Franchise Tax Board

ANALYSIS OF AMENDED BILL

Author:	Runner/Dutton	Analyst:	Anne Mazur	Bill Number:	SB 359
Related Bills:	See Legislative History	Telephone:	845-5404	Amended Date:	April 9, 2007
		Attorney:	Daniel Biedler	Sponsor:	

SUBJECT: Motion Picture & Commercial Production Credits/Research Expenses Credit Modifications/Joint Strike Fighter or Crew Exploration Vehicle Credit/Extend Repeal Date/Net Receipts In Sales Factor For Treasury Function/Single Sales Factor For Qualified Business Activity

SUMMARY

Under the Personal Income Tax and Corporation Tax laws, this bill would do the following:

- Create tax credits based on certain wages paid or amounts paid to purchase or lease certain property used to produce motion pictures or commercials in California.
- Modify the credit for research expenses to 16% of the excess of the qualified research expenses.
- Modify the alternative incremental research credit (AIRC).
- Re-establish Joint Strike Fighter (JSF) property and wage credits.
- Add Crew Exploration Vehicles (CEV) to the JSF property and wage credits.

Under the Corporation Tax Law, this bill would do the following:

- Change the method used by companies in specified industries to calculate their California net income by modifying the apportionment formula.

Provisions that were added or revised as a result of the April 9, 2007, amendments are discussed separately in this analysis.

This bill would also add provisions to the Sales and Use Tax Law (SUTL). This analysis will not address these changes to the extent they do not impact the department or state income tax revenue.

Board Position:			Department Director	Date
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SUMMARY OF AMENDMENTS

The April 9, 2007, amendments made the following changes:

- Added an author.
- Added provisions to establish motion picture and commercial production credits.
- Added language that would: (1) reenact the JSF credits and establish CEV credits for taxable years beginning on or after January 1, 2007, and revised the repeal date to January 1, 2017; (2) allow any unused credits to be carried over until exhausted; and (3) resolve the technical considerations discussed in the department's analysis of the bill as introduced February 20, 2007.
- Added a specified repeal date of January 1, 2017, for the quadruple-weighted sales factor provisions.
- Removed the provisions of the bill relating to the treasury function.
- Added uncodified provisions to: (1) require the Business, Transportation and Housing Agency to submit an annual report to the Governor and Legislature evaluating the effectiveness of the film production tax credits; (2) provide that the various provisions of this bill are severable; and (3) provide language regarding local mandate reimbursement.

Except for the elimination of analysis sections relating to the treasury function, revision of applicable analysis sections for the JSF/CEV credits, and the addition of an analysis of the motion picture and commercial production credits, the analysis of the bill as introduced on February 20, 2007, continues to apply. A complete analysis of the motion picture and commercial production credits amended into this bill on April 9, 2007, is provided below. Revised <u>Implementation Considerations</u>, <u>Technical Considerations</u>, and <u>Economic Impact</u> sections are added below for the JSF/CEV credits. Technical Considerations are also provided for the sales factor provision.

PURPOSE OF THE BILL

According to the author's staff, the purpose of this bill is to accomplish the following:

1. Increase economic productivity in California.
2. Encourage certain industries to invest in California.

EFFECTIVE/OPERATIVE DATE

This bill is a tax levy and would be effective immediately upon enactment. This bill provides the following operative dates for each of the following provisions:

1. Motion Picture and Commercial Production Credits would be operative for taxable years beginning on or after January 1, 2007, and would be repealed on January 1, 2017. The bill also specifies that the amount upon which the motion picture credit is based does not include any qualified wages paid or incurred for services performed or any qualified property purchased or leased before January 1, 2007. In addition, the bill specifies that qualified production costs for a qualified commercial do not include qualified wages paid or incurred before January 1, 2007.
2. Research and Development Credit: Taxable years beginning on or after January 1, 2007.
3. Joint Strike Fighter Credit: Taxable years beginning on or after January 1, 2007, ending before January 1, 2017, and would be repealed on January 1, 2017.

4. New Revenue & Taxation Code (R&TC) section 25128: Quadruple-Weighted Sales Factor: Taxable years beginning on or after January 1, 2007, ending before January 1, 2017, and would be repealed on January 1, 2017.
5. Current law R&TC section 25128: Taxable years beginning before January 1, 2007, and again for taxable years beginning on or after January 1, 2017.

POSITION

Pending.

Summary of Suggested Amendments

Technical amendments 1 through 10 are attached to correct incorrect phrases and references.

