

STATES OF JERSEY



£200,000 GRANT TO FILM COMPANY (P.A.C.2/2013): RESPONSE OF THE MINISTER FOR ECONOMIC DEVELOPMENT

**Presented to the States on 7th June 2013
by the Minister for Economic Development**

STATES GREFFE

**£200,000 GRANT TO FILM COMPANY (P.A.C.2/2013): RESPONSE OF THE
MINISTER FOR ECONOMIC DEVELOPMENT**

Ministerial Response to: P.A.C.2/2013

Ministerial Response required by: 6th June 2013

Review title: £200,000 Grant to Film Company

Introduction

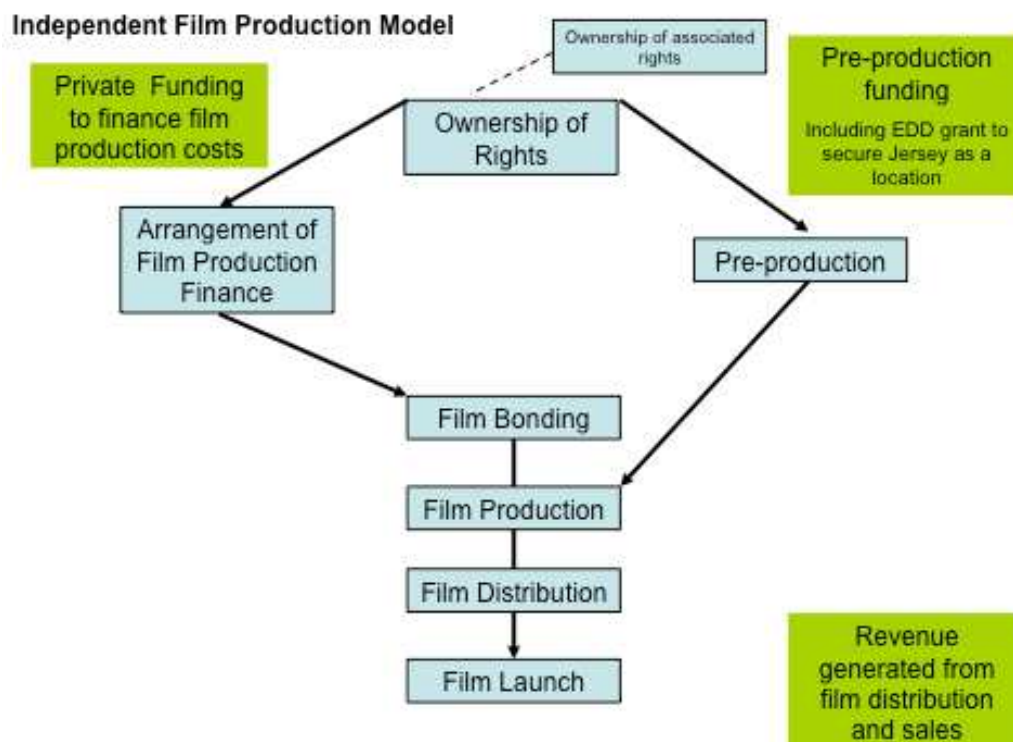
This review relates to a grant of £200,000 provided to a film company. The review has been confined to the process undertaken by the Economic Development Department only.

EDD response to introduction

EDD's response to the findings and recommendations of the Public Accounts Committee (PAC) review of the grant to Canbedone Productions Limited are included below. Whilst the review has focused in the main on process, the review has, in part, addressed broader issues that should benefit from a response from the Economic Development Department (EDD).

The Minister for Economic Development and EDD are charged with growing and diversifying the Jersey economy to create employment across a broad range of sectors. For many years there has been a call for Jersey to follow other smaller jurisdictions, such as the Isle of Man, and secure significant involvement in the film production sector including, but not limited to, establishing Jersey as a location for film production. Our competition (such as the Isle of Man) supports this activity through financial support given either through fiscal incentives or through direct grant assistance. Therefore any conclusion that government support for pre-production activity is somehow novel and contentious is not borne out by the strategies and policies adopted by our competition, including other Crown Dependencies. This is the strategic context within which the EDD grant to Canbedone Productions Limited was made.

