Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

Author:	Fuentes, et. al.	Analyst:	John Pavalasky	Bill Number:	AB 2026
Related Bills:	See Legislative History	Telephone:	845-4335	Introduced Date:	February 23, 2012
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Motion Picture Credit/California Film Commission Extend The Allocation Of Credits Until July 1, 2020, & Extend Limit On Aggregate Amount Of Credits Allocated Through The 2019/20 Fiscal Year

SUMMARY

This bill would extend, for five additional years, until July 1, 2020, the California Motion Picture Credit.

RECOMMENDATION

No position.

PURPOSE OF THE BILL

According to the author's office, this bill is seeking a five-year extension to the existing law.

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective immediately upon enactment. Thus, upon enactment, the California Film Commission (CFC) would be able to accept applications for credit allocations in fiscal years 2015/2016 and each fiscal year thereafter, through and including the 2019/2020 fiscal year.

ANALYSIS

FEDERAL/STATE LAW

Current Federal Law

Depreciation & Expensing

The cost of motion picture films, sound recordings, copyrights, books, and patents are eligible to be recovered using the income forecast method of depreciation. In lieu of capitalizing the cost and recovering it through depreciation, taxpayers may elect to deduct up to $15 million ($20 million if the production expenses are incurred in certain distressed areas) of the cost of any qualifying film and television production, commencing prior to January 1, 2012, in the year the expenditure is incurred.

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Domestic Production Activities Deduction

Qualified film productions are eligible for the domestic production activities deduction. This provision allows a 9 percent deduction (in 2010 and thereafter) of "qualifying production activities income (QPAI)."

- With respect to film productions, QPAI refers to the net income from the license, sale, exchange, or other disposition of any "qualified film" produced by the taxpayer.
- The deduction is limited for a taxable year to 50 percent of the W-2 wages paid by the taxpayer with respect to domestic production activities during such taxable year.
- The law contains special rules in determining the W-2 wage limit for non-corporate business entities, like partnerships and S corporations.
- The deduction is generally allowed for purposes of the Alternative Minimum Tax (AMT).

Definition of Qualified Film. The deduction is available for any motion picture film or video tape (but not sexually explicit films as defined in 18 U.S. Code Section 2257), including television programming, if at least 50 percent of the total production compensation constitutes compensation for services performed in the United States by actors, production personnel, directors, and producers.

Credit

Federal law does not allow any credit for motion picture productions.

Current California Law

Depreciation & Expensing

California conforms to the use of the income forecast method of depreciation for the recovery of costs of motion picture films, sound recordings, copyrights, books, and patents, with modifications. However California does not conform to the federal expensing provision for film and television production.

Domestic Production Activities Deduction

California does not conform to the federal domestic production activities deduction.

California Film & Television Tax Credit

The first taxable year that a tax credit may be taken under this program is on the tax return for 2011, even though credits were allocated by the CFC during fiscal years 2009/10 and 2010/11. The statistics for current year 2011 tax returns will not be available until 2013.

The tax credit to a qualified taxpayer, as defined, is for 20 percent of qualified expenditures, as defined, attributable to the production of a qualified motion picture, as defined, and 25 percent of qualified expenditures, as defined, attributable to the production of a qualified motion picture where the motion picture is a television series relocated to California or an independent film, as defined, in California.

This credit is allocated in the fiscal year that the production begins and is certified by the CFC after the production is completed.

A qualified taxpayer may, in lieu of claiming the credit allowed by this provision, make an irrevocable election to apply the credit amount against qualified sales and use taxes imposed on the qualified taxpayer.

This credit specifically overrides the credit usage limitation rules for credits earned by disregarded entities.

Any credit unused in a taxable year because it is in excess of the taxpayer's tax liability can be taken over a period of six taxable years or until the credit is exhausted, whichever occurs first.

A qualified corporate taxpayer may elect to assign any portion of the credit allowed to one or more affiliated corporations for each taxable year in which the credit is allowed.

For credits attributable to an independent film, the qualified taxpayer is permitted to sell a credit to an unrelated party. The unrelated party is subject to the same requirements as the qualified taxpayer. The qualified taxpayer is required to report to FTB prior to the sale of the credit all required information in the form and manner specified by FTB. Credits may not be sold to more than one taxpayer nor may the credit be resold by the purchaser to another party. In the event that both the taxpayer originally allocated a credit by the CFC and a taxpayer to whom the credit has been sold both claim the same amount of credit on their tax returns, FTB may disallow the credit of either taxpayer, as long as the statute of limitations upon assessment remains open. FTB is authorized to prescribe rules, standards, procedures, and the like to implement this aspect of the provisions. The Administrative Procedures Act requirements regarding regulations do not apply.

Allocation

The aggregate amount of credits that may be allocated by the CFC in any fiscal year is equal to the sum of the following:

- $100,000,000 in credits for the 2009/2010 fiscal year and each fiscal year thereafter, through and including the 2014/2015 fiscal year.
- The unused allocation credit amount, if any, for the preceding fiscal year.
- The amount of previously allocated credit not certified.

Credit Certificate

Tax credits are allowed for taxable years beginning on or after January 1, 2011, in which the CFC issues a credit certificate.

In accordance with rules and regulations promulgated by the CFC, qualified taxpayers must comply with audit requirements prior to the issuance by CFC of the credit certificate. The credit is disallowed if the taxpayer fails to provide the copyright registration number required by the CFC and until this requirement is met.

Annually, the CFC is required to provide the FTB with a list of qualified taxpayers and the tax credit amounts allocated to each qualified taxpayer by the CFC.

THIS BILL

This bill would extend the CFC's requirement to allocate the tax credits five additional years, until July 1, 2020. This bill would also extend the limit on the aggregate amount of credits that may be allocated through the 2019/20 fiscal year.

