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Creation of Financial Instruments for Financing Investments in Culture, Heritage and Cultural and Creative Industries

Executive Summary

**WE CONSULTANTS
(MEGALOCI –
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e Território)**

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Executive Summary

The study on ‘Creation of Financial Instruments for Financing Investments in Culture, Heritage and Cultural and Creative Industries’ is part of the comprehensive and ambitious initiative of the Secretary of State of Culture which is implemented by the GEPAC - Gabinete de Estratégia, Planeamento e Avaliação Culturais (GEPAC - Office for Cultural Strategy, Planning and Evaluation). This initiative aims to advance the creation of a coherent set of ten research projects, in the context of the European Strategic Framework 2014-2020, designed to fully take advantage of opportunities and to maximise the benefits arising from this cycle of European Union public policies.

This study, prepared by WE CONSULTANTS, has as its main objective the presentation of reasoned conclusions and recommendations on the financing of agents, projects and investments in art and culture through repayable financial instruments.

Benefitting from qualified and diverse analytical bases, bibliographies and statistics, the favoured methodology, along with the analysis, debate and reflection by the team, allowed face-to-face meetings with numerous key stakeholders and players in the, and for the, financing of art and culture, whose input confirmed the rationality of this choice of methodology. Their generous availability not only secured access to the relevant information, but also aided the understanding of the important dimensions of the problems addressed by the study and, consequently, supported the framework and rationale of the presented conclusions and recommendations.

In contrast to the positive evolution of ‘cultural consumption’ between 2004 and 2012 which (according to the INE’s ‘well-being index’¹) tends to be higher than the ‘quality of life index’ and, in particular, the evolution of ‘material conditions of life’, the 2013 Eurobarometer on ‘cultural participation and access’ reveals three conclusions which are particularly relevant to the present study: (i) despite the differences among Member-States, a general decline in cultural activity participation and access has been confirmed for the EU-27; (ii) the internet is the most frequently used instrument in Europe for access to cultural information, buying cultural products and reading cultural articles; (iii) the levels of cultural access and participation in Portugal are very low in comparison with the rest of Europe. The analysis of the explanatory reasons indicates that ‘cost’ (of the frequency and utilisation of cultural goods, products and services) is not the factor most frequently cited, and is clearly surpassed,

¹ INE - Instituto Nacional de Estatística, the Portuguese institution in charge of producing official statistical information.

particularly in Portugal, by references to ‘lack of interest’ and ‘lack of time’ – a situation that presents important transversal challenges for European and national public policies.

The importance that we attach to overcoming these challenges is not only justified in terms of the collective objective of improving cultural access and participation, taking into account that its scope and meaning are inherent to two fundamental considerations: culture is a key asset for the creation of wealth, whose macroeconomic weight grows in tandem with the principal indicators of quality of life and well-being; cultural activities are factors in the creation of employment and even more so when the degree of socio-economic development is greater. It tends, however, to be undervalued as a result of difficulties in the respective identification, accounting and temporal volatility.

Naturally, these considerations are supported by exercises to quantify the economic and social relevance of culture and the arts. In particular, it should be taken into account that the European Commission valued the contribution from culture at 3.3% of GDP in the EU-27 (increasing from 2.6% in 2003). These values are consistent with the results achieved in 2010² for the contribution to wealth creation in Portugal – estimated at 2.8% (with 2006 taken as the time reference). On the other hand, the impact of artistic and cultural activities on employment was quantified as 1.7% for the EU-27 group in 2009 – a value identical to that recorded in Portugal, by the INE, in 2012.

Taking into account these quantitative dimensions, the study proceeds to examine on the one hand the prevailing models of financing and, on the other, the existing financial instruments in Portugal.

In particular, we verify that in terms of arts and culture the different conceptions of the State and its relationship with society and the economy, which characterise and separate the Anglo-Saxon countries from continental Europe, influence, perhaps decisively, the financing models which are adopted.

Taking aside any dynamic realities, characterised as much by convergence of tendencies as by specific details of national (and regional) implementation, the model of continental financing is based on the pursuit of public policy objectives, established (with involvement of varying significance from stakeholders) by public institutions overseen by a member of the Government, through the management of predominantly public resources. The Anglo-Saxon model of financing assumes an approach which is more liberal and participatory in the

² Augusto Mateus & Associados.

definition of political priorities, trusting its implementation to non-public entities and stimulating the leverage of public resources through the mobilisation of private resources.