SUMMARY OF ECONOMIC IMPACT

Estimated Revenue Impact of SB 359 Effective for Taxable Years BOA January 1, 2007 Assumes Enactment After June 30, 2007 ($ in Millions)				
	2007/08	2008/09	2009/10	2010/11
Motion Picture/Commercial Production Credits	– $40	– $50	– $55	– $60
Research Credit	– $40	– $50	– $55	– $55
Joint Strike Fighter/Crew Exploration Vehicle Credits	– $25	– $40	– $55	– $75
Quadruple-Weighted Sales Factor	– $125	– $160	– $165	– $165
Total Revenue Impact of this Bill	– $230	– $300	– $330	– $355

This estimate does not consider the possible changes in employment, personal income, or gross state product that would result from this bill.

The estimates for the four provisions above were totaled and extrapolated to subsequent tax years. The extrapolation was based upon the latest Department of Finance forecast of corporate profits. For the 2007 tax year, the total impact of this bill was estimated to be a revenue loss of $229 million. This loss includes a loss of $37 million due to the movie credit provision, a loss of $40 million due to the research credit provision, a loss of $22 million due to the JSF credit provision, and a loss of $130 million due to the quadruple-weighted sales factor provision.
The tax year estimates were then converted to fiscal year estimates, which are shown in the table above. For example, the fiscal year 2007/08 cash flow estimate of a revenue loss of $230 million includes a $130 million loss from the 2007 taxable year, plus a $100 million loss from the 2008 taxable year.

Revenue discussions are included separately below for the motion picture and commercial production credits and the JSF/CEV credits.

QUALIFIED MOTION PICTURE CREDIT AND COMMERCIAL PRODUCTION CREDIT

ANALYSIS

FEDERAL/STATE LAW

Current state and federal laws generally allow taxpayers engaged in a trade or business to deduct all expenses that are considered ordinary and necessary in conducting that trade or business (e.g., employee wages and benefits). However, when a taxpayer produces or creates a product (e.g., video, film, etc.) the taxpayer will generally incur a great portion of the expenses before the product is ready to produce income. When this happens, the taxpayer is usually required to capitalize those expenses and amortize—recover or deduct—them over the period that the product produces income using a specialized cost recovery method called the "income forecast" method. Amortized expenses include costs of researching, preparing, producing, recording, and other direct production costs. It also includes an allocation of indirect costs such as utilities, tools, clerical, and equipment rental.

The federal American Jobs Creation Act (AJCA) of 2004 contains provisions that impact the income tax treatment of motion picture productions. Effective for productions commencing after October 22, 2004, and before January 1, 2009, the AJCA permits qualifying film and television productions to elect to deduct certain production expenditures in the year the expenditure is incurred in lieu of capitalizing the cost and recovering it through depreciation allowances under the income forecast method discussed above. This provision only applies to qualified productions the aggregate cost of which does not exceed $15 million. For this purpose, a qualified film or television production is defined as any production of a motion picture, miniseries, scripted, dramatic television episode, or movie of the week if at least 75% of the total compensation expended on the production is for services performed in the United States. For an episodic television series, only the first 44 episodes qualify under the provision. The AJCA modifies the income forecast method to include certain participations and residuals in the adjusted basis of the property. The AJCA also allows a deduction equal to a portion of the taxpayer's qualified domestic production activities, including any disposition, lease, rental, or license of qualified film produced by the taxpayer. California has not conformed to these provisions.

Current state and federal laws do not provide any tax credits relating to production of commercials or motion pictures.

THIS PROVISION

This provision would create two credits. Each credit will be discussed separately.

Qualified Motion Picture Credit

This bill would create a franchise tax or income tax credit for a percentage of the wages paid or amounts paid to purchase or lease tangible personal property used in the production of a qualified motion picture, as defined, in California that is allocated and certified by the California Film Commission (CFC). The bill would also allow the motion picture credit to be claimed against sales or use tax liability in lieu of the franchise or income tax liability. Any credit unused in a taxable year because it is in excess of the taxpayer's tax liability would be carried over to succeeding years until exhausted. The carryover amount would be available to offset any amounts due to the FTB, Board Of Equalization (BOE), or amounts due under the Unemployment Insurance Code.

Credit Amount – **In general.** 12% of the "qualified amount" of wages and property during the production period of a "qualified motion picture." **Additional 3% for movie of the week and miniseries.**
Maximum Credit:
The lesser of: The amount of initial credit allocation; the amount of credit based on actual allowable expenditures on completion; or $3 million per qualified motion picture.

Qualified Wages – Wages and certain fringe benefits paid or incurred by the production company with respect to a qualified individual for services performed on a qualified motion picture in this state.

Qualified Property – Tangible personal property purchased or leased in California that is used primarily in the production of a qualified motion picture.

