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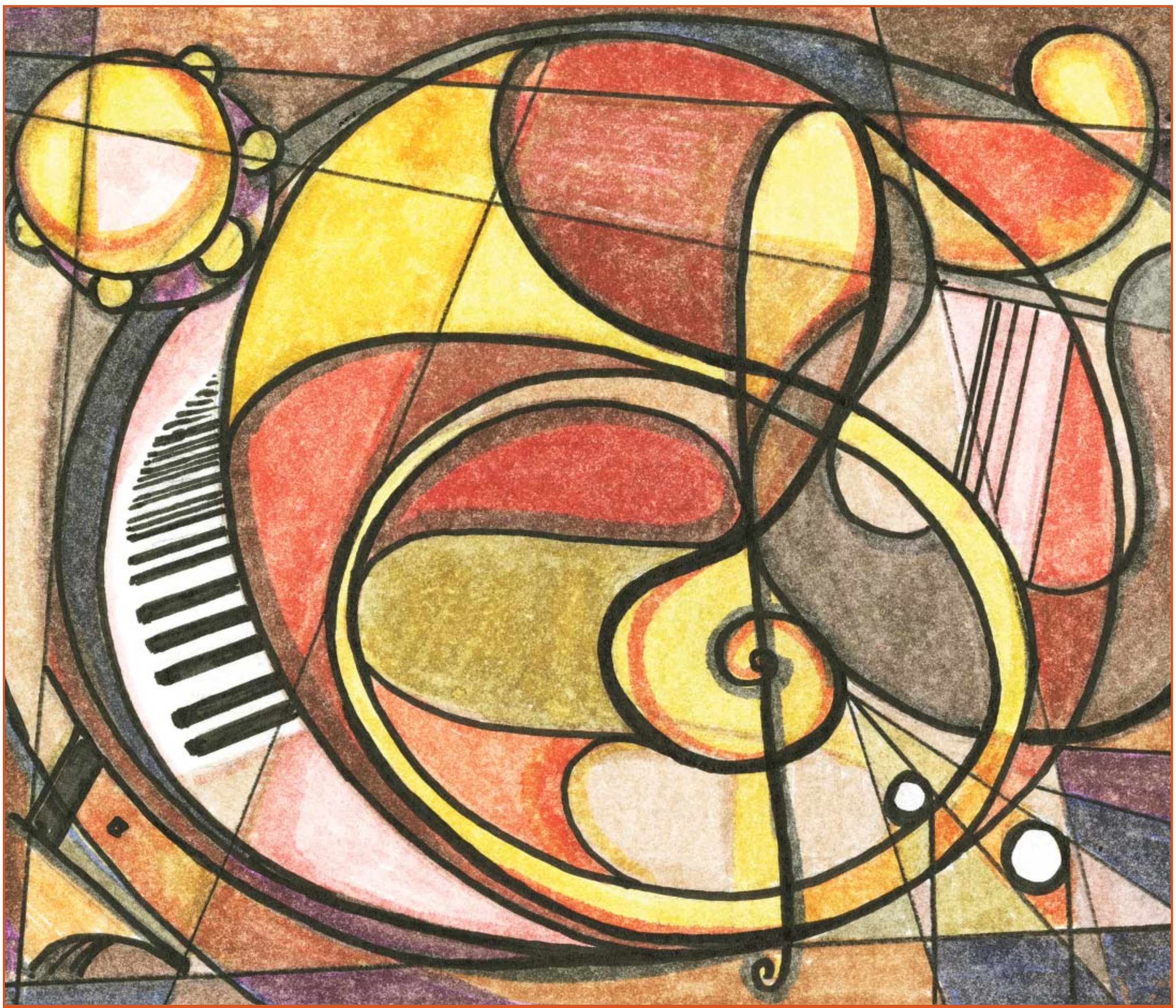

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State Film Incentives: Hollywood May Be Coming to a Town Near You

