Tax Incentives for Filmmakers Face Uncertain Future

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10-13 minutes

Film and television productions have been leaving Los Angeles and New York for many years, chasing cheaper production costs and a change of scenery. Recently, U.S. states have upped the ante with increasingly competitive tax credits, picking up a percentage of in-state expenses in the hopes of developing local industry, generating state revenue, and increasing film-related tourism. Questions abound, however, regarding the wisdom and sustainability of these schemes, as well as their potential impact on content.

Here are five things you need to know about tax credit incentive schemes:

1. There are three main types of credit schemes, of varying degrees of desirability.

2. The effectiveness and long-term viability of tax credit programs is unclear.

3. Tax credit incentives have contributed to a loss of production in LA, and increased competition between LA and states

offering incentives.

4. Tax credits are crucial but not enough on their own to build local film and television industries.

5. PR concerns cause some states to place restrictions on the content of qualifying productions.

1. There are three main types of credit schemes, of varying degrees of desirability.

Currently, 27 states and the District of Columbia offer refundable tax credits or rebates. Twelve states, as well as Puerto Rico, have transferable tax credits, and only two states offer non-transferable credits (California's credit is non-transferable, but independent productions can apply for a transferable credit). For current breakdowns of tax credits offered by state, see reports published by Entertainment Partners and The Incentives Office.

There are three different categories of rebates – refundable, transferable, and non-transferable. The differences among the three are significant for studios and production companies.

- **Refundable:** The most desirable form of credit for producers, the state refunds a percentage of the production company's qualified expenses upon the completion of a tax return, regardless of the amount owed in taxes.
- **Transferable:** This tax credit can only be applied to existing tax liability in the state, though it can be sold to another party. A broker generally handles this sale and the production company does not receive the full value of the tax credit.
- **Non-Transferable:** The least desirable credit, only redeemable

to cover the production company's tax liability.

Percentages of a budget that can be claimed vary, and states often cap either individual expenditure per film or the total credited in-state in a year, in addition to imposing a minimum-spend amount. Michigan's scheme, for example, imposes no annual or project cap, but requires a minimum spend of $50,000. Missouri offers a transferable 35% tax credit, but total annual credits are capped at $4.5 million. The lack of caps on the most successful incentives suggest they are pitched at mid- to high-budget productions, and states generally have minimum-spend amounts that commonly range from $50,000 to $500,000, although Utah and South Carolina have minimum spend amounts of $1 million, and New Mexico has no minimum spend.

(Read more - Entertainment Partners "Basic Overview of U.S. and International Production Incentives")

2. The effectiveness and long-term viability of tax credit programs is unclear.

While many of the programs have brought a steady flow of production activity to areas that have not historically been production centers, questions surround the wisdom of such schemes. Reports prepared by Ernst & Young for state governments in New Mexico and New York report that each dollar of incentives returns $1.50 and $1.90 respectively, on every dollar spent on incentives. But other studies have presented a less rosy picture. A study by the Arrowhead Center at New Mexico State University argued the return on investment was only $0.14 per dollar spent, and the conservative Tax Foundation has recently issued a report opposing incentive programs at a national level, arguing the motion picture industry should not be favored over other industries, and that research on the benefits of incentive schemes is questionable.

The image of some state programs has been tarnished by accusations of corruption, most notably in Iowa. There, Governor Chet Culver has suspended the tax credit program for all new productions until the completion of an investigation into misuse of tax credit dollars, including credits issued for the purchase of vehicles unrelated to film production. Questions about corruption or proper accountability on a smaller scale have also marred incentive programs in Louisiana and New Mexico.

3. Tax credit incentives have contributed to a loss of production in LA, and increased competition between LA and states offering incentives.

Albuquerque Studios, a purpose-built studio (via Open Threads of Flickr (CC))

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Competition from locations outside the US, such as Vancouver, has already diminished Los Angeles-based production, and state-based tax credits have recently exacerbated the situation, creating difficulties for filmworkers in Los Angeles (and New York). *Variety* reports “estimated pilot production spending in the

L.A. region dropped from $309 million in 2005 to $207 million in 2009," with credit programs cited as an important contributing factor. To compete with increasingly lucrative offers elsewhere, both California and New York have implemented tax credit programs of their own -- California offers a non-transferable tax credit of 20-25% and New York a more generous refundable 30% credit. Nonetheless, productions continue to leave the coasts to take advantage of other states' more lucrative incentives.

