

**Games Ireland Submission to
Department of Finance on Review of R&D Tax Credit**



IRELAND
GAMES

Executive Summary

The video game industry today is a unique marriage of innovation and technology that is at the centre of worldwide growth in digital media both on and offline. It is expanding faster than any other part of the entertainment sector and its annual worldwide revenues now exceed those of recorded music and cinema combined¹. The game industry's high annual growth leads to increased employment both in the industry itself and in sectors which serve it such as the software, technology, animation, music, scriptwriting, game console, smartphone and computer industries. Ireland should seize the opportunity to play a leading role in European game development and reap the significant benefits in cross-sectoral employment and innovation that will follow.

The foundation of a successful game industry is game development and not enough game development is happening in Ireland today. The Research and Development (R&D) tax credit is the only tax credit available to the industry in this country covering game development and as presently drafted the credit is narrow to benefit the local games industry. As a result only a small number of games companies have been successful in availing of the credit. This is largely because its parameters excludes ancilliary R&D activities which are key to the development of a video game today.

If Ireland is to build on its undoubted potential to grow and become a European hub for the game industry there must be adequate incentives to encourage game development in this country by local companies both international and indigenous and by companies yet to locate and/or be established here. The key individuals and the companies which employ them and benefit from such incentives will serve as the anchor for the development of tomorrow's games industry in Ireland. Increased game development can only happen with the incentive of an R&D tax credit which is 'fit for purpose' for today's video game industry by covering all relevant R&D activities.

¹ PWC Global Entertainment and Media Outlook 2102-2016
<http://www.pwc.com/gx/en/global-entertainment-media-outlook/index.jhtml>

Games Ireland Submission to Department of Finance on Review of R&D Tax Credit

The International Games Industry

The international video game industry is the most advanced and fastest growing segment of the international entertainment sector. The industry's digital origins and rapid development as a creative, technological and commercial force mean that it now has larger annual revenues than the recorded music and cinema industries combined. It has rapidly evolved over the past thirty years beginning with games played in amusement arcades and on early model computers to games played on personal computers, specialised and continually evolving game consoles, computers and laptops with the greatest growth now coming on portable and handheld devices including iPads and smart phones. On regular occasions the top ten apps sold in the Apple Apps store are game apps².

This rapid development combined with an eagerness to devise new business models has meant that this ground breaking industry is forecast to grow at a compound rate of 8% by 2015³. Although a relatively small number of companies laid the foundations of the modern video game industry, the rapid development that is taking place online and in relation to mobile has meant that the industry now has a much greater number of international participants all of whom can take advantage of rapidly evolving and widely available means of distribution. In theory many of these companies could locate their European headquarters in Ireland and a relatively small number have already done so.

The establishment of a successful games industry in a country can give it the technological and cultural boost required to reinvigorate many related sectors. Countries such as Canada, the United States, Korea and Japan are clear examples of what can happen when government investment in infrastructure and technology, combined with a favorable and incentivised investment environment, create a games industry which has positive knock on effects for related sectors, i.e. encouraging competitiveness in emerging fields such as the cloud, big data, analytics, large scale infrastructure, iOS & Android and other new platforms as well as the established areas of software, technology, design, animation, music etc.

Although the average gamer is frequently perceived to be a young teenager recent studies have confirmed that the average age is actually 30 and 47%⁴ of all gamers are women. In addition the average age of a gamer who purchases content on the internet is now assessed at 34⁵. The industry is therefore continually becoming more universal in terms of content, audience and participants.

The Irish Games Industry

² <http://www.apple.com/euro/itunes/charts/apps/top10appstorepaid.html>

³ PWC Global Entertainment and Media Outlook 2102-2016
<http://www.pwc.com/gx/en/global-entertainment-media-outlook/index.jhtml>

⁴ <http://www.theesa.com/facts/>

⁵ <http://www.theesa.com/facts/>

Games Ireland Submission to Department of Finance on Review of R&D Tax Credit

The Irish industry here has evolved over the last twenty years with most of the growth taking place over the last five years. Although still small (2,800)⁶ the industry is larger than that of some EU countries (eg. Sweden 1500). There are 13 multinational companies established in the country and around 40 to 50 smaller indigenous companies. However the vast majority⁷ of the personnel employed by multinationals in the industry work in areas unrelated to the development of the vital IP of the industry, the video games themselves. Large numbers work instead, for example, in customer care and game localisation. Details of the specific occupations that exist within the industry can be found in a recent Irish study.⁸