Qualified Motion Picture Credit

Initial Allocation
Taxpayer's apply to CFC for initial allocation on first-come-first-served basis under CFC regs.

Filming Starts
Taxpayer uses initial allocation for financing and begins filming within 180 days of initial allocation.

Picture Complete
Motion picture completed; taxpayer submits independent audit to CFC; and makes irrevocable election to claim credit

Final Certification – CFC makes final certification of **qualified taxpayer**; **amount of credit** allowed to each; and **notifies** qualified taxpayer, FTB, and BOE.

Taxpayer Claims Credit on franchise tax, income tax, or sales tax return

Qualified Motion Picture **In general.** A motion picture produced for exploitation in theaters, TV, videotapes, videodiscs, DVDs, or any other digital format or on commercial carriers and at least 75% of the total days spent in principal photography occur wholly in California. **Budget requirements**. **A feature film** qualifies if it has a minimum budget of $3 million and a maximum budget of $75 million. A **movie of the week or miniseries** qualifies if it has a minimum budget of $500,000 and a maximum budget of $75 million. **TV Episode.** Also qualifying is a single episode in a single season (not exceeding 22 episodes) of a TV series that is new to California with a minimum budget of $500,000 and a maximum budget of $1.8 million per episode.

Maximum Allocation – An amount equal to $10 million for each calendar quarter, plus unused credit allocations.

<u>"Qualified amount"</u> does not include any of the following:

- Wages paid or incurred for services performed before January 1, 2007.
- Qualified property purchased or leased before January 1, 2007.

<u>"Qualified motion picture"</u> does not include any of the following:

- Motion picture produced:
  - for private noncommercial use, such as weddings or graduations,
  - by students made as part of any educational course, or
  - for industrial purposes.
- News program, current events or public events program, talk show, game show, sporting event, or awards show.
- Telethon or other production that solicits funds.
- Reality television program.
- A feature where 80% or more of the content consists of computer-generated images.
- Clip-based programming if more than 50% of the content is comprised of licensed footage.
- Documentary.
- Variety program.
- Daytime drama.
- Strip show.
- One-half-hour (air time) episodic television show.
- Any production that falls within the recordkeeping requirements of Section 2257 of Title 18 of the U.S. Code.

<u>"Qualified wages"</u> does not include any of the following:

- Expenses, including wages, in excess of the first $25,000 paid per person per qualified motion picture for writers, directors, music directors, music composers, music supervisors, producers, and performers, other than background actors with no scripted lines.
- Expenses, including wages, for legal or accounting services except production accountants.
- Expenses, including wages, related to new use, reuse, clip use, licensing, secondary markets, or residual compensation, or the creation of any ancillary product, including, but not limited to, a soundtrack album, toy, game, trailer, or teaser.
- Expenses, including wages, paid or incurred with respect to acquisition, development, turnaround, or any rights thereto.
- Expenses, including wages, related to financing, overhead, marketing, promotion, or distribution of a qualified motion picture.

<u>"Qualified property"</u> does not include any of the following:

- A story, script, or scenario to be used for a qualified motion picture.
- The literary, dramatic, or musical material upon which the qualified motion picture is based or may be adapted.
- Any rights relating to the two preceding items.

Commercial Production Credit

This provision would also create a franchise tax or income tax credit for a percentage of the incremental production costs of producing a qualified commercial in California that is allocated and certified by the CFC. Any credit unused in a taxable year because it is in excess of the taxpayer's tax liability would be carried over to succeeding years until exhausted.

Commercial Production Credit

Qualified commercial production company applies to CFC for credit allocation.

Application must contain qualified production costs for the base year and the taxable year.

If limit exceeded, CFC aggregates all applications within 120 days of due date and makes pro rata allocation.

<u>Certification</u> – CFC makes certification of **qualified taxpayer**; **amount of credit** allowed to each; and **notifies** qualified taxpayer and FTB.

<u>Taxpayer Claims Credit</u> on franchise tax or income tax return

<u>Credit amount</u> – 12% of the incremental qualified production costs.

<u>Maximum credit</u> –

The lesser of: <u>$500,000</u> per qualified production company per calendar year, or <u>the credit allocated</u> by the CFC to the qualified commercial production company.

<u>Incremental qualified production costs</u> – Qualified production costs for the taxable year greater than the qualified production costs for the base year.

<u>Qualified production costs</u> – Costs for tangible property used and services directly and predominantly in the production of a qualified commercial. Costs for qualified wages, technical and crew production costs, certain depreciation, and other specified expenses.

<u>Qualified commercial</u>
A commercial or advertisement composed of moving images and sounds that is recorded on film, videotape, or other digital medium, created for display on a network, regional channel, or cable where 75% of the total production days occur wholly in California.