The analysis of instruments of financing for culture, heritage and cultural and creative industries is supported by the systematic organisation of coherent and aggregated domains and subdomains of the corresponding agents, activities, goods, products and services, and in the referencing of the quantitative information for the period 2010-12.

Apart from its descriptive and quantitative dimensions, this analysis also assumes (in relevant situations) a critical perspective. This is done not only to maximise efficiency and efficacy but also, and above all, because we believe that the successful creation and operation of repayable financing instruments, from public initiative and aimed at supporting the fulfilment of public policy objectives, are conditioned by the global coherence of the corresponding system of financing of activities, projects and investments. This is done not only because we believe (with the fundamentals explained in this report) that these instruments should progressively assume a central role in public policy financing, but also because, particularly in an environment of significant shortage of public financial resources, it is important to ensure complementarity with the area of subsidy financing and, consequently, avoid competition between these two financing modes.

The financing instruments analysed are classified into three types: market financing, public financing and private financing.

The first – market financing – includes copyright and the sale and supply of services.

Copyrighting ensures, in particular, the recognition that the authors and creators own inalienable rights over the reproduction and representation of their creative works and products and, consequently, over the remuneration arising from the authorisation of the corresponding reproduction and representation. They represent, on average for 2011-12, around 34 million euros, displaying a downward trend from the previous years. Copyrighting is confronted with two relevant challenges: on one hand, due to irregular practices within the scope of private copying; on the other, challenges associated to the increasing utilisation of the internet in the dissemination of artistic and cultural creation.

Sales and supply of services constitutes, as expected, the most relevant and significant form of financing of culture, heritage and cultural and creative industries, representing in terms of

2011-12 annual averages, around 5,180 million euros, or around 1.5% of total turnover in the Portuguese economy. The temporal evolution of this variable exhibits significant reduction in the temporal period considered, at a higher percentage value than in the total economy³. This not only confirms the effects of the economic and financial crisis on the consumption and utilisation of goods and services which can be considered non-essential or non-priority, but also reveals the general reduction of the revenue and income of cultural creators and agents.

The second type of financing instrument includes public resources, which, in addition to their quantitative expression, assume particular relevance for the study (particularly in the context of the previously mentioned objectives of ensuring complementarity and the avoidance of competition between the two modes of financing.)

We analysed first the instruments which are financed by the European Union, both those managed by the Portuguese Strategic Reference Framework (QREN) and those administered by the Commission.

Based on the information from the study 'Fundos Estruturais e Cultura no Período 2000-2020'⁴, the artistic and cultural activities, initiatives and investments received funding through the generalities of the Operational Programmes of the 2007-2013 QREN of a value (approvals) of greater than 150 million euros.

The EU initiative and management programmes specifically aimed at artistic and cultural agents and activities, embodied between 2007 and 2013 by the CULTURE and MEDIA programmes, showed significantly reduced financing attributed to Portuguese projects, which we quantified for the 2010-12 annual average as being around 1.7 million euros.

We also considered financing from the EEA Financial Mechanism which, for the support of the activities and investment in question, amounted to around 1 million euros as the annual average over the period considered.

The national public financing instruments include, in addition to the tax benefits given by the IRC (on average over 4 million euros annually), the subsidies awarded by Central Government and the Regional and Local Governments in the areas relating to the study, the global value of which is around 825 million euros on average annually.

³ The rate of change of turnover in the selected CAE (economic activities) shows a reduction of -19.1%, while the total from the economy has had a decrease of -8.6%.

⁴ Document about structured funds and culture in the period 2000-2020, prepared, in the context of the group of studies promoted by the Secretary of State of Culture, by the Instituto de Geografia e Ordenamento do Território of the University of Lisbon with coordination from Professor Isabel André and Professor Mário Vale.

It is important to start by noting that this value is divided in almost equal proportions among Central Government and the Regional and Local Governments (around 412 and 414 million euros, respectively), noting also that the subsidies given by the Municipalities are directed towards the components with greater materiality than those given by the Central Government.