By Ethan Bordman

Hollywood, California may historically be known as "the Movie Capital of the World";[1] however, the competition among states to offer lucrative production tax incentives means that this title is up for grabs. For several years, Michigan—the location of films such as *Up in the Air*, with George Clooney; *Gran Torino*, with Clint Eastwood; *Real Steel,* with Hugh Jackman; *You Don't Know Jack,* with Al Pacino; and *Conviction* with Hilary Swank[2]—was dubbed "The Hollywood of the Midwest,"[3] thanks to a rebate credit of up to 42%.[4] Georgia, which offers up to a 30% transferrable credit (a 20% base incentive plus an additional 10% if the project features a state logo)[5] has been referred to as the "Hollywood of the South,"[6] serving as the location for *The Blind Side*, starring Sandra Bullock and *Flight*, starring Denzel Washington.[7] Louisiana is another contender for the title of southern movie capital; it is often referred to as "Hollywood South."[8] It offers a tax credit of up to 35% and no annual cap.[9] Films such as *Side Effects,* with Channing Tatum and Catherine Zeta-Jones and *Django Unchained*, starring Jamie Foxx and Leonardo DiCaprio, have been filmed there.[10] Pittsburgh is another popular location. *Entertainment Weekly* called this city the "Hollywood of the East," thanks to a 25% state tax credit and state cap increase from $10 million to $75 million in 2004.[11] However, this cap was reduced to $60 million in 2013.[12] Film and television incentives and credits were offered by only a handful of states in the early 2000s. Currently, 39 states and Puerto Rico[13] offer financial incentives designed to attract motion picture, television, and interactive productions.

Runaway Productions

When choosing a location for a shoot, producers consider factors such as the setting for the screenplay, availability of the crew, access to sound stages, and costs of travel and lodging. However, their first priority is to reduce the cost of production. According to Vans Stevenson, Senior Vice President State Legislative Affairs for the Motion Picture Association of America (MPAA), "Incentives are the number one item that film finance and production companies look at when they are trying to decide where to locate a production."[14] Stevenson also pointed out that labor costs and location are important, although he noted that most places can be made to look like someplace else.[15] One example is *Battle: Los Angeles.* This film, about an alien invasion of Los Angeles, was not filmed in that city or even in the state of California; nearly all of it was filmed in Shreveport and Baton Rouge, Louisiana.[16]

The incentives in the United States have grown since Louisiana became the first state to create a program in 2002.[17] The creation and growth of incentives is a response to "runaway productions," those that leave the U.S. to be produced elsewhere. A 2005 report by the Center for Entertainment Industry Data and Research attributed this trend to factors including financial incentives and exchange rates.[18] The Canadian Production Services Tax Credit, enacted in 1998, offered a rebate of 11% on qualified Canadian labor; individual provinces offered additional rebates on labor that ranged from 11% to 47%, along with other incentives.[19] This credit, coupled with a favorable exchange rate (in June 1998, $1.00 U.S. was worth $1.47 Canadian) [20] 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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Tax Incentives—Credits, Rebates and Refunds

Production incentives in different states vary on certain points. These include the type of incentive offered, qualifying expenditures, and whether a financial cap is allocated to the incentive. The typical forms of incentives are tax credits, tax rebates and refundable tax credits. A state can issue a tax credit to refund a portion of the tax incurred by a production in the state. A tax rebate pays cash, in the form of a check, to a production for certain expenditures made in the state. A refundable tax credit is paid by the state to the production for the balance in excess of taxes owed. The credits are based on qualified expenses, which vary from state to state.

Many states allow tax credits to be "tradable" or "transferrable," meaning that they can be traded for cash, like stock options. 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 cents 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 state's government. The production company then has $270,000 in cash to use at its discretion.

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 project is produced in New York City.[21] 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 cards, and in 30-second commercials on taxicab video monitors.[22] The New York Police Department (NYPD) offers the services of the NYPD Movie/TV Unit, which assists productions in dealing with any filmed scenes that may impact public safety.[23] For the 2014 season, 24 television pilots were shot in New York City.[24]

The types of expenditures included in the incentive vary from state to state. "Qualified expenses" generally cover pre-production, production, and post-production expenditures such as salaries, facilities, props, travel, wardrobe, and set construction. "Qualified labor" includes those individuals whose salaries are covered by the incentive, but many states place a cap on an individual's salary. For example, Georgia has no restriction on salary[25] but Michigan has a $2 million salary cap per individual per production.[26] "Qualified production" usually includes feature films, episodic television series, television pilots, television movies, and miniseries. Most incentives exclude documentaries, news programs, interview or talk shows, instructional videos, sports events, daytime soap operas, reality programs, commercials, and music videos.

