive the normal 34% rate of AVEC on their VFX costs, capped at 80%.

2.14 To claim the 5% uplift in relief and exemption from the 80% cap on qualifying costs, companies must submit a return for the production's completion period. This is the accounting period when the film or programme is complete and the production has received a final certificate from the BFI.

2.15 When calculating the amount of additional relief due, UK visual effects costs should be separated from other production costs. The 80% cap will be applied as normal to non-visual effects costs. The 80% cap will not apply to UK visual effects costs (at Step 3 of section 1179CA CTA 2009).

2.16 At Step 5 of section 1179CA CTA 2009, the relevant percentage for the production's qualifying costs that are UK visual effects will receive an uplifted AVEC rate of 39%. The relevant percentage for other costs will remain at 34%.

2.17 Companies should show the amount of expenditure credit given at each rate in their computations.

2.18 The process of redeeming expenditure credits in section 1179CC CTA 2009 is expected to remain unchanged.

2.19 HMRC will publish further detailed guidance on this process in due course.

Chapter 3

Summary of responses

3.1 A total of 19 responses were received and the government also benefited from several meetings with stakeholders during the process. These included responses from individuals, industry groups, businesses, and accounting firms.

3.2 The overwhelming majority of respondents to the consultation emphasised the success of the UK visual effects sector and the opportunity for the sector to grow and build on its existing strengths in innovation.

Definition of visual effects

3.3 This section covers the government's response to the consultation about government's approach to defining 'visual effects' for the purpose of the additional tax relief.

3.4 The government stated that it would use the British Film Institute's definition of visual effects as a starting point for the legislation. The definition reads as follows:

Visual effects is defined to mean the digital alteration of a film's (or high-end programme's) images. This will include the following activities carried out as part of Asset Build, Shots and Facility Overhead, but not those activities relating to principal photography: Pre visualisation, Concept Design, Computer Generated Images (CGI), Character/Creature Animation, Colour Correction, 2D Compositing, 3D Animation, 3D Modelling, Software Development, Digital Intermediate, Stereo Conversion, Virtual Sets/Studio Motion Capture, Digital Matte Painting, Lighting and Rendering, Images as well as supervision, support and management of the artists and individuals engaged in this activity.

3.5 The government stated that it agreed with the principle that visual effects are the digital alteration of filmed footage. In line with this principle, the government proposed excluding the following types of costs from the additional tax relief:

3.5.1 Special effects: Special effects are created physically rather than digitally.

3.5.2 Generative artificial intelligence (AI): Generative AI will not qualify for the additional tax credit, as it does not involve filmed footage

and therefore does not meet the basic principle of the BFI's guide definition of visual effects.

3.5.3 Animated TV and animated films: films and TV programmes that qualify for the animation tax credit (now part of AVEC) will not qualify for the additional visual effects tax relief. They will only be able to claim AVEC as an animated film/TV programme, under which they will receive an enhanced rate of 39%.

3.5.4 Virtual production: Visual effects costs incurred in virtual production will be eligible to receive the additional tax relief. Other costs incurred in virtual production, such as filming in front of an LED screen, will not be eligible. The government expects companies to apportion virtual production and visual effects costs.

Question 1: Do you anticipate there to be any issues or unintended consequences with the government's approach to defining 'visual effects' for the purpose of the additional tax relief?

3.6 The vast majority of respondents expressed concern with two aspects of the definition: a) the absence of the 'creation' of footage from the definition of visual effects, and b) the requirement that the images being altered must be 'filmed footage'.

3.7 In particular, it was widely commented that it is common for some images in a film or TV programme to be crafted entirely digitally by visual effects artists, with no filmed footage involved. Examples given include an image of a city in the medieval era and an image of a spaceship landing on an imagined alien planet, both of which may need to be created entirely through computer generated imagery.

3.8 Many respondents expressed concern with the government's proposal to exclude costs associated with generative AI. Key concerns expressed include the difficulty in distinguishing between generative AI and non-generative AI costs in the process of claiming the additional tax relief. Respondents commented that AI is a commonly used tool in the visual effects process and has been for several years. Many respondents highlighted the possible negative impact of an exclusion on the attractiveness and international competitiveness of the policy.