In order for the sector in Ireland to grow at the same rate as, for example in the Canadian province of Quebec, it is necessary that more, 'sticky' jobs be created, most of whom would be related to the development of games. These types jobs are the foundation for a successful and thriving games industry and the service industries which support it. As the technology associated with the games industry is more than often 'cutting edge,' as described above, it fits well with most government digital technology objectives. In addition, the ICT and engineering jobs that would be created by an expanding and stable game industry would greatly enhance Ireland's reputation as a place to work and develop creative skills in the ICT sector. The country could become known as a place where all the skills necessary to build a platform or other e-commerce systems would be available.

The shining example of what can be done in relation to game industry growth is, as mentioned above, Quebec, where as a result of carefully targeted government incentives, the game industry has grown from a workforce of 3,500 to a figure of over 20,000 today including several multinational and many local game studios. The Quebecois stimulus for growth originated from the local government's desire in the mid 1990's to re-invigorate the province's high tech industries in the face of growing local unemployment. This jobs initiative was in turn mirrored by similar schemes in other Canadian provinces such as Ontario and British Columbia which resulted in Canada becoming the third biggest games industry in the world after the U.S. and Japan.

Although recent industry growth has been constant, Ireland now has to counter a negative international image arising from the recent economic downturn and also compete with the increasing number of incentives offered by close neighbours (UK, France, Spain) to attract investment, infrastructure and key talent to their countries. If the game industry is to flourish here a more favorable financial environment must be created to stimulate local game development. Many of the jobs in today's technology and game industries did not exist three to five years ago. Therefore if Ireland is to remain competitive in these sectors it must be able to attract the key talented people into this country, as well as nurturing home grown talent. Jobs created was a result would be 'sticky' jobs i.e. high value positions capable of creating up to five additional ancillary/support jobs.

Developing the Irish Games Industry

⁶ <http://www.gamedevelopers.ie/features/viewfeature.php?article=5652> The Games Industry in Ireland 2012

⁷ <http://www.gamedevelopers.ie/features/viewfeature.php?article=5652> The Games Industry in Ireland 2012

⁸ <http://www.gamedevelopers.ie/features/viewfeature.php?article=47>

Games Ireland Submission to Department of Finance on Review of R&D Tax Credit

Games Ireland feels that the Irish game industry will grow fastest by stimulating game development in three main areas:

- a. increasing development by indigenous game companies
- b. encouraging development, or more development by multi-nationals who are already located here
- c. attracting new development-based companies both at home and from abroad

The cumulative effect of growth in these three areas will lead to the creation of hundreds of new development jobs which in turn will lead to the creation of many more spin-off positions both in the game companies themselves and in the companies that provide services to same. It is estimated that the tax incentives which were introduced in Quebec in the 1990s have resulted in double the amount of investment in the local industry in relation in comparison to tax revenue lost. As for our nearest neighbour, the UK, it was estimated⁹ that the soon to be introduced 25% tax break will create 1500 new studio jobs and increase investment in the local industry.

Not enough companies nor most of all, the 'key talent,' the individuals that are developing the games of the future are in Ireland at this time. For the Irish industry to grow those companies and individuals must be attracted to Ireland and we must therefore compete more effectively with current market forces. Introducing an R&D tax credit which is more in tune with the requirements of the game industry would be a big step in the right direction.

The main step that must be taken in this regard is the inclusion of all development-related activities, including ancillary functions, as activities covered by the R&D credit. It is Games Ireland's view that this must be an essential part of any strategy aimed at growing the Irish games industry and so creating stable employment in this country's digital sector.

The Existing Research and Development Tax Credit

The existing R&D tax credit is a 25% tax credit for qualifying incremental R&D expenditure incurred in the current year over and above what was incurred in the base year (an accounting period ending in 2003).

