

ANALYSIS OF ORIGINAL BILL

Franchise Tax Board

Author: Wyman Analyst: Kimberly Pantoja Bill Number: AB 465

Related Bills: See Legislative History Telephone: 845-4786 Introduced Date: 02/21/2001

Attorney: Patrick Kusiak Sponsor: _____

SUBJECT: Film Production Credit

SUMMARY

This bill would create a credit of one-third of the costs to produce a film.

PURPOSE OF THE BILL

According to the author's staff, the intent of the bill is to utilize the tax system to provide tax incentives to keep the film industry from moving film production activities out-of-state.

This bill is intended to be compatible with the newly-launched federal Small Business Administration's (SBA) loan project designed to help keep production of small, independent films at home to reduce the exodus of film production to other countries. In order to qualify for SBA loans, films must meet community standards relating to violence and sexual content and may not advocate a particular religious or political doctrine.

EFFECTIVE/OPERATIVE DATE

This bill is a tax levy and would be effective upon enactment. The credit would be operative for taxable years beginning on or after January 1, 2001, and does not have a sunset date.

POSITION

Pending.

Summary of Suggested Amendments

Amendments are provided to address the department's technical concern. Department staff is available to assist with amendments to resolve the implementation and policy concerns described below.

ANALYSIS

FEDERAL/STATE LAWS

Existing state law establishes the Film California First Program, which authorizes the Trade and Commerce Agency to pay and reimburse the film costs incurred by a public agency according to specified procedures.

Board Position:

____ S ____ NA ____ NP
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Department Director

Date

Alan Hunter for GHG

05/10/01

Both state and federal laws allow a deduction for all ordinary and necessary expenses of a trade or business, including expenses relating to film production.

Existing state and federal laws generally allow a depreciation deduction to the owner for the obsolescence or wear and tear of property used in a business or investment property. The amount of this deduction is determined, in part, by the cost (or basis) of the property. In addition, the property must have a limited, useful life of more than one year. Depreciable property includes equipment, machinery, vehicles, and buildings, but excludes land. Significant improvements to property increase the basis of the property and are depreciated over its remaining useful life.

Both state and federal laws provide various tax credits designed to provide tax relief for taxpayers that must incur certain expenses (e.g., renter's credit) or to influence behavior, including business practices and decisions (e.g., research credits).

Neither state nor federal laws have a credit comparable to the credit proposed by this bill.

THIS BILL

This bill would create a tax credit equal to 1/3 of the amount paid or incurred for the costs of film production in this state.

The bill defines several terms. "Taxpayer" means any person engaged in film production who is eligible or otherwise qualified for a Small Business Administration loan. "Film" includes feature motion pictures, videotapes, television motion pictures, commercials, and stills. "Production" means the activity of making a film for commercial or noncommercial purposes on property located in this state.

Any excess credit could be carried over until exhausted.

IMPLEMENTATION CONSIDERATIONS

This bill's definition of "taxpayer" specifies that the person must be "engaged" in film production and "eligible" for an SBA loan. However, there is no requirement to specify how frequently the taxpayer must engage in film production. Since "production" may consist of making films for noncommercial purposes, it could be interpreted that any individual who is theoretically "eligible" for an SBA loan could claim a credit on a video camera purchased for home use. Further clarification of the terms used in this bill would help to ensure that the author's intent is met.

Also, the bill's definition of "taxpayer" is inconsistent with the definition of "taxpayer" in the Revenue and Taxation Code (R&TC). Another term such as "qualified taxpayer" would eliminate confusion.

The term "costs" is not defined and could be interpreted to mean everything from purchases of tangible items such as studio buildings, cameras, film, lights, props, costumes, etc., to intangible items such as payment of wages for writers, directors, actors, technical crew, etc., to payments made to outside companies, such as film developers, caterers, or advertisers. A definition for this term would be helpful to prevent disputes between the department and taxpayers.

TECHNICAL CONSIDERATIONS

Amendment 1 is provided to specify the operative date for this credit.

Small Business Administration is capitalized in the personal income tax (PIT) section of the bill, but is not capitalized in the bank and corporation tax (B&CT) section of the bill. Amendments 2 and 3 are provided for consistency.

LEGISLATIVE HISTORY

AB 484 (Kuehl, Stats. 2000, Ch. 699) enacted the Film California First Program.

AB 41 (Wesson, 1999/2000) would have created a tax credit for employer wages paid to television or movie studio employees credit, but that language was deleted from the bill.

AB 358 (Wildman and Kuehl, 1999/2000) would have created a refundable tax credit for the wages and salaries paid for production of or musical scoring for a television program or a motion picture. This bill failed passage in Senate Appropriations.

OTHER STATES' INFORMATION

Review of *Florida, Illinois, Massachusetts, Michigan, Minnesota, and New York* laws found no comparable tax credits or deductions. These states were reviewed because of the similarities between California income tax laws and their tax laws.

FISCAL IMPACT

Once the implementation concerns are resolved, this bill is not expected to impact the department's costs significantly.

ECONOMIC IMPACT

Due to the lack of definitions, almost all costs associated with commercial or noncommercial videotaping, filmmaking, or photographing could qualify for this credit. Therefore, the revenue impact of this bill is potentially in the hundreds of millions of dollars annually.

ARGUMENTS/POLICY CONCERNS

Conflicting tax policies come into play whenever a credit is provided for an expense item for which preferential treatment already is allowed in the form of an expense deduction or depreciation deduction. Since "costs" are undefined, this bill would have the effect of providing a double benefit for a number of items, including depreciable buildings and currently deductible wages and other expenses. On the other hand, making an adjustment to limit the amount of current deductions or reduce basis in order to eliminate the double benefit creates a state and federal difference, which is contrary to the state's general federal conformity policy.

Since costs of film production could be interpreted to include wages, this bill would allow taxpayers located within an enterprise zone to claim both this credit and the enterprise zone hiring credit for the same employee. The enterprise zone credit provisions do not restrict the taxpayer to one credit based upon a single employee.

Also, most wage-based incentive credits in existing law define qualified wages as a percent of minimum wage, rather than allowing credit computations based upon the full amount of wages paid.

This bill does not specify a repeal date or limit the number of years for the carryover. Credits typically are enacted with a repeal date to allow the Legislature to review their effectiveness. However, even if a repeal date were added, the department would be required to retain the carryover on the tax forms indefinitely because an unlimited credit carryover period is allowed. Recent credits have been enacted with a carryover period limitation since experience shows credits are typically used within eight years of being earned.

LEGISLATIVE STAFF CONTACT

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FRANCHISE TAX BOARD'S
PROPOSED AMENDMENTS TO AB 465
As Introduced February 21, 2001

AMENDMENT 1

On page 1, line 3, and page 2, line 16, strike "There" and insert:
For each taxable year beginning on or after January 1, 2001, there

AMENDMENT 2

On page 2, line 22, strike "small business" and insert:
Small Business

AMENDMENT 3

On page 2, line 23, strike "administration" and insert:
Administration