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The Current State of Film and Television Tax Incentives in the United States

By Ethan Bordman

The Los Angeles region has historically been the world capital of moviemaking, but in recent years there has been significant competition among states to offer lucrative production tax incentives. For a time, Michigan — the location of such films as *Up In The Air* with George Clooney and *Gran Torino* with Clint Eastwood — was dubbed "The Hollywood of the Midwest" thanks to a refundable credit of up to 42%. Georgia, which offers up to a 30% transferable tax credit with no production cap, has been referred to as "the Hollywood of the South," considering its location for *The Blind Side* starring Sandra Bullock, and *Flight* starring Denzel Washington. Louisiana is another contender for the southern movie capital. It offers a tax credit of up to 35% and no production cap; both *Killing Them Softly* starring Brad Pitt and *Django Unchained* starring Jamie Foxx were filmed there.

This article surveys current tax-incentive opportunities in the United States for motion picture, television and interactive media productions. Presently, 40 states offer financial incentives designed to attract such productions.

The creation and growth of the incentives is a response to "runaway productions" that leave the United States to be produced in other countries. As early as 2005, a report by the Center for Entertainment Industry Data and Research (CEIDR; www.ceidr.org) attributed this trend to factors including financial incentives and exchange rates. *See*, "The Global Success of Production Tax Incentives and the Migration of Feature Film Production from the U.S. to the World," available at http://bit.ly/12gJQUL. The success of the Canadian Production Services Tax Credit, enacted in 1998, offered a rebate of 11% on qualified labor along with individual provinces offering an additional rebate on labor from 11% to 47%. The credit, along with a favorable exchange rate (at the time, $1.00 U.S. was worth $1.47 Canadian) and the ability of Canadian cities, such as Toronto, to convincingly represent U.S. cities like New York, made Canada a popular draw for films and television.

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Decision of Note

Second Circuit Sends *Ghost Rider* Copyright Back to District Court

By Mark Hamblett

A dismissed lawsuit over the rights to the *Ghost Rider* comic book character has been revived and sent back for trial. The U.S. Court of Appeals for the Second Circuit decided that Gary Friedrich, who claimed he created the flaming-skull motorcycle superhero, will get a chance to challenge Marvel Comics' claim that the character was the result of a collaborative process within Marvel. *Gary Friedrich Enterprises LLC v. Marvel Characters Inc.*, 12-893.

The Second Circuit reversed the decision of Southern District Judge Katherine Forrest, who had granted summary judgment for Marvel and other defendants on Marvel's claim that it owned the renewal rights on the *Ghost Rider* character, which made its debut in 1972. District Judge Forrest found that Friedrich had assigned any rights to *Ghost Rider* when he executed a work-for-hire agreement in 1978, six years after the comic book first appeared. She dismissed Friedrich's claim and awarded $17,000 in damages to Marvel on its counterclaim for copyright infringement.

At the federal appeals circuit, Judges Ralph Winter, Denny Chin and Christopher Droney made the

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Tax Credits vs. Tax Rebates

Incentives and production caps vary from state-to-state. A "tax credit" refunds a portion of taxes incurred by a production in a state. A "tax rebate" pays cash to a production for certain expenditures made in a state. Some states refer to their incentive as a "credit" when it is actually a "rebate." Further, some states offer a combination of credit and rebate called a "refundable credit" for which a tax credit is first given to the production and is then followed by a rebate for any excess credit that may be owed. "Credits" and "rebates" are based on "qualified expenses," which vary from state-to-state and are discussed below.

Many states allow tax credits to be "tradeable" or "transferrable," meaning that they can be traded for cash, like a stock option. For example: A film production spends $1 million in a state that offers a 30% tax credit. After all the receipts and financials have been processed by a certified public accountant, proving the money was spent in the state and is a qualified expenditure, the production company files a request with the state for a tax credit certificate. Once approved, the state gives the production a tax credit certificate for $300,000 (30% of $1 million). This credit can then be used to lower the taxes accumulated on the production — or the credit can be sold. If it is sold, the dollar value — for example, 90¢ on the dollar — is negotiated with a buyer. This allows the buyer, which could be any business located in the state, to buy a $300,000 tax credit for $270,000 and use it toward taxes owed to the government. The production company then has $270,000 in cash to use in any way it chooses.

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Cities, too, may offer additional enticements in the forms of tax credits, city services and marketing credits. New York City's Office of Film, Theatre and Broadcasting's "Made in New York" Marketing Credit Program offers media packages where at least 75% of the film is produced in New York City. The credit, which varies based on the below-the-line budget of the film, allows promotion and advertising of the film through public transportation — at bus stops, on subway fare cards, and in 30-second commercials on taxicab video monitors. The New York Police Department offers the services of the NYPD Movie/TV Unit, which assists productions in dealing with vehicle and pedestrian traffic by closing streets and sidewalks in the vicinity of filming. For the 2013 season, a record 21 television pilots have been scheduled to film in New York City.