Funding from Central Government is primarily directed towards the subsidies for “Radio, Television and Publishing Services” which, having shown a decrease in the period in question, is still significantly larger than – more than double – the total expenses of the Central Government on Cultural Services (generally corresponding to the entities covered by the Secretary of State of Culture). This is a situation that, even considering the dimension and cultural impact of these activities, we cannot help but question in terms of reasonableness.

The Secretary of State of Culture naturally performs an important role in the financing of arts and culture. This is due both to the volume of financial resources it is responsible for, and to the responsibility it exercises in setting public policy strategy and priorities and in the subsequent guidance on the financing instruments and inherent influence on the decisions and behaviour of the artistic and cultural agents.

In an environment of strict discipline in public finances, budgetary allocations from the Secretary of State of Culture have come to exhibit a downward trend, which seems to have stabilised in more recent years at a value of around 180 million euros annually, corresponding to around 0.08% of the total expenditure of the state budget (initial allocations).

These amounts are subject to an effective reduction, witnessed when we quantify the budgetary implementation, as much by the blocking and reduction of initial allocations, as by the non-utilisation of the full amount. This leads to values of average annual budgetary execution between 2010 and 2012, of around 145 million euros.

The analysis of financing to arts and culture under the ambit of the Secretary of State of Culture allows us to conclude that these areas are almost entirely the beneficiaries of the DG Artes (around 16 million euros on average annually), the Cinema and Audiovisual Institute (ICA) (around 20 million euros) and the Cultural Development Fund (approximately 25 million euros), with the first two being different from the latter in terms of nature and applied methodology.

Being consistent with international practices, the methodology of evaluating applications and subsequent allocation of financial support adopted by the DG Artes and the ICA generally uses contests overseen by juries (which comprise individuals and experts in the areas involved and an

institutional representative). These appreciate the respective merits of the proposals under predefined criteria which are subject to a hierarchy (in descending order of score).

The evaluation criteria used generally focus on quality, artistic value and the potential of the candidate projects, and the CV of the promoters, on which we make the following comments:

- Valuing the CV component of the promoters of the projects seems to be excessive in face of the other evaluation criteria, which may lead to not considering projects where sufficient experience cannot be clearly demonstrated;
- Consideration of the economic and financial dimension is undervalued or even ignored – a fact that contradicts our understanding that this dimension should be explicitly assumed by public policy, in the sense that the reception by the national or international market should constitute one of the determining factors in the evaluation of the respective merits of projects and to also influence the nature of the projects and the behaviour of their promoters. The incorporation of this dimension into the selection criteria can be done by introducing conditions for the attribution of financial support or by attributing awards indexed to the results actually achieved.

The appreciation of the methodology for fixing the value of the allocated financial support should be, in our understanding, altered. This should be done in particular by separating the phases of the evaluation of the admissibility of applications and of the decision about the allocated support, assessing the absolute merit of each project in the first phase and quantifying the financing in the second phase, by application of a maximum percentage value to the categories of eligible expenditure.

The Cultural Development Fund (CDF) constitutes a third great source of financing for artistic and cultural activities and agents. The analysis of the respective Activity Plan for 2013, which was assessed as being a list of funding granted that year, leads to conclude that it should ideally include the systematisation of the objectives and results sought, and the specification of the contribution of funding for attaining the respective goals. Reference to the applicable legislation and the established governmental guidelines should naturally be considered.

We understand, moreover, that the efficiency and efficacy of the CDF would benefit from the establishment of a 'Funding Management Regulation'. This should establish a multiannual framework for financing decisions and actions related to the areas covered, the types of the entities, projects and investments, potential beneficiaries, the procedures for submission and selection of applications and their funding, the supervision and monitoring of the supported

activities, as well as the obligations assumed by the beneficiaries within the scope of the execution of the projects and the supply of financial execution reports.

The creation of conditions for effective supervision and monitoring of the allocated funding and the evaluation of results achieved should, in our understanding, be carried out within the framework of all the financing instruments of Central, Regional and Local Public Government.

The third and final type of financing is related to the activities and achievements of private entities and institutions, including investments in art and culture carried out by foundations and businesses, patronage and the counterparties to QREN's financial support.

The first case deals with the allocation of private or individual resources for the pursuit of objectives and the production of results of collective interest which, not exhaustively quantified, amounts to around 42 million euros. The analysis of the collected information shows that the majority of these funds are directed to projects and initiatives carried out by these same entities, on a permanent or occasional basis.