To place EDD's response in context, it is important to understand the process of independent film production. The diagram included below, which was supplied to the Public Accounts Committee (PAC) seeks to do this:



In basic terms, in the early stages of a project, independent film production follows a twin-track approach. Pre-production activity, which along with other film industry investment, the EDD grant supported encompasses, but is not limited to, writing and editing the script and the screenplay, selecting locations, defining filming schedules, discussing involvement with potential cast members, preparing initial costings and outlining the cash-flows and commercial returns that, in the event of success, the film would generate. In parallel, the production team seeks investment to allow the film to be produced – in this case from the UK, the USA and China. These are parallel processes and EDD’s grant funding for the Knights of Impossingworth was solely aimed at the pre-production element of the process, and not the process of securing sufficient finance to allow the film to be brought to production. In doing so, the EDD objective was to secure Jersey as a location for the elements of the film to be shot.

The following extract from the House of Lords Communications Committee – “First Report The British Film and Television Industries” dated 14th January 2010 summarises film financing –

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

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

As this response is being written, EDD continues to work with Canbedone Productions Limited to ensure that film production begins in early course. To this end, the CEO of Venture 3D, one of the pre-production co-investors active in the efforts to secure financing for the production from China and elsewhere will be visiting the Island from the USA in mid-June to review progress. Despite the adverse publicity generated by coverage of the PAC report, Jersey locations still features heavily in the film production schedule. EDD hopes that the Knights of Impossingworth provides the catalyst for the development of a broader creative industries sector in the Island and welcomes PAC’s comments in this regard.

The Minister for Economic Development and EDD thanks and compliments PAC on the review. What follows is a detailed response to the findings and recommendations. In preparing this response, the Minister and the Department would like to thank officials from Treasury and Resources and the Chief Minister’s Department for their assistance and input.

FINDINGS

	Findings	Comments
5.12	There was no reference within the Financial Report and Accounts 2011 to the initial grant being part of a multi-year grant.	<p>The Financial Report and Accounts report the States’ overall out-turn position; and the grant expenditure for the Economic Development Department (EDD) for 2011 is included in ‘Grants and Subsidies payments’ in the Consolidated Operating Cost Statement and separately in EDD’s Operating Cost Statement in the Annex to the Accounts.</p> <p>The current level of disclosure in the Financial Report and Accounts with regard to grants is transparent, and was consulted upon with the Chair of the Corporate Services Scrutiny Panel. Significant grants (i.e. grants of £100,000 and over) are disclosed in a Note to the Accounts, and grants below £100,000 are shown in Appendix 1 of the Annex to the Accounts. Whilst not all information can be included in the Statutory Accounts, the Note and Appendix set out the purpose of the grant</p>

	Findings	Comments
		and for all significant grants year the Strategic Priority supported. The relevant MD (MD-E-2011-0104) published on the States website (www.gov.je) clearly states that the grant was for the sum of £200,000.
9.3	The Ministerial Decision confirming the grant was signed only after the first tranche of the grant (£50,000) had been paid.	Not agreed. The EDD Ministerial Decision giving approval for payment was signed on 19th August 2011. Whilst the process to facilitate payment (which could have been stopped at any time prior to payment) was instigated on 11th August, the Order was only approved and receipted on 23rd August 2011 and the cheque issued on 26th August 2011. N.B. There is no central requirement for an MD for expenditure of this nature – the MD in this case, as with many other elements of EDD expenditure, is an additional step in the governance process, introduced by EDD, to ensure that the Minister is fully informed of, and in agreement with, budget allocation.
9.6	The grant had been paid to a different company from that stated in the Ministerial Decision.	Agreed. However, the principal of Canbedone (Jersey) Limited and Canbedone Productions Limited (a UK-registered company) are the same person, and EDD files contain contracts that define the ongoing relationship between the two. The change in corporate identity resulted in no change to the grant or changed the nature of the project in any way. Taxpayers' money was not put at risk as a consequence of the change in corporate identity.
9.9	The contract between EDD and Canbedone Productions Ltd. was not signed until some 3 months after the first payment was made to the company.	The contract with Canbedone Productions Ltd. was signed by Canbedone Productions Ltd. on 23rd November 2011, by EDD on 24th November 2011; and the first payment to Canbedone Productions Limited was made on 6th December 2011, some 2 weeks after the contract was signed.
9.13	The first payment was made to Canbedone Productions Ltd. without any contractual conditions having been effected.	As explained above, the first payment made to Canbedone Productions Ltd. was raised on 6th December 2011. The contract was signed on 23rd November 2011.