<u>Maximum allocation</u> – An amount equal to $20 million for the 2008 calendar year, plus unused credit allocations.

<u>Pro rata allocation</u> – If the amount allocable to commercial production companies exceeds maximum amount allowed to be allocated in any year, the CFC is required to make a pro rata allocation of that maximum amount.

<u>“Qualified commercial”</u> does not include any of the following:

- Program length production with an advertising component including a documentary length commercial.
- An infomercial.
- A news or current affairs program.
- Interview or talk program.
- Network promotion (short form content intended to promote other programming).
- Game show, sporting event, or award ceremony.
- Daytime drama.
- Reality entertainment programming.
- Program intended primarily for industrial, corporate, or institutional end users.
- Fundraising or political commercial.
- A program consisting primarily of stock footage.
- A program produced by an organization organized under Section 527 of the Internal Revenue Code, relating to political organization.
- Any production that falls within the recordkeeping requirements of Section 2257 of Title 18 of the U.S. Code.

<u>“Qualified production costs”</u> do not include costs for any of the following:

- A story, script, or scenario to be used for a qualified commercial.
- Qualified wages paid or incurred before January 1, 2007.

<u>“Qualified wages”</u> do not include wages, salaries, or other compensation for any of the following:

- Writers,
- Directors,
- Music directors,
- Producers, and
- Performers (other than background actors with no scripted lines who are employed by a qualified commercial production company).

This bill contains special rules for both credits that appear to provide that in the case of an S corporation, the credit can be claimed only by the shareholders and not the S corporation.

IMPLEMENTATION CONSIDERATIONS

The department has identified the following implementation concerns. Department staff is available to work with the author's office to resolve these and other concerns that may be identified.

Verifying certification for the credits when processing returns would result in a new manual workload. Administering this bill would have a relatively small impact on audit workloads if qualifying for the credit includes the requirement that the name of a taxpayer claiming the credit must appear on the list of those qualified taxpayers that were allocated credits by the CFC.

This bill does not limit the number of years for the carryover period. 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 because experience shows credits typically are exhausted within eight years of being earned.

A taxpayer may make an irrevocable election to claim the credit against sales or use tax liability in lieu of the franchise or income tax liability. The applicable provision in the SUTL would be repealed January 1, 2018, but the applicable provisions in the R&TC would be repealed January 1, 2017. Because these provisions are intended to work together, it is suggested that the bill be amended to make the repeal dates the same.

The bill would require the CFC to issue rules and regulations by an unspecified date in 2007 to implement these credits. The bill would also allow such rules and regulations to be adopted on an emergency basis if necessary to meet a March 1, 2008, deadline. It may not be possible for the CFC to issue rules and regulations by either of these dates if this bill is enacted in 2007. It is recommended that the bill be amended to make these two dates consistent.

For the commercial production credit, the bill indicates an aggregate credit allocation amount of $20 million for the 2008 calendar year. Because the bill provides that the credit would be allowed for taxable years beginning on or after January 1, 2007, the bill should be amended to indicate that this amount applies for the 2007 calendar year, and each calendar year thereafter.

The commercial production credit would be a credit on incremental costs; however, the bill contains no mechanism to prevent a production company from creating a new production entity for each commercial production and claiming the credit on the full amount of, rather than the incremental, costs. The author may want to consider adding anti-abuse language.

TECHNICAL CONSIDERATIONS

It appears the intention of this bill is to allow the motion picture and commercial production credits only at the shareholder level and not to allow an S corporation to reduce the entity level tax by any portion of such credits. If this assumption is correct, there are provisions of the bill that are incompatible and internally inconsistent. In addition, staff identified grammatical and reference errors. Amendments 1 through 9 attached to this analysis are provided to correct these issues.

This bill would allow the motion picture/commercial production credits to be claimed for taxable years beginning on or after January 1, 2007. The credits would be repealed on January 1, 2017. If the author's intent is to allow the credits for taxable years beginning on or after January 1, 2007, and before January 1, 2017, the repeal date should be no earlier than December 31, 2017. This would allow fiscal year filers with taxable years beginning in 2016, ending in 2017, and that incur qualified costs in 2017 to claim the credit for that fiscal year. The author may wish to amend the bill to revise the repeal date to December 31, 2017, to include the last fiscal year.

LEGISLATIVE HISTORY

SB 740 (Calderon, 2007/2008) would provide refundable credits otherwise identical to this bill. This bill is currently in the Senate Revenue and Taxation Committee.

AB 777 (Nunez, 2005/2006) would have provided refundable credits otherwise identical to this bill. This bill was held in the Senate Revenue and Taxation Committee.