Patronage displays similar characteristics to those stated previously, although exclusively directed to supporting the initiatives of others. Also, in this case, the available information only permits the quantification of funding to entities under the scope of the Secretary of State of Culture (around 2 million euros on average annually).

The final point of consideration as a source of funding is related to the compensation demanded by the funding bodies from the EU. The most relevant situations are in the case of incentives to businesses and to productive investment, where the promoters mobilised around 26 million euros.

The overview of financing of culture is summarised in the following table, which clearly shows both the importance of sales and supply of services, and the relevance of those with public origin.

Quantification of financing of culture by origin and by domain (2010-2012)
(thousand euros)

		DOMAINS				
		Artistic Creation	Cultural Heritage	Cultural Industries	Creative Industries	TOTAL
'MARKET'	Copyrighting	33.631	0	0	0	33.631
	Sales and supply of Services	261.454	72.188	2.358.124	2.450.785	5.142.551
	'Market'	295.085	72.188	2.358.124	2.450.785	5.176.182
PUBLIC FINANCING	QREN 2007-2013	60.421	61.958	26.415	4.078	152.872
	Central Public Government (without Secretary of State of Culture Services)	58.384	118.774	89.548	218	266.924
	Secretary of State of Culture Services	31.658	64.402	48.555	118	144.733
	Regional and Local Public Government	59.093	285.160	69.854	0	414.107
	European Programmes and EEE Mechanism	386	1.100	1.195	0	2.681
	Fiscal benefits	9	2.177	2.066	1	4.253
	Public Financing	209.951	533.571	237.633	4.415	985.570
PRIVATE FINANCING	Subsidies, Prizes, Grants, Donations and Permanent and Occasional Activities	3.341	16.767	21.067	355	41.530
	Patronage managed by the Secretary of State of Culture	8	1.039	940	0	1.987
	Private Compensations QREN 2007-2013	13.526	5.159	4.324	2.957	25.966
	Private Financing	16.876	22.965	26.331	3.312	69.483
TOTAL		521.911	628.724	2.622.088	2.458.512	6.231.235

Existing financing instruments and the growing importance of the economic and social impact of art and culture led the team, in the context of the creation of financing instruments, to organise potentials and opportunities to explore:

- Existence of cultural agents and cultural and creative industries relevant to the Portuguese business corporations and in the structure of employment and innovation;
- Progressive internationalisation of the agents, initiatives and activities;
- Multiplication of the types of financing instruments;
- Increasing availability of financing from the CDF;
- Increasing importance of the third sector in cultural and artistic activities;

- Opportunities associated to the Partnership Agreement and Operational Programmes 2014 -20;
- Possibility to rethink the autonomous and exclusive mechanisms of financing of heritage conservation and management activities;
- Possibility of considering, with the IRS, artistic and cultural entities as potential beneficiaries of donations from individual contributors;
- Possibility of widening of the range of beneficiaries of the current ‘Cultural Patronage Law’ to profit-making entities;
- Interest in recovering guidelines for a possible ‘Single Cultural Desk’.

And, in parallel, the respective constraints and threats:

- Lack of a true culture of international and national market orientation of the national cultural and artistic agents and protagonists;
- Difficulty in accessing up-to-date and appropriately focused information on existing financial support for culture;
- Dispersion of the origins and sources of financing instruments in the public sector;
- Maladjustment of the financing model and the public management standards to the needs of the agents and, in our view, the rationality and efficacy of public governance;
- Frequent understanding of investment in art and culture as being a ‘soft issue’ for many stakeholders;
- High percentage of the budget of public artistic and cultural entities spent on fixed structural costs and on the management and maintenance of existing assets;
- Expression, which in our view is exaggerated, of free access to artistic and cultural goods and services;
- Sharp decrease of cultural patronage directed to public entities;
- Lack of competencies and experience of the cultural agents in the areas of economy, finance, marketing and human resources;
- Constraints and limitations of previous experiences of public-private financing of artistic and cultural activities in Portugal.

We found therefore that the use of financing instruments in culture, heritage and cultural and creative industries has not, particularly in Portugal, deserved the reception that we would consider justified and desirable. In addition, the negative consequence of the

predominant use of subsidies has become particularly evident with the enforcement of austerity and rigorous discipline in public finance and management following the global economic and financial crisis. This is particularly true due to the fact that it was impossible to maintain the previous levels of financing, which were furthermore systematically considered or perceived as insufficient by the stakeholders.

