

Draft for a model of tax-based cultural promotion in the field of interactive electronic works

A. Issue and objective

Digital games have become a mass medium: half of Germans play computer and video games. The stories and characters from computer and video games have impacted generations and influence our aesthetics and social discourse. The stories underlying many computer and video games hark back to ancient tales and sagas, which they reinterpret. For example, the Polish worldwide games success ‘The Witcher’ is based on old Polish fairy tales. Computer and video games set global trends. The worldwide prevalence of Japanese anime and manga culture has been driven above all by the dominance of Japan in the development of games. At the same time, the media of film, books and games are becoming increasingly interrelated. Literary works are used as the basis for video games, successful games titles are turned into films and typical gaming perspectives are seized on as new staging opportunities in films. In addition to the influence of games on other media, on our culture and our aesthetics, we have also seen a rise in social and cultural engagement with the medium, its manifold narrative forms and its development. Museums across the world – such as the Museum of Modern Art (MoMA) in New York – and in Germany now hold games exhibitions. And computer and video games are by no means only a medium for what are known as the ‘digital natives’.

Computer and video games are a contemporary cultural form of expression and generally acknowledged to be a cultural asset. They take up the issues of our time and enable us to experience them in a unique way. Games are a primary digital medium and a form of cultural expression of the digital society. Today, their technologies and interactive mechanisms are used far beyond the cultural and entertainment sector, for example in the automotive industry, the health system, training and further education and journalism. However, thus far the political discourse about computer and video games has centred largely on regulation and the prevention of consumption, but not on the promotion of creative diversity and new, high-quality games.

There has not yet been any strategically orientated promotion of games development by the German government. The annual recognition of the best games by the German Computer Games Awards is the only acknowledgement. To date there has been no strategic government funding source that supports the development of digital games that promote cultural diversity and pursues a long-term vision for the medium and Germany as a development location.

Conversely, numerous countries inside and outside Europe, such as the UK, France, Finland and Canada, have been systematically and sustainably promoting the production of games, for example through tax incentives or wage subsidies. In Germany, the cultural value and the substantial potential of the sector have long been underestimated. Additionally, the development costs on all platforms on which computer and video games can be played (PC, console, online and mobile) have increased hugely over recent years, meaning that frequently German studios are unable to afford the development costs for elaborate games titles due to the resources that this requires.

As a result, the titles that make a serious impact on gaming culture are rarely produced in Germany. Overall, Germany is losing influence as a development location. Recently, the revenue share of games development based in Germany fell to just 6.5 per cent. Germany is a large market for the sales of computer and video games, but remains a small production location. The number of jobs – an above-average number of which, as compared to the culture and creative economy, are permanent positions subject to social insurance contributions – has only seen small rises recently, whilst the market for computer and video games has experienced double-digit growth. Thus, the development curve of the computer and video games industry in Germany runs counter to the general trend given that the games sector is the media sector with the strongest growth.

Despite these bad omens, some – mainly young – German companies have risen to international prominence over the past years. At the same time, many young developer teams have recently set up their own studios in Germany. These are regarded as being particularly creative and innovative; and some of these studios only gained attention for the first time at the German Computer Games Awards, for instance. However, measured against the growth of the market as a whole, the potential of the games sector in Germany is far too frequently left untapped. There is currently no funding that enables the studios to survive once they have been set up.

Without effective countermeasures, German games risk falling behind in the development of this medium of the future on the international stage. This would necessarily also involve the loss of influence over the development of the principal medium of the digital society. Other locations will necessarily shape the medium. This would also see the loss of a varied development landscape and thus also cultural diversity in the development of computer and video games. Further, there would be a risk of many creative jobs being lost.

Now is the time to act to prevent the German computer and video games industry from succumbing to the permanent supremacy of individual locations such as North America, Japan

or South Korea and their associated cultural dominance. The German film sector had to work very hard before it was able to start breaking up rigid international structures and the concentration on productions from Hollywood and to set its own visible features as a production location. This needs to be headed off in the computer and video games industry at an early stage.