A small number of games companies in Ireland have successfully claimed the R&D tax credit for software development activities. However, there is an ongoing concern within our membership that the R&D tax credit as currently administered does not enable a games company to claim all the key ancillary activities that are essential to attracting the investment to allow for the development of a new game.

⁹ 'Investing in the Future - a Tax Relief for the UK Video Games Development Sector' - TIGA (UK) January 2011

Games Ireland Submission to Department of Finance on Review of R&D Tax Credit

Games are inherently interactive software¹⁰ and development of a new game in the current environment in keeping with the consistent evolution of new platforms and business models increasingly involves the resolution of uncertainty in relation to the viability of that game in terms of gameplay, interactivity and the social media sphere. There is however an amount of ancillary and incidental supporting activity which is integral to the development of a successful game and which is open to question.

How the Current Tax Credit Should be Amended

It is clear that the extent to which ancillary and incidental activities play a critical role in the games industry R&D necessitates clarification to the qualifying expenditure criteria associated with the credit to include these costs. This principle was recognised by the Forfas Games Sector Study “An Action Plan for Growth” (2011) in relation to the social sciences.¹¹

We believe that this can be achieved within the existing legislative framework (i.e. no change of law would be required) through the publication of additional limited Guidance specific to the games industry. For example, if the new Guidance was to allow a Games company (which is undertaking a specified amount of software development activity) to also claim the R&D tax credit on the ancillary activity that is required to support the development of a game a more inclusive and appropriate level of game development activities would be covered. Measures could also be put in place to ensure that the ancillary activity does not outweigh the core software development activity.

Game development is seen as an ‘end to end’ activity by the games industry, with software development being a major part of this (but only one part). However recognition is needed that without the necessary ancillary activity, there will be no end product, no game and ultimately no games industry.

If the above clarification was provided it would ensure greater certainty to the games industry both international and national when considering Ireland as a location for games development. Without this certainty, it is unlikely that significant high end investment will ever be attracted into Ireland.

¹⁰ Dáil Report 05/03/12

Tax Reliefs

181. Deputy Seán Kyne asked the Minister for Finance if, in view of Section 20 of the Finance Bill which extends the tax-relief for the film industry, consideration will be given to extending such relief to the electronic gaming industry so as to encourage indigenous entrepreneurship which would compliment the multi-national presence in Galway and Dublin among other locations. ‘Minister for Finance (Deputy Michael Noonan): Digital games are essentially software development and would already be a field of science and technology for the purposes of the R&D tax credit scheme. Relevant R&D expenditure on games should already qualify under the existing terms of the tax credit scheme, provided any specific games development achieves scientific or technological advancement and involve the resolution of scientific or technological uncertainty. I announced a review of the R&D tax credit scheme in Budget 2013. An invitation for submissions to this review can be found on my Department’s tax policy website (www.taxpolicy.gov.ie).’

¹¹ p 55

Games Ireland Submission to Department of Finance on Review of R&D Tax Credit

Effect of Extended R&D Tax Credit on the Local Market.

An amended tax break as described above if limited to the digital media sector would have a negligible effect on tax revenue within the country whilst having a strong incentivizing influence on investment, innovation and job creation.

Other Territories with Game Industry Tax Incentives

There are several examples where the offer of tax and skills incentives to national games industries have rapidly grown those industries and had substantial benefit for other associated sectors. For example as a result of incentives which exist in several of its provinces, especially Quebec and British Columbia, **Canada** is now the world's leading location for foreign direct investment (FDI) in video games, attracting one quarter of all jobs created worldwide by foreign investors from 2003-2011.

Nearly 100 foreign companies established greenfield FDI projects in the creative industries sector in Canada between 2003 and 2011. FDI in Canada's information and communication technologies (ICT) industry reached an accumulated Euro 15 billion in 2011.¹² Quebec in itself is a good comparator to what could happen in Ireland when a games industry that in 2005 was similar in size to Ireland grew as a result of targeted incentives including a 30% tax credit to support 12,000 employees in 2011.