Government response

3.9 The government agrees that images that are necessarily entirely created by computer technology should be included in the scope of the additional tax relief.

3.10 Following stakeholder engagement, the government has therefore amended the definition of visual effects for the purpose of the

additional tax relief to the following: *visual effects is work consisting of the use of computer technology to create or alter images for the inclusion in the film or programme.*

3.11 The government will provide further guidance on the visual effects definition in due course.

3.12 The government acknowledges the concerns raised by respondents regarding the proposed exclusion of generative AI costs, including the complexity an exclusion would add to the claims process. The government will not legislate a rule to exclude AI costs from the scope of the additional tax relief.

Comments on policy design

3.13 The government set out the key design feature of the additional tax relief in the consultation:

3.13.1 AVEC's 80% cap will not apply to qualifying UK visual effects costs. This means that even if a company has placed 80% of its non-visual effects production costs in the UK, it can place visual effects work in the UK and still receive the 39% credit rate on that visual effects expenditure. All other types of production costs will continue to be subject to the 80% cap.

3.13.2 Qualifying UK visual effects in film and high-end TV productions will receive a 5 percentage point increase in the rate of tax credit. The total rate of tax credit for UK visual effects expenditure will therefore be 39%. The 39% rate applies to all qualifying UK visual effects costs in a production, regardless of whether the visual effects costs exceed or are below the 80% cap.

3.13.3 Visual effects work must be carried out in the UK for the associated costs of this work to qualify for the additional relief.

3.13.4 The government stated that it would work with the British Film Institute to develop a process for accrediting visual effects costs as genuine and incurred in the UK.

Question 3: Do you anticipate there to be any issues or unintended consequences with the government's approach to defining 'visual effects' for the purpose of the additional tax relief?

Question 2: Do you anticipate there to be any issues or unintended consequences with the government's approach to defining 'visual effects' for the purpose of the additional tax relief?

3.14 The majority of respondents were supportive of the proposed design of the additional tax relief and felt it would achieve the stated objective of the policy, to increase the amount of visual effects work carried out in the UK.

3.15 A small number of respondents suggested that the uplift in tax relief should be higher, on the basis that other jurisdictions offer specific visual effects incentives that are more generous in terms of their credit rate than the UK's proposal.

3.16 Several respondents suggested that the government should legislate that visual effects costs incurred from 1 January 2025 should be eligible for the additional tax relief. Respondents commented this would bring forward investment decisions and help the visual effects sector recovery from the impact of strikes by actors and writers in the US in 2023.

3.17 Some respondents suggested that films which claim the Independent Film Tax Credit (IFTC) should also be able to claim the additional tax relief for visual effects. Respondents felt this would benefit smaller visual effects studios.

3.18 Some respondents commented on the need for the government to ensure that the additional tax relief does not impact the efficiency of how AVEC is currently administrated. Some respondents commented that the government should ensure that the British Film Institute have adequate resource to accredit visual effects as genuine, should the government proceed with this approach.

Government response

3.19 The government believes that the 5 percentage point increase will provide a substantial boost to the competitiveness of the UK's offer for visual effects and lead to more visual effects work being done in the UK. Beyond the headline rate, our incentive compares favourably to other jurisdictions because the additional relief will be available on a wide range of costs. In addition, there will be no additional eligibility requirements that companies must meet to access it. This uplift comes on top of an already generous rate of relief for all other production costs. It will complement the existing strengths of the UK as a destination for visual effects work, including our world-class skills base.

3.20 The government acknowledges the merits of specifying that visual effects costs will be eligible for the additional tax relief if they are incurred from 1 January 2025. The government will put into legislation that costs incurred from 1 January 2025 will be eligible for the additional tax relief.

3.21 Companies claiming the IFTC will not be able to claim the additional relief for visual effects. All qualifying production costs, including visual effects costs, in certified low-budget films will receive an enhanced AVEC rate of 53% under the IFTC. This is a highly generous

rate and the government does not expect the exclusion of certified low-budget films from the additional tax relief for visual effects to have an adverse impact on companies.

3.22 The government is committed to ensuring the efficient administration of AVEC and the additional tax relief for visual effects. The government does not expect the administration of the additional tax relief to impose a substantial additional resourcing on the BFI.

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