The primary aim of this draft model is therefore to use tax-based funding to lower the production cost of interactive electronic works that promote cultural diversity and by doing so safeguard the development of high-quality games in Germany. The aim of a calculable improvement in the financing situation is to facilitate new scope for artistic invention, increase the quality of games developed in Germany and, by doing so, increase their attractiveness and distribution. Reducing the costs of the production of computer and video games is key to enabling more games to be developed in Germany and cultural diversity in the market for computer and video games to be preserved as a result. Small, mid-sized and large development studios should profit equally from the financial incentives as they all interact to guarantee the diversity of the medium. It is especially important that small and young development studios benefit, even though these have no or no significant taxable revenue. Through the creation of new financial scope and greater financing security, developer studios in Germany should be enabled to explore new artistic paths and realise new ideas and concepts.

By improving the financial situation of the development studios, overall investment volumes in the computer and video games sector should be expected to increase, which in turn should result in better utilisation of the developer studios and their service providers. The long-term effect of this will be to establish an independent, creative and successful German and European games culture, which will safeguard the jobs of many creatives.

B. Solution

The introduction of a cultural promotion bonus for expenditure relating to the development of interactive electronic works that promote cultural diversity, by offsetting these costs proportionately against the liability for corporation or income tax. This means either that the tax liability can be reduced or, if the cultural promotion bonus exceeds the income tax payable, a direct payment will be made. Eligibility for funding will be demonstrated by a positive culture test. Developer studios that manage and are responsible for the development of a game from Germany will be eligible to apply.

The development of computer and video games involves the interaction of a wide range of different technical and artistic disciplines: The development of a video game is a highly complex process that renders budgeting and scheduling very complicated; changes to the

project plan are part of the business. In order to have a long-term impact, a tax-based funding system needs to cater for these volatile development conditions, and it needs to be manageable and also predictable and reliable in practice. Funding via the tax system guarantees this. The tax-based funding mechanism envisaged in this draft model will benefit young and small developer studios just as much as mid-sized, mostly owner-managed German studios and is also suited to making Germany more attractive for long-term investments and new locations in Germany by international market players.

C. Alternatives

None.

D. Costs

Tax shortfalls and the anticipated medium-term additional tax and social insurance contribution receipts still need to be quantified.

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Article 1

Amendment of the German Income Tax Act (EStG)

Under Section 35 b of the German Income Tax Act (EStG) in the version of the announcement dated 8 October 2009 (Federal Law Gazette I pp. 3366, 3862) as amended by Article 7 of the act dated 31 July 2016 (Federal Law Gazette I p. 1914), the following new Subsection 6 is inserted:

‘6. Tax reduction for expenditure relating to the creation of interactive electronic works

Section 35 c

Tax reduction for expenditure relating to the creation of interactive electronic works

(1) 1As regards expenditure relating to the creation of an interactive electronic work, the standard income tax will be reduced upon request (cultural promotion bonus)

1. by 25 per cent of the eligible expenditure as defined at Section 35 d Paragraph 2 (eligible expenditure) for income from commercial companies as defined at Section 15 Paragraph 1 Sentence 1 Number 1,

2. by 25 per cent of the proportional eligible expenditure as defined at Section 35 d Paragraph 2 (eligible expenditure) for income from commercial operations as a partner as defined at Section 15 Paragraph 1 Sentence 1 Number 2 or as a personally liable shareholder in a partnership limited by shares (*Kommanditgesellschaft auf Aktien*) as defined at Section 15 Paragraph 1 Sentence 1 Number 3.

2In the cases of Sentence 1 Number 1, the cultural promotion bonus will only be granted to a taxpayer who is responsible for managing the creation and shaping of the interactive electronic work (eligible party). 3In cases where Sentence 1 Number 2 applies, the prerequisite of Sentence 2 shall be deemed satisfied if it pertains in the event of a partnership or a partnership limited by shares; the eligible party is the partner or the personally liable shareholder in a partnership limited by shares.