SB 58 (Murray, 2005/2006) would have provided a refundable franchise and income tax credit for certain wages paid or amounts paid to purchase or lease certain property used to produce a motion picture in California. This bill was held in the Senate Revenue and Taxation Committee.

AB 1830 (Cohn, 2003/2004) and AB 2747 (Wesson, et. al., 2001/2002) would have provided a refundable income tax credit for wages paid in connection with the production of a motion picture in California. AB 1830 did not pass out of the Assembly policy committee. AB 2747 did not pass out of the Senate Appropriations Committee.

AB 484 (Kuehl, 1999/2000), as amended July 14, 1999, would have provided a refundable income tax credit for wages paid in connection with the production of or musical scoring for certain television programs or motion pictures. As enacted, AB 484 (Stats. 1999, Ch. 699) created the Film California First Program within the Technology, Trade, and Commerce Agency to assist in the underwriting of actual costs incurred by production companies filming in California.

AB 358 (Wildman, 1999/2000) would have provided a refundable income tax credit for wages paid in connection with television programs or motion pictures similar to AB 484. AB 358 did not pass out of the Senate Appropriations Committee.

OTHER STATES' INFORMATION

Numerous states and foreign jurisdictions provide incentives to the motion picture industry. Attached as appendices to this analysis are charts compiled by the CFC summarizing the most significant of these incentives.

Recently enacted, the *Oregon* legislature established two film production incentives:

- Effective in 2005, the Greenlight Oregon Labor Rebate Fund, which offers productions a rebate of approximately 6.2% on qualified wages. Income taxes withheld from wages on a qualified production are put into a suspense account at the Oregon Department of Revenue, and rebated back to the production when filming in Oregon is completed. Productions must spend at least $1 million on production-related expenses in Oregon to qualify. This rebate also applies to commercial productions, if a company spends at least $1 million on production expenses in the state in a single year.
- A credit is allowed for contributions to the Oregon Production Investment Fund that is certified by the Oregon Film and Video Office. The credit applies to tax years beginning on or after January 1, 2005, for tax credit certifications issued on or after July 1, 2005.

FISCAL IMPACT

These credit provisions would require a new form or worksheet to be developed to calculate the credits. As a result, this bill would impact the department's printing, processing, and storage costs for tax returns. The additional costs have not been determined at this time. As the bill continues to move through the legislative process, costs will be identified and an appropriation will be requested, if necessary.

It is assumed that FTB's activities to administer this bill would be limited to verifying that the taxpayer claiming the credit is in fact the qualified taxpayer allocated credits by the CFC and then making or denying the credit as applicable. If this assumption—as described in <u>Implementation Considerations</u> section of this analysis—is incorrect or not resolved, the department's costs to administer this bill would be substantial.

ECONOMIC IMPACT

<u>Revenue Estimate</u>

See the chart in <u>Summary of Economic Impact</u> section of this analysis above.

<u>Revenue Discussion</u>

The revenue impact of the movie credit would depend on the amount of qualified wages and tangible personal property paid beginning on or after January 1, 2007. Qualified wages are estimated as the product of the number of employees in the film/video industry, the average weekly wage, the number of workweeks per year, and an adjustment factor to account for the various restrictions relating to the qualified wages. Average weekly wage and employment data are provided by the Employment Development Department.

The amount of qualified wages for the 2007 taxable year is projected to be $1.08 billion derived as follows:

23,800 (employees) X $1,774 (average weekly wage) X 50 (weeks) X 0.51 (adjustment factor)
= $1.08 billion in qualified wages

The amount of qualified tangible personal property is assumed to be equal to one-half of qualified wages. This is based on analysis of the relationship between wages and depreciation expenses as reported on the department's 2002 corporation sample. The amount of wages and qualified property costs are then adjusted downward to account for incomplete movies (25%) and taxpayers failing to take advantage of this credit (10%).

The amount of motion picture production credit—assuming no allocation cap—generated for the 2007 taxable year is projected to be $132 million as follows:

$1.08 billion X (1 + 50%) (qualified wages and qualified property) X (1 − 25%) (adjustment for uncompleted movies) X (1 − 10%) (adjustment for businesses that do not take advantage of the credit) X 12% (credit rate) = $132 million of motion picture production credit.

Because this amount is greater than the $40 million allocation cap, the revenue impact of this credit would be limited to the annual allocation limit of $40 million. It is assumed that 4% of the credits allocated in each year will be determined to have been invalid. It is further assumed that only 65% of the remaining allocated credits will be used by taxpayers for the 2007 taxable year. The net amount of credit that would be used in 2007 is $25 million ($40 million X 96% X 65%).