In these circumstances the utilisation of public initiative financing instruments, which are known to be increasingly introduced in the scope of public policy financing, is especially important, taking into account that:

- They enable the re-use of public resources in the financing of new investments, thereby improving efficiency;
- They allow the leverage of public resources through private or third sector resources, maximising the available levels of financing for the pursuit of public policy objectives;
- They focus on the use of resources to finance viable projects and investments, positively affecting non-profitable project support and leading to better decisions in the process of allocating public funds;
- They allow flexibility in the financing conditions (particularly rates and maturities) demanded for viability of the projects and investments;
- They penalise situations of continuous (sometimes assumed) dependency on public financial resources;
- They can be used (i) as separate financing solutions or (ii) in combination with subsidies (both in the required situations for viability of projects and investments and in the financing of the compensation required of the promoters who benefit from public support).

The analysis carried out for this study and the reflections of the team, which take into consideration the experience acquired with national and international repayable financing instruments, leads to the following considerations and recommendations:

- Not to be used to finance all types of projects and investments, repayable financing instruments are particularly suitable for the funding of projects and investments which (i) are financially viable, (ii) do not receive sufficient funding, through public subsidies or private resources, for their implementation and (iii) are aligned with the objectives and goals of public policy;
- Notwithstanding the importance of the specificities and characteristics of the entities, activities, projects and investments which, together, can justify public financial

support, the domains which form the thematic focus of this study (culture, heritage and cultural and creative industries) should be thought of as being part of a progressive scale for using financing instruments for their funding. On this scale, artistic creation projects and investments would be low, those related to heritage would be medium, in the case of cultural industries it would be high and for creative industries very high;

- The financing instruments are essentially, in addition to hybrid solutions, loans, guarantees and capital (particularly risk capital and venture capital), of types which can be combined in order to offer financing solutions which are more appropriate to the needs and specifications of the initiatives, projects and investments;
- The eventual mobilisation of EU financing resources for funding of financing instruments requires compliance with the specific regulatory standards, including the elaboration of an ex-ante evaluation study under the initiative and responsibility of the financing Operational Programme(s);
- The governance model of financing instruments should ensure balance between the evaluation of the contribution of the supported projects and investments to the public policy objectives (specified in the established investment strategy) and the autonomy of the management entities in assessing respective merits. In addition to their technical competencies these should be selected based on their ability to effectively mobilise, directly or indirectly, private (or third sector) resources and, thus, leverage public finance.
- The creation of financing instruments should be coherent and coordinated with the global financing system of the economy, whether in respect to the instruments specifically related to arts and culture, or those which support companies and business investment (including incentives for innovation, R&D and internationalisation) – emphasising the desirable coordination with the Development Finance Institution;
- In mobilising public resources, ideally leveraged by private resources, the creation of financing instruments by public initiative is only justified if overcoming existing market failures is guaranteed (particularly the availability of financing for the projects and investments in question), presenting comparative advantages over the solutions offered by the financial market, namely (i) ensuring lower financial costs and (ii) offering longer repayment periods (maturities).

The study proceeds finally, under the specified terms, to the evaluation of the potential demand for repayable financing instruments for funding culture, heritage and cultural and creative industries, as well as the identification of potential and mobilised players and stakeholders.

We conclude with the estimation of potential demand, made on the basis of the ‘approved eligible investment’ proxy for incentive systems in the relevant activities and assuming a flexible model of financing instruments, with flexibility maximised by the grouping of identified success factors, which can correspond to an annual value of around 35 to 45 million euros. The cost of financing, management and application of financing instruments will represent a fraction of this value (corresponding to the amount of the rate of interest which will be applied, to the confirmed imparities in the context of the mutual guarantees that will be established and the balance between positive and negative risk capital investments, plus the management costs of the financing instruments).

The mobilised players and stakeholders will potentially integrate, in addition to those stakeholders inherent to the allocation of national resources (through, in particular, the FFC), ideally maximised by EU funding (especially under the 2020 Partnership Agreement) and also, through the BEI, those from collaborative and partnership agreements with the most relevant foundations in the domain of arts and culture, as well as large and medium sized businesses, namely those responsible for the supply of services of general economic interest and financial institutions.