Some states have approved projects and later reversed the decision. In 2011, New Jersey Governor Chris Christie blocked a $420,000 tax credit, which was to be issued by the state's Economic Development Authority, to MTV's *Jersey Shore*.[27] New Jersey, which at the time included reality television as a qualified production, had approved the credit before filming the show's first season.[28] 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."[29] This action by Christie brought on a debate about "content neutral" issues in choosing which projects may qualify for a state's incentive.[30]

Some states also have guidelines in choosing which projects are approved based on the project's content. According to the Texas Moving Image Industry Incentive Program, the state may "deny an application or eventual payment on an application because of inappropriate content or content that portrays Texas or Texans in a negative fashion, as determined by the (Film) Commission, in a project."[31] In 2010, after it was produced, the Texas Film Commission denied the incentive for the film *Machete*, which stars Robert De Niro and Danny Trejo, stating that the film portrayed the state negatively.[32] The producers of the film filed a lawsuit against the Texas Film Commission, claiming that officials approved the credits before filming and later denied them.[33] The lawsuit stated that the Commission reviewed and approved the script in 2009—but after the movie trailer was released in May 2010, it ruled that the content was "'inappropriate' or portrayed Texas or its citizens 'in a negative fashion,'"[34] following complaints to the Texas Film Commission that the film contained inappropriate content.[35] The production spent $8 million in the Lone Star State, employing 125 crew and 420 cast members.[36]

Here Today May Not Mean Here Tomorrow

One key consideration in choosing a state based on its financial incentives is that programs can be changed or eliminated at any time. In May 2014, Florida announced that all of the $296 million allocated to the state's incentive program had already been spent, well prior to the program's end date of 2016.[37] Before this announcement, the MPAA released an analysis, showing that Florida's Film and Entertainment Industry Financial Incentive Program—which offered a 20% to 30% transferrable credit—had supported 87,870 jobs, $2.3 billion in wages, and $7.2 billion in economic spending across the state since 2010.[38] Further, the analysis pointed out that—for nearly 20% of visitors—viewing a movie or television series filmed in Florida contributed to their decision to travel to the state.[39] Gus Corbella, chairman of the Florida Film and Entertainment Advisory Council, emphasized that the lack of additional funding by the legislature sends a negative message to producers: "[t]hat kind of roller-coaster ride of financing is detrimental to trying to bring and grow and maintain that kind of business here in Florida."[40] Graham Winick, the film coordinator for the city of Miami Beach and past president of Film Florida, explained that besides scaring off producers, not having a program in place undermines the infrastructure that took decades to build.[41] Staff and crew will move from the state and considerable effort will be required to attract qualified professionals to return when the incentive is reinstated.

In August 2014, North Carolina, which offered a 25% refundable credit and $61 million in incentives in 2013, replaced the incentive with a $10 million grant program starting on January 1, 2015.[42] The cap per production would be $5 million, a quarter of what the state paid to productions such as 2012's *Iron Man 3,* which employed 2,377 people and generated $81 million for the state on a $20 million credit.[43] However, the new program may be a good source for television pilot season, which typically takes place between November and April; these projects will be filmed in the first quarter of the year when grant funds are more likely to be available.[44] The availability of state funds is another concern for producers in utilizing the incentive. No production wants to start filming and find that by the time of completion, the state has spent all of the funds allocated to the program for the term or the year. However, pilot episodes are not usually tied to a specific filming location, so it is possible to begin filming in a state without a commitment to continue an entire series there.[45] *Revenge,* an ABC drama that takes place in New York, generated $5.5 million in spending and received $1.3 million in incentives, while *Hart of Dixie*, a CW comedy-drama that takes place in Alabama, spent $3 million and received $772,816 in incentives.[46] Both shows shot their pilot episodes in North Carolina, but moved to California once they were ordered as a series.[47] As a result of the new incentive, the MPAA stated that North Carolina could lose as many as 4,000 jobs in addition to the overall economic boost brought by a production.[48] According to the North Carolina General Assembly, the reduction in the incentive was intended to create an even economic playing field for all businesses and industries in the state.[49]

From 2008 to 2011, Michigan had one of the most lucrative film incentives in the country—a credit of up to 42%.[50] Clint Eastwood, who in 2008 directed and starred in *Gran Torino*—which takes place and was filmed in the state—proclaimed that Michigan "will be the new film capital of the world."[51] However, when Governor Rick Snyder took office in January 2011, he soon announced that Michigan's Film and Digital Media Production Assistance Program would incur significant cuts.[52] In the most drastic reduction, the previously unlimited incentive would now be subject to a cap of $25 million; in addition, the incentive rebates would also be lowered.[53] 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.[54] In each of these years, $209.3 million with $73 million in credit costs and $322.6 million with $117.2 million in credits costs, respectively, was spent on total production expenditures in Michigan.[55] As a result of this spending, each dollar of net film tax credit cost generated $5.89 in economic output in 2009 and generated $5.94 in 2010.[56]