(2) 1The cultural promotion bonus may only be claimed if the place of business in which the creation of the interactive electronic work takes place is located in the European Union or the European Economic Area. 2The taxpayer, or, in cases of Paragraph 1 Sentence 1 Number 2 the partnership or partnership limited by shares, must also operate a place of business in Germany from where responsibility for managing and shaping the creation of the interactive electronic work is handled.

(3) 1In the case of partnership as defined at Section 15 Paragraph 1 Sentence 1 Number 2, or in the case of partnerships limited by shares as defined at Section 15 Paragraph 1 Sentence 1 Number 3, the proportion attributable to the individual partners or personally liable shareholders shall be determined separately and uniformly. 2The proportional allocation of the cultural promotion bonus to a partner is based on his or her share of the profits of the partnership in accordance with the general profit distribution scheme; advance dividends shall not be taken into account. 3The proportion of the cultural promotion bonus shall be calculated as a percentage rounded to two decimal places.

(4) The cultural promotion bonus may only be claimed if:

1. The eligible expenditure as defined at Section 35 d Paragraph 2 for the creation of an interactive electronic work exceeds 200,000 euros by publication,
2. the prerequisite of the cultural test pursuant to Section 35 e Paragraph 6 Sentence 4 is satisfied and

3. there are no indications that it poses a risk to young people as defined by Section 15 of the German Protection of Young Persons Act (JuSchG). Such indications shall be deemed not present in particular if the interactive electronic work is awarded a classification as defined at Section 14 Paragraph 2 of the German Protection of Young Persons Act or, in the view of a recognised institution of voluntary self-regulation pursuant to Section 19 of the Interstate Treaty on the Protection of Minors (JMStV), is suitable for one of the age groups set out in Section 5 Paragraph 1 Sentence 2 of the Interstate Treaty on the Protection of Minors.

(5) The total amount of the cultural promotion bonus over the eligibility period shall be limited to the sum of 5 million euros per interactive electronic work (maximum sum).

(6) If the cultural promotion bonus exceeds the actual amount of payable income tax, the excess amount shall be payable to the eligible party.

(7) 1Cumulation with other financial assistance granted in the context of the creation of the interactive electronic work is permissible. 2If the sum of the cultural promotion bonus and other financial assistance granted in the context of the interactive electronic work exceeds 50 per cent of the eligible expenditure as defined at Section 35 d Paragraph 2, the cultural promotion bonus will be reduced such that it together with the financial assistance granted for other purposes constitutes a maximum of 50 per cent of the eligible expenditure as defined at Section 35 d Paragraph 2.

Section 35 d

Definitions and eligible expenditure

(1) 1Interactive electronic work as defined at Section 35 c Paragraph 1 refers to a computer program that is based on a games idea, reacts to user input, generates moving image content, serves educational or entertainment purposes and is intended for publication. 2Interactive electronic works include computer and video games in particular. 3Alongside the production, the creation of an interactive electronic work also comprises the further development of the interactive electronic work after its publication; the costs of the further development are eligible for funding up to the amount of the overall eligible costs for the production of the interactive electronic work to which the taxpayer is entitled under Section 35 c Paragraph 1 and Paragraph 3.

(2) 1The following expenditure is eligible, provided it is incurred in connection with the production of the interactive electronic work:

1. Staff expenses, provided the services giving rise to this expenditure are rendered in the European Union or the European Economic Area;
2. set-offs for the depreciation of movable assets attributable to the place of business as defined by Section 35 c Paragraph 2; if the entire service life of these movable assets is not dedicated to the production of the interactive electronic work as defined at Paragraph 1, only such depreciation occurring during the project as determined using standard accounting principles shall be deemed eligible;
3. costs for hiring third parties who are resident in the European Union or the European Economic Area for the production of the interactive electronic work up to a maximum amount of 50 per cent of the total eligible expenditure;
4. costs for the transfer of the right of use or the right to utilise rights, in particular copyright and industrial property rights, relating to commercial, technical, scientific and similar experience, knowledge and skills;
5. costs of system and application programs;
6. costs of the verification of the interactive electronic work, including costs of acquiring users for the testing and analysis of the interactive electronic work;
7. general costs.