	Findings	Comments
9.15	The second tranche of the grant (£75,000) was made without regard for confirmation of the funding milestones as required in the contract.	Not agreed. Clause 2.2 of the “Conditions of Grant” states that the second payment of £75,000 will be made “ on January 1st 2012 or upon confirmation being received of a £3 million funding commitment to the film from Jersey investors ...”. 1st January was the latest date the payment could be made. N.B. Due to public holidays, payment was made on 4th January 2012.
9.21	The contract was poorly written and executed, and left the Jersey taxpayer exposed to undue risk.	Not agreed. As detailed in the introduction to this response, funds were advanced to cover the cost of pre-production expenditure with the objective of securing Jersey as a location for the production. Significant in Island activity in the period Q2 2011 to date, including identification of filming locations, etc. highlighted in the PAC’s report supports the fact that this activity has been undertaken. In addition, the director has been resident in the Island in this period, and with 100% of his time being occupied with pre-production activity, this supports the fact that the objectives of the grant have been met. The risk that, in the absence of funding, no element of the production would be secured in Jersey has been mitigated, allowing Jersey taxpayers to realise a return on the investment of the grant funding.
9.24	The requirements of Ministerial Decision MD-E-2011-0104 were not properly reflected in the contract between the Economic Development Department and Canbedone Productions Ltd., notably a stipulation that the grant monies were to be expended in Jersey.	Accepted. It could have been clearer in the contract that the intention was for the majority of expenditure to be spent on Island. However, given the international nature of the film production industry, it would have been unreasonable to expect ALL expenditure to be undertaken in Jersey. It is clear that the majority of pre-production activity has been undertaken in Jersey. Clauses in the contract, such as Clause 5, clearly indicate that EDD would regularly monitor expenditure. The fact this was done is evidenced by the record of numerous meetings, e-mails and reports from Canbedone Productions Ltd. Contrary to the PAC’s assertion, evidence provided to the PAC (i.e. a document on file submitted to them) titled: “Expenditure June 2011 to Dec 2011” shows actual vs. forecast expenditure.

	Findings	Comments
9.30	The Economic Development did not maintain inspection of Canbedone Productions financial records prior to the Public Accounts Committee hearing, and this poor financial governance left the Department exposed.	Not agreed. EDD commissioned an initial financial investment appraisal from BDO in 2010 as an integral part of the process through which the grant was awarded. Subsequently, through numerous meetings, e-mails and reports, EDD closely monitored expenditure and activity on the project. This regular contact, in effect close account management, represents good governance above and beyond that which would be achieved by simply receiving written reports. At the Public Hearing, the Chief Executive Officer of EDD gave a commitment to ensure the PAC had a report that was completely up-to-date. This should not be taken to imply that EDD did not closely monitor activity and expenditure on the project earlier in the process.
9.33	There is no clear indication as to whether monies have been expended in Jersey as per the Ministerial Decision MD-E-2011-0104.	Not agreed. Evidence submitted to PAC in a document on file entitled: "Expenditure June 2011 to Dec 2011" sets out how monies were spent in this period. This document demonstrates that monies were expended in Jersey.
10.9	There is no evidence of anything having been done by the Department in response to concerns raised by persons familiar with the film industry about the bona fides of the project, although the Department accepted that such concerns had emerged.	Not agreed. Documentary evidence of a file note prepared after a conversation with said persons was included in the files submitted to PAC. In addition, EDD do not consider that the person "familiar with the film industry" was in a position to make any objective criticism of the film, having no direct involvement whatsoever with the project. It is difficult to understand why PAC placed any weight on this evidence, particularly in the light of comments on the quality of the production included in evidence from Tesco Stores and several well-known personalities from the film and entertainment industry, who were familiar with the production. In addition, despite requests, PAC refused to allow EDD access to information supplied by the third party.
10.15	The production of 'Knights of Impossingworth' is a high-risk project.	The PAC presents no evidence for this conclusion and has apparently made no attempt to analyse the range of EDD investments (made in the form of grant funding) against a risk profile. As indicated to the PAC in the response to the draft report