The revenue impact of the commercial production credit would depend on the amount of incremental qualified production costs (IQPC). It is likely that most commercial productions costs, under this bill, would be treated as incremental. Therefore, for the 2007 tax year, IQPC was estimated to be $293 million, and the incremental commercial production credit generated was $35 million ($293 million X 12% credit rate). Because this amount is greater than the $20 million annual allocation cap, the revenue impact of this credit is limited to the allocation limit of $20 million. It is assumed that 4% of the credits allocated in each year will be determined to have been invalid. It is further assumed that only 65% of the remaining allocated credits will be used by taxpayers for the 2007 taxable year. The net amount of credit that would be used in 2007 is $12 million ($20 million X 96% X 65%).

Combined, it is projected that the motion picture and commercial production credits that would be used in the 2007 taxable year is $37 million ($25 million + $12 million).

LEGAL IMPACT

This bill would require taxpayers to produce motion pictures or commercials in the state to qualify for the credit. This requirement may be subject to constitutional challenge under the Commerce Clause of the United States Constitution.

ARGUMENTS/POLICY CONCERNS

This bill provides that the CFC would allocate credits to a qualified taxpayer based on information required to be included with the taxpayer's application and certify the allowed credits upon completion of the motion picture or commercial in accordance with rules and regulations promulgated by the CFC. Because the bill would require the CFC to certify the allowed credit prior to being claimed on a franchise or income tax return, FTB administration of the credit would be limited to verifying that the taxpayer claiming the credit is in fact the qualified taxpayer allocated credits by the CFC, and then making or denying the credit as applicable. In this regard, administration of the credit would be relatively simple. FTB currently administers the low-income housing credit and the natural heritage preservation credit, both of which are allocated by a designated agency, in this manner. However, if the allocation certification feature were eliminated or if the bill is amended to require FTB to examine returns subsequent to the taxpayer claiming the credit, such examinations would be lengthy, complex, and costly.

Unlike other allocated tax credits, such as the low-income housing credit and the natural heritage preservation credit, this credit does not specifically restrict the taxpayer to be able to claim the credit for the expenses of producing the motion picture or commercial to the owner (or owners) of the motion picture or commercial.

Conflicting tax policies come into play whenever a credit is provided for an item that is already deductible as a business expense or is otherwise reflected as an adjustment to the basis of property for tax purposes. Providing both a credit and allowing the full amount to be deducted (or added to basis) would have the effect of providing a double benefit for that item or cost. On the other hand, making an adjustment to deny the deduction or reduce basis in order to eliminate the double benefit creates a difference between state and federal taxable income, which is contrary to the state's general federal conformity policy.

JOINT STRIKE FIGHTER CREDITS

IMPLEMENTATION CONSIDERATIONS

This bill does not limit the number of years for the carryover period. 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 because experience shows credits typically are exhausted within eight years of being earned.

TECHNICAL CONSIDERATIONS

The bill references[1] credits claimed under R&TC sections 17053.49 and 23649, respectively. Those sections—relating to the manufacturer's investment credit—each expired by their own terms effective January 1, 2004. Therefore, it appears that a JSF or CEV credit could not be claimed on property that is also used as a basis to claim the now expired manufacturer's investment credit.

The bill would allow the JSF/CEV credits to be claimed for taxable years beginning on or after January 1, 2007, and before January 1, 2017. Therefore, the last fiscal year that a credit would be allowed would be for the period beginning December 1, 2016, and ending on November 30, 2017. However, in the bill under the personal income tax and corporation tax law, the JSF property credit repeal date is January 1, 2017, eleven months before the end of the last taxable year the credit is allowed. The author may wish to amend the bill to revise the repeal date to December 1, 2017, to include the last fiscal year.

ECONOMIC IMPACT

Revenue Estimate

See the chart in the Summary of Economic Impact section of this analysis above.

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[1] On page 24, line 38, and on page 52, line 33.

Revenue Discussion

The JSF and CEV budget for 2006 is $4.4 billion and $895 million, respectively. The impact of this bill would depend on the amounts of qualified wages and property under the JSF and CEV programs.

The qualified wages for the JSF and CEV credit are estimated to be $94 and $20 million, respectively. These estimates were based on the assumptions that 10% of the projects would be done in California, wages account for 33% of the contract, 51% of all wages would qualify, and 90% of qualified wages would be filed.

The property cost credits were estimated to be $133 and $27 million, respectively. These estimates were based on the assumptions that 10% of the projects would be done in California. Property costs account for 46% of the contract, and 90% of qualified property costs would be filed.