The types of expenditures that are included in incentives vary from state to state. "Qualified expenses" generally cover pre-production, production and post-production expenditures such as facilities, props, travel, wardrobe and set construction. New York, for example, does not cover general travel costs; Michigan covers these costs if travel to the state is arranged through a Michigan travel agency. "Qualified labor" includes those individuals whose salaries are covered by the incentive. Most states place a cap on any one individual's salary; for example, Georgia has a limit of $500,000 per person but Alaska has no restriction on salary. "Qualified production" usually includes feature films, episodic television series, television pilots, television movies and mini-series. Most incentives exclude documentaries, news programs, interview or talk shows, instructional videos, sports events, daytime soap operas, reality programs, commercials and music videos.

In 2011, New Jersey Governor Chris Christie blocked a $420,000 tax credit that was to be issued by the state's Economic Development Authority to MTV's *Jersey Shore*. New Jersey, which at the time included reality television as a qualified production, had approved the credit before filming of the show's first season. Governor Christie stated: "I am duty-bound to ensure that taxpayers are not footing a $420,000 bill for a project which does nothing more than perpetuate misconceptions about the State and its citizens." This action by Christie, a former U.S. Attorney for the District of New Jersey, brought on a debate about "content neutral" issues in choosing which projects may qualify for a state's incentive.

Some states also have guidelines in choosing which projects are approved based on the project's content. The Texas Moving Image Incentive Program, which offers up to 17.5% of eligible spending or up to 29.25% of eligible wages, says any project "that includes inappropriate content that portrays Texas or Texans in a negative fashion" is deemed ineligible for the incentive. In 2010, after viewing the film *Machete*, which featured Robert De Niro, the Texas Film Commission denied the incentive, stating that the film portrayed the state negatively. Director Robert Rodriquez noted the state had read the script and approved it under the incentive before the film was shot.

Here Today May Not Mean Here Tomorrow

One key consideration in choosing a state based on its financial incentives is that programs can be reduced or eliminated at any time. From 2008 to 2011, Michigan had the most lucrative film incentive in the country — a refundable credit of up to 42% — but it was reduced when the state elected a new governor. Rick Snyder, who took office in January 2011, announced that Michigan's Film and Digital Media Production Assistance Program would incur drastic film-incentive cuts. In the most severe reduction, the previously unlimited incentive would now be subject to a cap of $25 million. In 2010, the state film office

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credited more than $115 million, so a $25 million cap was a significant change. The revised incentives cut expenditure rebates to 32% (from 40%) for Michigan personnel and to 25% (from 30%) for non-Michigan personnel. The credit for non-Michigan personnel will continue to fall — to 20% in 2013, 15% in 2014 and 10% in 2015. In February 2011, Ernst and Young issued a report showing the economic effect of Michigan's film credit in 2009 and 2010, prior to the cuts. In each of these years, $209.3 million and $322.6 million, respectively, was spent on qualifying productions in Michigan. As a result of this spending, each dollar of net film tax credit cost generated $5.89 in economic output to the state in 2009 and $5.94 in 2010.

Federal film incentives may also come and go. In 2004, as part of the American Jobs Creation Act of 2004, Congress enacted 26 U.S.C. §181 (http://1.usa.gov/10R7wRq): "Treatment of certain qualified film and television productions," in an effort to stimulate the activity of productions in the United States. Section 181 encourages investment in U.S.-based productions by giving tax benefits to investors who can elect an immediate deduction for qualifying expenditures of the film in the year the expenditure occurs. The incentive applies to productions whose budgets do not exceed $15 million ($20 million if a significant portion of the production is filmed in areas designated as distressed) as long as 75% or more of the total compensation earned occurred in the United States. The law expired in December 2011 but was renewed in January 2013 as part of the American Taxpayer Relief Act of 2012 (the "Fiscal Cliff") for productions that commence in the 2013 calendar year.

Recently, several states have taken measures to curb expenditures. A state representative from Wisconsin recently proposed a bill that will reform the states' tax code, including eliminating the state film tax credits. Wisconsin currently offers a 25% Production Services Tax Credit and has been a location for the motion pictures *Transformers 3* and *Public Enemies*.