	Findings	Comments
		<p>circulated to EDD for comment, EDD invests in a broad range of projects with a spectrum of risk. It was pointed out to PAC that it was important to put this investment into context, in that the 2011 grant of £50K represents 0.28% of EDD budget, and the 2012 investment of £150K represents 0.84% of EDD budget. As EDD is c.3% of States expenditure, the total investment of £200K represents 0.03% annualised States expenditure. In many cases, risk can be quantified and managed, but cannot be fully mitigated. The potential benefits to Jersey of a successful outcome (evidenced by precedent from other jurisdictions and academic research) justified the investment of a small minority of EDD funds.</p> <p>Furthermore, the contract provides sufficient conditions prior to payments to limit the risk and/or claw back if required.</p>
10.19	Due diligence on the key figures was not undertaken.	From the outset, the director's professional credentials were assessed through IMDB, the comprehensive, credible, internationally recognised and publically available database of the film industry. In addition, during the process of approval and during the period of the stage payments, extensive contact and communication was made by EDD with the director and his associates to establish the continued fidelity of the director and the production. Although the evidence in files submitted to the PAC did not include any printouts of such an assessment, this was discussed during the public hearing.
10.22	The due diligence into the company was materially insufficient.	Not agreed. EDD were very encouraged by the involvement of Tesco Stores Limited and others at the early stages. As highlighted to PAC, the Minister for ED, the Chief Officer and other EDD officers discussed the specific matter of due diligence with senior representatives of Tesco Stores Ltd., and subsequently EDD officers met with Tesco Stores Ltd. representatives whilst undertaking EDD's due diligence on the project. It is important to state that EDD did not rely on the due diligence undertaken by Tesco Stores Ltd.; rather, EDD saw the Tesco Stores due

	Findings	Comments
		diligence process as complimenting work undertaken by both EDD officials and BDO. It is clear from evidence presented to the PAC and given at the Public Hearing that the company was established for the purpose of producing the film and, as such, would not have a lengthy trading history – this is typical of independent film production activity. Furthermore, evidence submitted to the PAC highlighted the total level of co-investment in pre-production activities from parties in the film production industry.
10.30	The due diligence undertaken by Tesco Stores Ltd. was for a different purpose than that of the Economic Development Department, however, it was used as part of the Economic Development Department's decision to go ahead.	Not agreed. PAC would be confident of the level of due diligence undertaken if they had contacted Tesco Stores Ltd. or, indeed, the director, as urged to by the CEO of EDD at the Public Hearing. This would have ascertained the nature, scale and scope of Tesco Stores Ltd.'s due diligence. It is wrong to suggest that this due diligence was “for a different purpose”. The due diligence was on all aspects of the film production and its commercial potential. The issue of the nature of the investment that resulted from this due diligence is a completely separate matter.
10.33	The due diligence undertaken by BDO for the Department was not for a grant of £200,000 to be provided to Canbedone Productions Ltd.	The due diligence undertaken by BDO was on the initial proposal from Canbedone (Jersey) Limited of an investment of £2 million. BDO stated however, that their comments still applied to the revised proposal of a £200,000 grant. The documentation presented to PAC was on all aspects of the film production and its commercial potential. The issue of the nature of the investment that resulted from this due diligence is a completely separate matter.
10.38	No ‘Know Your Client’ process was undertaken by the Economic Development Department.	As mentioned in the response to 10.19 above, from the outset the director's professional credentials were assessed through IMDB, the internationally recognised database of the film industry. In addition, during the process of approval and during the period of the stage payments, extensive contact and communication was made by EDD with the director and his associates to establish the continued fidelity of the director and the production.