The amount of JSF and CEV credit generated were estimated to be $73 million as follows:
($94 mil x 50% + $20 mil x 50%) + ($133 mil x 10% + $27 mil x 10%) = $73 million

It was estimated for the 2007 tax year that taxpayers could only use $22 million of the credit generated to reduce their tax liabilities.

QUADRUPLE-WEIGHTED SALES FACTOR

TECHNICAL CONSIDERATIONS

The sales factor section of this bill makes reference to a section of the R&TC that does not exist. Amendment 10, attached to this analysis, would correct this error.

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APPENDIX
SUMMARY OF CURRENT MOTION PICTURE PRODUCTION INCENTIVES OF OTHER STATES

STATE	INCENTIVE	DESCRIPTION
ARIZONA	**TRANSFERABLE TAX CREDIT**	• 20% transferable income tax credit on in-state production expenditures on projects spending $3 million or more (10% when spending under $3 million.) • 50% sales and use tax rebate on purchase or lease of tangible property on productions spending $1 million or more. • To qualify, a production must hire a minimum of AZ residents.
CONNECTICUT	**TRANSFERABLE TAX CREDIT** **WAGE TAX CREDIT**	• 30% transferable tax credit on qualifying production costs (25% credit on productions spending less than $1 million) • 25% nontransferable credit on wages of Connecticut residents.
FLORIDA	**FILM INDUSTRY REBATE PROGRAM**	• 15% reimbursement of qualified Florida expenditures for productions spending at least $850,000. • Funded at $20 million per year. Capped at $2 million per project.
GEORGIA	**INVESTMENT TAX CREDIT**	• 9% Transferable income tax credits on all costs spent in Georgia, plus: • 3% credit on wages paid to GA residents, plus: • 2% credit for TV productions that spend more than $20 million annually, plus: • 3% credit for productions in distressed areas.
HAWAII	**REFUNDABLE TAX CREDIT**	• 15% tax credit on qualified production costs. • 20% tax credit if production takes place in a county with a population of less than 700,000. • Capped at $8 million per project
ILLINOIS	**TRANSFERABLE WAGE TAX CREDIT**	• 20% transferable income tax credit on Illinois production spending, plus: • 15% credit on Illinois wages for employees from geographic areas of high employment or poverty.

Source: California Film Commission (March 2007)

APPENDIX
SUMMARY OF CURRENT MOTION PICTURE PRODUCTION INCENTIVES OF OTHER STATES

STATE	INCENTIVE	DESCRIPTION
LOUISIANA	**TRANSFERABLE TAX CREDIT** **EMPLOYMENT/LABOR TAX CREDIT** **SALES & USE TAX EXCLUSION**	• 25% transferable tax credit on Louisiana spending (if spending exceeds $8 million, otherwise 10% credit) plus: • 10% credit on total aggregate payroll of Louisiana residents (excluding salaries in excess of $1 million) plus: • 4% sales and use tax exclusion
MAINE	**WAGE TAX REBATE**	• 10% wage rebate on non-residents; • 12% rebate on wages of Maine residents
MARYLAND	**WAGE REBATE** **SALES TAX EXEMPTION**	• Wage rebate up to $12,500 per eligible employee for projects spending over $500,000. Funded at $6.8 million per year. • Sales tax exemption
MASSACHUSETTS	**TRANSFERABLE EMPLOYMENT CREDIT** **PRODUCTION TAX CREDIT**	• 20% of Mass. payroll (excluding salaries over $1 million) plus: • 25% on all in-state production costs (excluding payroll) if half the production shoots in state. • Capped at $7 million per project
MICHIGAN	**PRODUCTION REBATE**	• Graduated scale for in-state spend: 12% for $200,000 – 1 million in spending 16% for $1 – 5 million in spending 20% for $5 – 10 million in spending Total program spending $7 million per year.
MINNESOTA	**PRODUCTION REBATE**	• 15% Rebate of qualified production costs. • Program capped at 1.7 million

Source: California Film Commission (March 2007)