2Eligible expenditure as defined at Sentence 1 only includes such costs defined at Section 4 Paragraph 4 that are not covered by Section 4 Paragraph 5.

Section 35 e

Certification and procedure

(1) 1A certificate in compliance with the following paragraphs confirms that the precondition of Paragraph 6 Sentence 4 is satisfied. 2The financial authorities will be bound by the certificate.

(2) 1After the application is made, a provisional certificate is granted if it can be assumed that the preconditions of Paragraph 6 Sentence 4 will be satisfied. 2The provisional certification must be revoked if the eligible party has not demonstrated that the work has been published within five years of the application being made. 3After publication, a final certificate will be granted to the applicant if the preconditions of Paragraph 6 Sentence 4 are satisfied.

(3) The German government may transfer the certification check to a suitable institution.

(4) 1A decision on the application for certification must be made within three months of receipt of the application. 2If the applicant does not receive a decision by this deadline, the application shall be deemed approved.

(5) The taxpayer shall bear the costs of certification.

(6) 1During certification a culture test regarding the interactive electronic work must be performed. 2The culture test shall be geared towards the following categories to be tested; here, the categories at Numbers 1 and 2 will receive the main weighting in the assessment:

1. context;
2. content;
3. developers of the content;
4. location of creative development.

3The review under the culture test will be performed using a points system. 4The interactive electronic work must score a minimum number of points to pass the culture test.

(7) The cultural promotion bonus shall lapse with retrospective effect if the provisional certification is withdrawn from the eligible party under Paragraph 2 Sentence 2.

(8) 1If the cultural promotion bonus lapses with retrospective effect in accordance with Paragraph 7, it shall be revoked; the corresponding tax statements or notices of assessment shall be amended to that effect. 2This shall also apply if the tax statements or notices of assessment have become final; the assessment periods will thus not end before the expiry of assessment period for the taxable period in which the precondition of Section 35 e Paragraph 6 Sentence 4 fails to be satisfied for the first time.

(9) 1Responsibility for the separate assessment under Section 35 c Paragraph 3 lies with the tax office that is responsible for the separate assessment of income. 2The basic notification for determining the cultural promotion bonus under Section 35 c Paragraph 1 is the determination of the share of the cultural promotion bonus under Section 35 c Paragraph 3 Sentence 1.

(10) The German government is authorised to issue legislative decrees to regulate further details relating to the performance and the process of granting the cultural promotion

bonus, the repayment under Section 35 e Paragraph 7 and Paragraph 8, the determination of the eligible expenditure under Section 35 d Paragraph 2, the grant of the certificate, the process for recognising the suitable institution (certification check) under Paragraph 3, the disbursement under Section 35 c Paragraph 6 and the design of the culture test.

(11) There may be no derogation from the provisions of the administration procedure set down in this act or on the basis of this act under national law.'

Article 2

Amendment of the German Corporation Tax Act (KStG)

Under Section 26 of the German Corporation Tax Act in the version of the announcement dated 15 October 2002 (Federal Law Gazette I p. 4144) as last amended by Article 4 of the act dated 19 July 2016 (Federal Law Gazette I p. 1730), the following new Section 26 a is inserted:

'Section 26 a

The provisions of Sections 35 c to 35 e of the German Income Tax Act shall be applicable to corporations as defined at Section 1 provided these are not exempt from corporation tax.'

Article 3

Amendment of the 1995 Solidarity Surcharge Act (SolZG)

In Section 3 of the 1995 German Solidarity Surcharge Act in the version of the announcement dated 15 October 2002 (Federal Law Gazette I p. 4130) as last amended by Article 8 of the act dated 19 July 2016 (Federal Law Gazette I p. 1730), the following new Paragraph 2 b shall be inserted after Paragraph 2 a:

'(2 b) The tax reduction under Section 35 c of the German Income Tax Act or Section 26 a of the Corporation Tax Act shall not reduce the assessment basis for the solidarity surcharge.'