	Findings	Comments
10.40	Financial Directions do not require full due diligence to be undertaken when dealing with grants.	Financial Direction 5.1 requires due diligence to be undertaken, and this was undertaken by EDD. Financial Direction 5.5 – Management of Grants, which is supplementary to FD 5.1, covers additional requirements relevant to the grants application and approval process. As part of the process, departments must require potential grant recipients to outline the controls they will operate to ensure that public money is spent in a proper manner and for the purposes intended. In addition, potential grant recipients are required to demonstrate that their corporate governance arrangements are robust, and must provide an explanation of the governance framework for inclusion in the Service Agreement where the grant is subsequently approved and is greater than £100,000.
11.5	The dates of the relevant documentation and the fact that key but basic financial information was obtained from the company by the Department only after the Committee had requested it indicates clear non-compliance with Financial Direction 5.4.	The accounts confirm additional non-EDD investment in pre-production. At the Public Hearing, the EDD CEO gave a commitment to ensure the PAC had a report that was completely up-to-date. This should not be taken to imply that EDD did not have knowledge of basic financial information and, in particular, its correct accounting treatment prior to the PAC’s request.
11.14	The grant was not paid from budgeted funds, but from a windfall surplus from funds, including TV licence fees, paid by Jersey residents.	<p>Agreed, but PAC’s findings fails to reflect evidence available in the public record.</p> <p>In August 2011, in accordance with States processes, the Minister for Treasury and Resources made Ministerial Decision MD-TR-2011-105 (“Carry forward and Digital Switchover Income to 2012”). EDD then has the ability to spend this in a manner deemed appropriate in line with departmental objectives.</p> <p>The following extract from the Ministerial Decision MD-TR-2011-0105 (that allocated the funds to EDD) refers. Relevant sections are shown in bold text below.</p> <p>The Department has proposed the following as the uses of the additional income –</p>

	Findings	Comments
		<ul style="list-style-type: none"> ● Provision of matched or seed-corn funding for key priority initiatives in the new Economic Growth Strategy focused on IT, media, E-commerce, Tourism and renewable energy, namely: <ul style="list-style-type: none"> ○ E-Commerce Commission ○ ICT Strategy ● Promotion of Jersey as a location for technology testing, particularly in ICT and Broadband ● Support of future Development and maintenance of broadcasting, communications and digital economy legislation and policy (including broadcasting and wireless telegraphy) in Jersey, to secure future economic advantage for local businesses and the population ● Greater exploitation of newly introduced legislation in areas such as E-Commerce, E-Gaming and intellectual property ● Mapping and developing on-island capacity in the media/creative industries, through the creation of a network capable of servicing local and off-Island requirements ● Delivering, in conjunction with the Skills Executive, against the potential to create future employment opportunities for young people within the tourism, broadcast, media, e-commerce or wider creative industries ● Marketing Jersey to outside media interests as a location for film/TV making, media conference hosting and future development of e-commerce/creative industries focused events. <p>It is unlikely that all of the additional income will be spent in 2011. EDD has therefore requested that it be allowed to carry forward the unspent amount into 2012 so it can be used for the purposes that the Department feels are appropriate.</p>

	Findings	Comments
		<p>PAC are incorrect in their finding as, at the time the grant was made, EDD's net revenue expenditure budget contained funds transferred as per MD-TR-2011-105.</p> <p>For information, the additional income added to the EDD net revenue budget by virtue of MD-TR-2011-105 is comprised of 2 components:</p> <ol style="list-style-type: none"> 1. Wireless Telegraphy Licence fees are collected by OfCoM on behalf of the States under authority of legislation including the Communications (Jersey) order 2003. A proportion of these monies have been passed to the States. 2. Digital Switchover Surplus. At the outset of the recent Digital Switchover, the BBC was allocated a sum of money out of the licence fee revenues to help the over-75s, the blind and partially sighted and those with serious disabilities, to get digital TV. However, the total cost of this exercise was lower than anticipated. As a result, some of the surplus funding was returned to the UK and Channel Islands governments. <p>Evidence supplied to PAC clearly demonstrates that allocation of such funds to projects within the EDD portfolio is governed by individual Ministerial Decisions. As mentioned in the response to 9.3 above, there is no central requirement for an MD for expenditure of this nature – the MD in this case, as with many other elements of EDD expenditure, is an additional step in the governance process, introduced by EDD, to ensure that the Minister is fully informed of and in agreement with budget allocation.</p>
12.7	There is a claw-back clause within the contract, but there are concerns as to its enforceability in practice against the recipient company (which is a UK company).	EDD thank PAC for its helpful observation in this area. The documents used and this contract is one of a number of standard template documents utilised by EDD. The Department will seek the Law Officers' advice on the provisions in the contract relating to claw-back.