APPENDIX
SUMMARY OF CURRENT MOTION PICTURE PRODUCTION INCENTIVES OF OTHER STATES

STATE	INCENTIVE	DESCRIPTION
MISSISSIPPI	PRODUCTION REBATE SALES TAX EXEMPTION	Tiered rebate for in-state expenditures • 20% on the first $1 million of local spend 25% on the next $4 million spend 30% on local spend over $5 million, plus: • 10% rebate for payroll of out-of-state workers • 7% Sales tax exemption for most production purchases.
MONTANA	REFUNDABLE TAX CREDIT	• 12% refundable tax credit on up to $50,000 in wages paid to Montana residents. • 8% credit on total in-state spending.
NEW JERSEY	TRANSFERABLE TAX CREDIT LOAN PROGRAM	• 20% transferable tax credit on in-state production spending if 60% of total production shoots in state. • Loan guarantee program up to $1,500,000 • Sales tax exemption
NEW MEXICO	PRODUCTION TAX REBATE INTEREST FREE LOAN	• 25% rebate on qualifying in-state production and postproduction expenditures • Interest free loan up to $15 million • Job training funds
NEW YORK	REFUNDABLE TAX CREDIT	• 10% refundable tax credit of qualified expenditures, funded at $60 million per year. • City of New York offers the same incentive with a refundable tax credit equal to 5% of qualified expenditures capped at $37.5 million for 3 years
NORTH CAROLINA	REFUNDABLE TAX CREDIT	• 15% refundable tax credit on qualifying in-state production expenses including wages. $7.5 million maximum refund per project.

Source: California Film Commission (March 2007)

APPENDIX
SUMMARY OF CURRENT MOTION PICTURE PRODUCTION INCENTIVES OF OTHER STATES

STATE	INCENTIVE	DESCRIPTION
OKLAHOMA	**REBATE PROGRAM**	• 15% of eligible in state costs. Capped at $5 million per year. • Sales tax exemption on tangible property and services
OREGON	**PROD. INVESTMENT FUND** **VENDOR REBATE** **LABOR REBATE**	• 10% rebate on in Oregon costs, capped at $250,000 per film production • 10% rebate with participating vendors. • 6.2% rebate on Oregon wages.
PENNSYLVANNIA	**INCOME TAX REBATE**	• 20% tax rebate of qualified Pennsylvania costs including wages when productions spend 60% of production costs in-state ($10 million annual cap) • 6% sales tax exemption
PUERTO RICO	**PRODUCTION PROJECT TAX CREDIT**	• 40% transferable labor tax credit (paid to Puerto Rican residents). At least 50% of the shooting must take place in Puerto Rico.
RHODE ISLAND	**TRANSFERABLE TAX CREDIT** **INVESTOR TAX CREDIT (non transferable)**	• 25% tax credit for all Rhode Island spending. Production must spend at least $300,000. • Investor will receive 15% tax credit for budgets between $300,000 and $5 million. For budgets over $5 million, investor will receive 25% tax credit.
SOUTH CAROLINA	**TRANSFERABLE TAX REBATES**	• 20% rebate of total payroll for employees who are subject to South Carolina withholding, if in-state spending is at least $1 million. Plus: • 7% sales tax exemption for purchases of in-state goods and services. Plus: • 30% rebate program for in-state purchases/rentals. • Capped at $28 million annually.
UTAH	**REFUNDABLE TAX CREDIT**	• 10% of Utah production spending. Plus: • 2% rural Utah credit • (maximum $500,000 per production)

Source: California Film Commission (March 2007)

APPENDIX
SUMMARY OF CURRENT MOTION PICTURE PRODUCTION INCENTIVES OF OTHER STATES

STATE	INCENTIVE	DESCRIPTION
WASHINGTION	**PRODUCTION REBATE**	• 20% rebate of qualified production expenses and wages. • Capped at $6 million per year.
WISCONSIN	**REFUNDABLE TAX CREDIT**	• 25% refundable tax credit for in-state expenditures. • 25% non-refundable wage credit up to the first 25,000 in wages.
WYOMING	PRODUCTION REBATE	• 15% rebate on in-state expenditures if at least $500,000 is spent. • Capped at $1 million per year.

Source: California Film Commission (March 2007)

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Attorney Daniel Biedler

FRANCHISE TAX BOARD’S
PROPOSED AMENDMENTS TO SB 359
As Amended April 9, 2007

AMENDMENT 1

On page 30, line 12, and on page 36, line 16, strikeout “(i)”.

AMENDMENT 2

On page 30, strikeout lines 21 through 24.

AMENDMENT 3

On page 34, line 2, after "23685" strikeout “, and”.

AMENDMENT 4

On page 34, line 34, and on page 62, line 36, after “qualified”, insert:

commercial

AMENDMENT 5

On page 36, strikeout lines 25 through 28.

AMENDMENT 6

On page 40, line 13, and on page 68, line 17, strikeout “motion pictures” and insert:

Commercials

AMENDMENT 7

On page 59, line 29, and on page 65, line 38, strikeout “(1)”.

AMENDMENT 8

On page 59, strikeout lines 33 through 36.

AMENDMENT 9

On page 66, strikeout lines 3 through 6.

AMENDMENT 10

On page 73, delete lines 11 through 13, inclusive.