Two lawmakers in North Carolina are currently supporting a bill, N.C. House Bill 994, which would eliminate the state's 25% credit and instead waive any tax liability accrued by the production company over the next five years, up to an equivalent amount. The state has been a location for the movie *Iron Man 3* and the TV series *Homeland*. One sponsor of the bill stated: "It was to fix a constitutional problem." In a memorandum of law, Jeanette Doran, Executive Director of the North Carolina Institute of Constitutional Law, explained why the incentive is considered unconstitutional. The incentive is a refundable credit currently structured as an appropriation, which requires a specific dollar amount to be approved by the legislature. "Public funds" are being given to production companies as a rebate; therefore, when the credit exceeds the production's total tax liability, monies disbursed by the treasurer without legislative authority are in violation of the state's constitution. It is proposed that eliminating the "refundable" portion of the film credit would correct this situation. The bill was recently in the House Rules Committee for review. In 2012, $376 million was spent on the North Carolina economy, of which $45 million in tax credits were issued to move production companies.

Louisiana's Motion Picture Investor Tax Credit has also seen opposition. Several legislators have introduced House Bill 696, which will reduce the state's program by $22 million annually, beginning in July 2014. The bill is intended as part of an effort to cut $525 million from the state's budget.

The Ernst and Young report on Michigan's film tax credit also showed that the impact of the incentive was felt far beyond the film and television industry. In 2009 and 2010, $190.2 million and $311.7 million, respectively, were spent on local catering services, lodging, equipment rentals, travel services, transportation and insurance — a considerable indirect economic impact. Some of these funds came from the production directly and some from the film crew, who spend a portion of the salaries they earn in the state on local retailers. In May 2013, a report entitled "Economic Impacts of the Massachusetts Film Tax Incentive Program," prepared for the Motion Picture Association of America (available online at http://bit.ly/12gTref), stated that in 2011 this state generated $375 million in total economic output through $38 million in tax incentives awarded. Massachusetts, which offers a 25% production credit and no annual or project cap, generated approximately $10 in local spending for every $1 awarded to moviemakers, leading to the creation of 2,200 full-time equivalent jobs across all industries in the state. In North Carolina, *Iron Man 3* spent $110 million — which included $19 million in wages for residents — or an average of $23,000 per job. The production spent $41 million on goods and services at more than 700 vendors.

Bad Reviews

In March 2013, the Massachusetts Commissioner of Revenue noted negative impacts, such as payments to non-residents who choose to take their salaries and spend the funds back in their home state. Also, although most states require a "qualified" purchase under the incentive to be made in the state, Massachusetts, for example, allows items to be purchased from out of state so long as they are used on the production — thus, state-based businesses lose out.

Moreover, much of the employment is short-term. The Ernst and Young study on Michigan stated that the average production lasts 90 days, and noted that most state residents work roughly one-third of their workdays on a single production. Also, although individuals may work steadily for a month on a film, they then may not work for several months thereafter. A counter-argument to short-term employment is that productions still create jobs for people who would otherwise be

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out of work, and the pay for a few weeks of work on a movie may be enough to satisfy living expenses for several months. The average compensation on a production in Michigan in 2010 for full-time equivalent employees was $64,400. Economist David Zin noted in a September 2010 report on Michigan's incentive that the benefits to private businesses usually outweigh those to the state (tax revenue). *See*, "Film Incentives in Michigan," available online from the Michigan Senate Fiscal Agency at http://1.usa.gov/18dJG4A. Thus, the decision of costs to benefits is one for policy-makers.

Though many residents enjoy the excitement of seeing a movie filmed in their neighborhood, many others dislike the interference of closed streets and sidewalks. In 2010, during filming of a scene in New York City, a production assistant on *Premium Rush*, starring Joseph Gordon-Levitt, was head-butted by an angry neighborhood resident after requesting that the resident wait a few minutes to cross a street. The resident was charged with assault and the assistant was treated for a broken nose.

THE NEXT 'HOLLYWOOD'

State film incentives have brought not only financial benefits to the states but publicity as well. A Cleveland-area friend recently mentioned that *Captain America 2* was being filmed right in front of his office. Being an eyewitness to the filming of a soon-to-be blockbuster movie and seeing an A-List star like Samuel L. Jackson walk down the local street is incredibly exciting for the city and its citizens. This type of publicity is difficult to match and even harder to quantify financially.

The competition for incentives will continue to increase through a combination of the "qualified" expenditures allowed by states and by raising or eliminating the cap on states' budgets for the incentives. *The Dark Knight Rises*, which intended to film in Michigan, relocated the production to Pittsburgh after the cap on the incentive was announced. Pittsburgh was recently named by *Entertainment Weekly* as the "Hollywood of the East," thanks to a 25% credit and state cap increase from $10 million to $75 million. The incentive has raised more than $100 million for three consecutive years for the city. Wilmington, NC, has also been called "Hollywood East" after serving as the location for productions such as *The Walking Dead*, *Revolution*, *Cloud Atlas*, and *The Hunger Games*. The competition among the states to entice productions will continue. Which state or city will be the next "Hollywood?"

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