RECOMMENDATIONS

	Recommendations	To	Accept/ Reject	Comments	Target date of action/ completion
5.13	The Financial Report and Accounts must make reference to the Ministerial Decision where a grant entry is part of a multi-year grant project.	TS*	Accept	Treasury will in future make it clear where a single grant commitment is to be paid over multiple years. Treasury agrees with the statement made by PAC in their report which states that “the Financial Report and Accounts document [is] not the place for fuller descriptions of the grants on an individual basis”.	
9.25	In every case where the grant is for a high-risk endeavour, following the application process, legal advice should be obtained in relation to the terms of the contract.	EDD	Accept	Agreed. Subject to a definition of “high risk” and resources available within the Law Officers’ Department, EDD will seek Law Officers’ advice on the provisions of their standard grant contract documentation.	
9.31	The Treasurer of the States must ensure that all departments have a precise framework for the proactive management of contracts to ensure robust monitoring, guaranteeing that evidence is obtained where clauses permit.	TS*	Already in place	Financial Direction 5.5 – Management of Grants, stipulates that details of any conditions attached to the grant and criteria for measurement of whether those have been fulfilled are to be documented in a Service Agreement for all grants over £25,000. The Agreement must also include arrangements for repayment of grants in the event of non-performance or non-compliance. In addition, organisations in receipt of a grant of over £5,000 are required to provide a Grant Assurance Statement confirming how the grant was spent and the outcomes achieved in comparison with the original terms of the grant.	
10.41	The Treasurer of the States must include due diligence requirements within Financial Direction 5.5.	TS*	Accept	Due diligence requirements are already covered in FD 5.1, but Treasury accept that further clarification as to the relationship between 5.1 and 5.5 would be	

	Recommendations	To	Accept/ Reject	Comments	Target date of action/ completion
				beneficial. Treasury will consider amending Financial Direction 5.5 to cover due diligence and make it incumbent on departments to carry out pre-grant due diligence assessment on organisations applying for a grant of over £100,000. The due diligence process will cover investigation into an organisation's governance framework and financial health, and its capacity to manage activities funded by the grant.	
10.42	A guidance note should be introduced to all departments for robust contract management aligned to financial directions.	TS*	Already in place	Departments are directed to the procurement toolkit, where information relating to contract management is available. Consideration will be given to providing additional guidance in this area in relation to grants.	
10.43	Prior to Ministerial Decisions being signed, Accounting Officers must sign a compliance statement to say that Financial Directions have been complied with.	TS*	Not accepted	<p>There is an obligation to comply with Financial Directions and the Public Finances Law at all times. On the basis that this framework already exists, it does not seem appropriate to also sign a separate statement, particularly given the number of Grants and Ministerial Decisions made by the States.</p> <p>Departments are required to report on non-compliance with Financial Directions as part of their annual Statement on Internal Control, and Internal Audit also perform work on key risk areas, including non-compliance.</p>	
10.46	SEB must put specific procedures in place to deal with those who fail to comply with Financial Directions.	CMD		CM	

	Recommendations	To	Accept/ Reject	Comments	Target date of action/ completion
12.8	Should delays continue after 30th September 2013, the claw-back clause must be activated.	EDD		If no material progress on the production has been made by 30th September 2013, consideration will be given to invoking the claw-back clause.	

*Treasurer of the States