The **United States** has a range of different video game tax incentives in over twenty states leading to a thriving games industry and the world leader both in terms of market (Euro 5.6 bn) and employment (120,000).¹³

Within the EU, a growing number of countries have seen the value of incentives for the game industry. **France** already has both a tax credit of 20% of expenditure for game development and are now considering yet more incentives.¹⁴ **The U.K.** is about to introduce a new tax credit set 25% of qualifying expenditure with no minimum threshold of expenditure or cap on investment.¹⁵ If Ireland is to compete internationally and avail of the tremendous opportunities that exist for growth in the video game and related sectors, it must introduce an R &D tax credit that is 'fit for purpose' for today's game industry.

¹² <http://investincanada.gc.ca/download/839.pdf>

¹³ <http://www.theesa.com/games-improving-what-matters/economy.asp>

¹⁴

¹⁵ <http://www.digitalspy.ie/gaming/news/a443228/uk-games-industry-to-benefit-from-25-percent-tax-relief-rate.html>

Games Ireland Submission to Department of Finance on Review of R&D Tax Credit

Table 1. Cost/Benefit Analysis to Revised R&D Tax Credit

Set out below is a rough estimate of the cost/benefit to the State of a revised R&D credit as described above:

1. Creation of 1000 incremental “sticky” mid-level jobs (including the software development and ancillary jobs) @ €100k per person
2. Total related investment in headcount salary = €100m
3. Total R&D tax credit (on all jobs) = €25m
4. R&D tax credit related to “ancillary activity” (assuming 49% of total headcount) = €12.25m
5. Payroll tax (assumed @ mean rate of 35%) = €35m capacity

Net income to State after Tax Credit = €10m

(plus positive ripple effect on other related sectors)

Market Distortion/Market Failure

1. The continuous evolution of the games industry as games are developed for and enjoyed on an increasing number of fixed and portable devices results in much greater competition. This in turn leads to a greater need to innovate and resolve uncertainty. All of these factors together with the comparatively small size of Ireland’s game industry now and into the future also mitigate against any Market Distorting effect that might be caused by a revised R&D credit.

2. As an example of the type of Market Failure in the current conditions we cite the recent case of a local thriving development-led company and former Games Ireland member based in central Dublin which was closed last year by its parent company. A growing and innovative games company with talented staff was lost from Ireland and the in-house jobs simply moved overseas to a more competitive employment market. Had there been a ‘fit for purpose’ and inclusive R & D credit in place these jobs would most likely have remained in Ireland. It is also likely that other FDI companies would have by now been carrying out more games development in Ireland in addition to supporting customer care and localisation activities.

Games Ireland Submission to Department of Finance on Review of R&D Tax Credit

Administration of Tax Credit

Games Ireland are aware that administration of a revised R&D tax credit may require additional administration resources. We are happy to nominate representatives to serve on any panel or assist in any procedure that will assist in formulating and administering a revised R&D tax credit structure.

Conclusions

Not enough of the companies and most of all, the 'key talent,' the individuals that are developing the games of the future are in Ireland at this time. For the Irish industry to grow those companies and individuals must be attracted to Ireland and we must therefore compete more effectively with current market forces.

Introducing an R&D tax credit which is more in tune with the requirements of the game industry would be a big step in the right direction. Including the ancillary activities associated with game development within the activities covered by the R&D credit is the clear step that should be taken and must be an essential part of any strategy aimed at growing the Irish games industry.

Games Ireland hopes that the Department of Finance will agree that the parameters of the current R&D tax break should be revised accordingly by way of new Guidance.

Games Ireland

Games Ireland represents companies involved in the creation, development, publishing and distribution of computer games on the island of Ireland. We are an advocacy group seeking to drive sustainable growth in the industry at a crucial time for this country. We want to create better awareness of the Irish Industry as it stands, and to lobby for initiatives that could help grow the local indigenous industry, as well as expand the scale and scope of the international industry activities in Ireland. Our members include international stakeholders such as Activision, BigFish, Microsoft and Riot as well as local pioneers including Havok, Demonware and Digit. Our overall objective is to ensure rapid local industry growth over the next five years placing Ireland at the forefront of European game development.

April 12 2013

**Games Ireland
Dublin Exchange Facility
St. George's Dock
IFSC
Dublin 1**