Other states have taken measures to suspend incentives. Alabama State Senator Del Marsh, who was responsible for creating the state's Entertainment Industry Incentive Act of 2009, proposed re-writing the language of the state's incentive.[57] His proposal was based on a study conducted by the University of Alabama entitled "An Evolution of Alabama's Entertainment Industry Incentives Program and the Economic Impact of the Program's Productions." This study focused on 24 films shot and produced in the state over the last three years; it showed that production companies received more money from the incentive then they should have.[58] Currently, the state has a $15 million cap, which will increase to $20 million in 2015.[59] The bill, which would have suspended the incentive from October 2014 until October 2016, never went for a vote.[60]

Federal film incentives also come and go. In 2004, as part of the American Jobs Creation Act of 2004, Congress enacted 26 U.S.C. §181: 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.[61] 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 U.S.[62] The law expired in December 2011 but was renewed in January 2013 during "Fiscal Cliff" negotiations, as part of the American Taxpayer Relief Act of 2012, for productions that commenced in the 2013 calendar year.[63]

Some of the changes in incentives are not related to the incentive itself, but rather from illegal conduct associated with the incentives. In 2011, Iowa prosecutors charged Tom Wheeler, the state's former film commissioner, with several felonies, including official misconduct, as a result of his handling of state film tax credits.[64] The allegations arose from an internal state audit that found irregularities in approved expenditures, including use of credit funds by filmmakers to purchase a Land Rover and other luxury vehicles for themselves.[65] The audit found that $26 million of the nearly $32 million in tax credits were improperly awarded, either because productions did not qualify for the credit or producers did not submit the required documentation.[66] Further, it was discovered that the film office allowed credits to be paid on estimates of production costs rather than actual expenses, and prosecutors claimed that producers set up shell companies with local addresses which actually purchased goods and services from out of state.[67] Producer Wendy Weiner Runge was sentenced to 10 years in prison after pleading guilty to first-degree fraudulent practices in the misuse of tax credits.[68] Runge's company received $1.8 million in incentives. Invoices showed she inflated prices of items, allegedly paying $225 for a broom, $900 for a step-ladder, and $450 for two shovels; additionally, Runge double-billed several items.[69] Wheeler, the former Iowa Film Office manager, was found guilty of one felony count of misconduct in office, given a deferred judgment, placed on two years' probation, and charged with paying a $750 civil penalty, restitution, and other court costs.[70] In announcing his sentence, the judge noted that Wheeler had not benefited personally from his actions.[71]

In 2012, a Los Angeles movie director pled guilty in Suffolk Superior Court in Massachusetts on charges of making a false claim, larceny, false claims to the department of revenue, and preparing a false tax return.[72] The director had filed inflated or fictitious expenses, falsely claimed withholding on taxes to lead actors' salaries, and inflated the salaries he had paid to the lead actors. This resulted in the director receiving a tax credit overpayment of more than $4 million for the two Cape Cod-based films he was producing.[73] In one example, an actor who was paid $400,000 was reportedly paid $2.5 million in filings with the film office.[74] The director was sentenced to two to three years in prison with a 10-year probation, and ordered to pay more than $4.3 million in restitution to the state.[75]

There is good news for some states. In 2014, the California Senate Appropriations Committee proposed bill AB1839, quadrupling the state's incentive to expand the allocation for tax credits to $400 million a year.[76] It would be the second-highest yearly incentive allocation in the country, behind New York, which offers a $420 million a year allocation.[77] The incentive was also expanded to include shows that air online and "big-budget blockbusters," along with additional incentives to productions that take place outside the Los Angeles area. According to the Bureau of Labor and Statistics, California lost more than 16,000 film and television jobs and more than $1.5 billion in wages from 2004 to 2012.[78] In August 2014 the California Senate amended the proposed allocation, passing the incentive to provide $330 million a year in tax credits for five years beginning in July 2015.[79] The bill is expected to pass the state Assembly and Governor Jerry Brown is expected to sign the bill soon thereafter.[80] With the increase in the cap on California's incentive, Hollywood may reclaim its title as the capital of the movie industry.