States offering incentives are well aware of their position as competitors in a globalized industry. In marketing their locations, many states paradoxically stress both their uniqueness and anonymity. The Louisiana Office of Film and Television touts its "range of locations from native swamp and plantations to urban cityscapes and Anywhere, USA towns," and New Mexico's largest purpose-built studio space, Albuquerque Studios, brags that "New Mexico can and has doubled for" locations as varied as Mexico and New York City, the Middle East and Munich. These selling points recognize the global competition in which Texas may not only be competing with California for a given film, but also with Michigan and Morocco.

4. Tax credits are crucial but not enough on their own to build local film and television industries.

A major concern regarding tax credit programs is that when incentive programs are removed, or producers find a better incentive elsewhere, productions will leave.

Most states have combined tax credit incentives with attempts to build a sustainable local industry through creating infrastructure and increasing training opportunities for local filmmakers and crewmembers. States that have enjoyed the greatest success in luring production, like Michigan, Louisiana and New Mexico, all offer significant studio resources to supplement tax credits.

Due to Filming Grass Will Not Be Cut Until May 29, 2009: Sign at a New Orleans Cemetery (via szlea of Flickr (CC))

In addition, a number of states include additional support to productions that employ local crewmembers. New Mexico offers a film crew advancement program that pays 50% of wages for local crew members who receive on-the-job training. West Virginia's more modest incentive program adds 4% to its 27% transferable credit for productions that hire 10 or more residents in the cast or crew, and Alabama's 25% rebate is bumped to 35% for the salaries of resident crew.

Despite these efforts for greater production sustainability, there is widespread agreement that the incentives are the crucial factor, as confirmed by states where incentives have been eliminated. New Jersey's tax credit program was slashed as part of a budget reform package on June 30th, 2010, and*Law & Order: SVU* moved across the Hudson River to New York. Steve Gorelick, Executive Director of the local film commission states that films like *The Messenger* and *The Wrestler* "would not have been made here without a tax credit."

Opponents of tax credits make the same argument, however. Dennis Kintigh, a New Mexico State Representative who has introduced legislation opposing the state's program, says: "We're told if we don't provide these incentives they will pack up and leave. If that’s the case the industry doesn’t have any roots here.” State governments are in the unenviable position of needing to build infrastructure and strengthen local crew bases to supplement credit programs and ensure a steady flow of film and television production, while also knowing that without the tax credits, the production would vanish.

5. PR concerns cause some states to place restrictions on the content of qualifying productions.

Tourism and positive PR are key motivators for many state tax credit schemes. Georgia’s Film, Music & Digital Entertainment Office tries to attract future activity and tourism by offering producers an additional 10% tax credit for including an animated state logo in the finished product.

Less conspicuously, other states have attempted to leverage their tax credit dollars to restrict how the state can be represented. Most states explicitly disallow pornography from receiving tax credits, but several states have imposed additional restrictions. Texas and Pennsylvania’s tax credit programs both withhold funding from projects that cast the state in a negative light. Michigan recently declined to award tax credits to *The Women*, a low-budget cannibal horror film, on similar grounds. A bill submitted to the House of Representatives in Florida earlier this year proposed an additional 5% ’family-friendly’ tax credit to productions that met the specific criteria. Eligible films would

> "have cross-generational appeal; would be considered suitable for viewing by children age 5 or older; are appropriate in theme,

> content, and language for a broad family audience; embody a responsible resolution of issues; and do not exhibit or imply any act of smoking, sex, nudity, nontraditional family values, gratuitous violence, or vulgar or profane language."

After outcry from the film industry, gay rights activists, and the media, legislators removed “nontraditional family values” from the final version of the bill. Even in its revised version, however, the ‘family-friendly’ credit is part of a trend toward content control that, rather than attracting activity, may send producers running for the Hollywood hills.