ANNEX 1

Draft of culture test as the basis for the tax-based games promotion

Objective: The culture test forms the basis of the application for tax benefits in accordance with the 'Draft for a model of tax-based cultural promotion in the field of interactive electronic

works'. The objective of the model is to strengthen the development of computer and video games in Germany and Europe that promote cultural diversity.

The purpose of the tax-based promotion is to improve the prevailing conditions of the computer and video game economy in Germany so that more games can be developed in Germany and Europe. Computer and video games are a cultural asset and a principal medium of the 21st century; they are an expression of and an art form for modern societies. They reflect the issues of our age; they generate new, creative impulses. The promotion of culturally relevant digital games will have a ripple effect in many fields of the cultural and creative industries. Promoting the development of games will make an important contribution towards safeguarding cultural diversity in Germany and Europe.

Passing this test is the basis for eligibility for the tax-based promotion for the development of computer and video games. The intention is to facilitate higher production budgets for games to promote artistic scope as well as the quality, attractiveness and thus also the national and international dissemination of computer and video games from Germany and Europe.

A further desirable outcome is for the costs expended in Germany and Europe in connection with the development of computer and video games to be increased and as a consequence for the developer studios and their service providers to be better utilised. Improving the funding of the developer studios and providing the corresponding technical infrastructure are key prerequisites for a lasting, creative and successful German and European games culture.

Fundamentals: Computer and video games promote cultural diversity and shall thus be eligible for funding if there is a significant German influence on the overall responsibility for their development (a division of labour between Germany, Europe and the European Economic Area is possible) and they deal with and/or reflect Germany's and Europe's culture, everyday life, society and identity, German and European history and life in Germany and Europe.

The basis of the test is a points system which has not been finally developed for this draft, but which outlines the underlying system and content of the test.

Sample points system:

Minimum requirement: 16

Maximum possible: 42 [Note: in this draft culture test, the maximum scores have not yet been allocated to the individual criteria]

Basic requirement for eligibility for funding:

- The game must be awarded an age rating of at least 18 or below in Germany.

Criteria:

None of the following criteria is a necessary condition for eligibility for funding; instead, criteria with an allocated score of at least 16 points need to be met.

1. Context

- The setting of the game is located in Germany or exhibits links to Germany
- The main characters exhibit links to Germany or represent a person of German and European contemporary and world history or a fictitious figure of German or European cultural history
- The game picks up on motifs, ideas, etc. that exhibit links to Germany
- The game is published in at least German
- The game picks up on a German or European context

2. Content

- The game is an expression of German and/or European cultural and social heritage and the diversity of life in Germany and Europe
- The game concept, game design or story pick up on Germany's culture (everyday culture, pop culture, youth culture, high culture, etc.), society, identity, German history and life in Germany in all its diversity
- The game deals with topics of current social and/or cultural relevance
- The game reflects regional diversity in Germany and Europe or the European Economic Area
- The story is based on a literary, filmic or other cultural basis from the German-speaking area

- The game continues German gaming traditions or develops these further

3. Creatives

- At least 1/3 of the managerial staff involved in the development of the game are resident in Germany or the European Economic Area and are liable for tax there
- At least 1/3 of the creative staff are resident in Germany or the European Economic Area and are liable for tax there

4. Location of creative development

- At least 50 per cent of the development costs arise in Germany
- Musical setting, sound, graphics, levels and/or content, software development, design and story are created in Germany to a significant extent
- The authors' input takes place in Germany to a significant extent
- At least 20 per cent of the market research on the release is conducted in Germany, and at least 80 per cent in the European Economic Area

**Revised version as compared to the publication for the Parliamentary Evening on 23 November 2016. The phrase 'culturally valuable' games included in the original draft was misleading and did not correspond to the intention of the BIU. For that reason, the input from the Parliamentary Evening has been integrated into the model, a clearer formulation selected and the underlying system of the culture test set out more clearly.*