More Than the Entertainment Industry

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, was spent on indirect economic activity that support the film industry, including lodging, building rentals, food services, equipment and material rentals, locations, travel services, other contracted services and insurance—a considerable indirect economic impact.[81] Moreover, a "ripple effect" occurred; some of these funds came directly from the production and some from the film crew, who spend part of the salaries they earn in the state by patronizing local retailers. Local tourism is also boosted when visitors come to the set to see the movie being filmed; they may also visit the shooting location after seeing the film. New York offers a "New York TV and Movie Sites Tour," "The Sopranos Sites Tour," and the "Central Park TV and Movie Sites Tour."[82] Each shows tourists where their favorite scenes from popular TV shows and movies were filmed.

Although it was not filmed in the U.S., the 2012 movie *Life of Pi* had an entire tourism campaign built around it by India's Ministry of Tourism.[83] The Leading Hotels of the World offers visitors a chance to stay in famous hotel rooms featured in the movies.[84] There is also the satisfaction gained from recognizing your hometown in the movie and the excitement of spotting celebrities at local restaurants. Movies and television shows that feature the name of a state, city or town also help to increase the public opinion and tourism since the title and city are featured in every poster, movie trailer, and advertisement, such as *Chicago*, *Casablanca, Fargo, Elizabethtown* and *Nashville.*

In May 2013, a report entitled Economic Impacts of the Massachusetts Film Tax Incentive Program, prepared for the MPAA, stated that in 2011, this state generated $375 million in total economic output through $37.9 million in tax incentives awarded.[85] 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.[86]

There are some detractors of the incentives. 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.[87] Further, although most states require a "qualified" purchase under the incentive to be made in the state, Massachusetts allows items to be purchased from out of state so long as they are used on the production—thus, state-based businesses lose out.[88] The report also measured *new* economic activity and did not include filming that occurred before the tax incentive was implemented, based on the presumption that the production would have continued had the incentive not been enacted.[89] Additionally, much of the incentive-related employment is short-term. The Ernst and Young study on Michigan stated that the average production lasts 90 days, and noted employees may not work every day during a single production.[90] Further, although individuals may work steadily for months on a film, they may not work for several months thereafter. A counterargument to short-term employment is that productions still create jobs for people who would otherwise be out of work; 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 for full-time equivalent employees was $53,700 in 2009 and $64,400 in 2010.[91] In 2013, film advocates in North Carolina invited skeptical lawmakers to the set of Showtime's *Homeland* set to meet a few of the 4,000 people statewide who work full-time in film in positions such as prop makers, carpenters, and camera operators.[92] Supporters stated that these individuals put in 15-hour days, earning at least $20 an hour for months on end.[93] Local companies get a boost as well. H & S Lumber in Charlotte stated that Hollywood productions account for 25% of sales, including an order of 50 miles of wood to build sets for *The Hunger Games*.[94] This production spent more than $55 million in the state, employing 1,133 people and received $13.7 million in tax credits.[95] 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).[96] The report concluded that the cost-benefit analysis is one for policy-makers.[97]

Though many residents enjoy the excitement of seeing a movie filmed in their neighborhood, many others dislike the disruption 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.[98] The resident was arrested for assault and the assistant was treated for a broken nose.

"State film incentives have brought not only financial benefits to the states, but publicity as well.… Watching the filming of a soon-to-be blockbuster movie, and seeing Samuel L. Jackson—an A-list star—walk down a neighborhood street, was incredibly exciting for Clevelanders. This type of publicity is difficult to match and even harder to quantify financially."

The Next "Hollywood"

State film incentives have brought not only financial benefits to the states, but publicity as well. Last year, a Cleveland-area friend mentioned that *Captain America 2* was being filmed in front of his office. Days before filming began, in an effort to avoid unnecessary calls to 911, production staff posted signs in the lobby of his office building and surrounding streets warning that gunshots and explosions were being staged in the area. Watching the filming of a soon-to-be blockbuster movie, and seeing Samuel L. Jackson—an A-list star—walk down a neighborhood street, was incredibly exciting for Clevelanders. 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 increasing tax incentives, allowing more qualified expenditures, and by raising or eliminating the cap on states' budgets for the incentives. The fact that changes to film incentives may occur at any time makes producers both excited and anxious, depending on whether the incentive improves or is reduced. Following the announcement of Michigan's reduced incentive cap in 2011, *The Dark Knight Rises* and *The Avengers*,[99] both scheduled to film in Michigan, relocated to Pittsburgh and Ohio respectively. The incentive in Pittsburgh has raised more than $100 million for four consecutive years[100] and Ohio, which offers up to a 35% refundable credit and a $20 million cap, has had over $300 million in economic output since 2009.[101] There is no end in sight to the competition among states to entice productions. Hollywood may be coming to a town near you!

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