LEGISLATIVE HISTORY

SB 1167 (Calderon, 2011/2012) is the same as this bill. It would extend the CFC's requirement to allocate the tax credits five additional years, until July 1, 2020, and would also extend the limit on the aggregate amount of credits that may be allocated through the 2019/20 fiscal year. This bill is currently in the Senate Governance & Finance Committee.

AB 1069 (Fuentes, Chapter 731, Statutes of 2011) extended the CFC's requirement to allocate the tax credits for one additional year, until July 1, 2015, and also extended the limit on the aggregate amount of credits that may be allocated through the 2014/15 fiscal year.

SBX3 15 (Calderon, Chapter 09X3-17, Statutes of 2009) enacted the California Motion Picture Credit.

OTHER STATES' INFORMATION

The states surveyed included Connecticut, Florida, Illinois, Louisiana, Michigan, New Jersey, New Mexico, New York, as well as the province of British Columbia, Canada.

Connecticut (CT): **The CT Digital Media & Motion Picture Tax Credit** is a 10 – 30 percent transferable tax credit. It was established in 2006. For income years starting January 1, 2010, the minimum expenditure is $100,000 and the credit amount is dependent on the production's total expenses or costs. Production companies incurring production expenses or costs between $100,000 and $500,000 are eligible for a 10 percent credit, between $500,000 and $1 million are eligible for a 15 percent credit, and over $1 million are eligible for a 30 percent credit. An eligible production company may sell, assign or otherwise transfer the tax credits to another taxpayer. Written notification of such transfer must be submitted jointly by the transferor and transferee no later than thirty (30) days after such transfer. The tax credits must be claimed against the corporation business tax or insurance premium tax for the income year in which final certification for the qualified production is made. Any tax credit not used in the income year in which final certification is made may be carried forward for, or in, the three immediately succeeding income years. The tax credits are nonrefundable.

Florida (FL): The **FL Film & Entertainment Industry Financial Incentive Program** is a 20 – 30 percent transferable tax credit. The funding allocated to the program is $242 million over five years (through June 30, 2015). The priority for qualifying/certifying projects for tax credit awards is determined on a first-come, first-served basis.

Illinois (IL): The **IL Film Services Tax Credit** offers producers a transferable tax credit of 30 percent of all qualified expenditures, including post-production. The Illinois Film Production Tax Credit Act has a sunset of 2021.

Louisiana (LA): The **LA Production Incentive** offers a 30 percent transferable tax credit incentive for total in-state expenditures related to the production of a motion picture. An additional five percent labor tax credit incentive can be earned on the payroll of LA residents that are employed by a state certified motion picture production. The tax credit incentives are fully transferable and LA has no limit to the amount of tax credit incentives that can be earned by a single production.

Michigan (MICH): The **MICH Media Production Credit** offsets, or subsidizes, a percentage of a film's actual production costs, as follows:

- **Michigan Personnel Expenditures** qualify for a 32 percent refund of eligible expenditures in 2012 to 2015.
- **Crew Personnel Expenditures (CPEs)** qualify for a 25 percent refund of eligible expenditures in 2012. CPEs will be reduced 5 percent annually until 2015.
- **Qualified Personnel Expenditures (QPEs)** qualify for a 27 percent refund of eligible expenditures from 2012 to 2015. QPEs will be reduced to 12 percent beginning January 1, 2015.
- **Direct Production Expenditures** qualify for a 27 percent refund of eligible expenditures from 2012 to 2015.

An eligible production can obtain an additional 3 percent incentive on Direct Production Expenditures and Michigan Personnel Expenditures for a production “produced at” at a Qualified Facility or Post-Production Facility in Michigan.

New Jersey (NJ): The **NJ Film Tax Credit** allows a production company to get 20 percent of its qualified film production expenses back in the form of a tax credit, which can be used to offset NJ state corporate business tax. In order to qualify, 60 percent of the production company’s total production expenses, excluding postproduction costs, must be incurred in NJ. If the production company earning the tax credit cannot use it, the tax credit may be sold to another eligible NJ taxpayer. The tax credit applies to tax periods beginning on and after July 1, 2005 and is set to sunset in 2015. **NJ Exemption From Sales Tax** - Certain tangible property used directly and primarily in the production of films and television programs is exempt from New Jersey's seven percent sales tax.

New Mexico (NM): The **NM Film Production Tax Credit** is a fully refundable 25 percent tax credit on all production expenditures (including NM labor) that are subject to taxation by NM.

New York (NY): The **NY State Film Production Credit** is a fully refundable 30 percent tax credit on qualified costs incurred in New York State. NY legislation enacted in August 2010 created an additional pool of funding (“Pool 2”) for the NY State Film Production tax credit program. The new funding allocated to the program is $420 million per year for calendar years 2010-2014 inclusive. Up to $7 million per year of this total amount will be available to the newly created, separately administered **NY State Post Production Credit**.

<u>British Columbia (BC):</u> The **BC Basic Production Services Tax Credit** is equal to 35 percent of a corporation's accredited qualified BC labor expenditure for the tax year. An additional six percent of a corporation's accredited qualified BC labor expenditure for the tax year is allowed for **Distant Location Production Services Tax Credit** – Prorated by the number of days of principal photography done in a distant location in BC, over the total number of days in which principal photography is done in BC. An additional 12.5 percent of a corporation's accredited qualified BC labor expenditure for the tax year is allowed for **Regional Production Services Tax Credit** – Prorated by the number of days the principal photography of the production is done in BC outside the Vancouver area, over the total number of days in which principal photography is done in BC; In addition, the **Digital Animation or Visual Effects (DAVE) Production Services Tax Credit** of 17.5 percent of the accredited qualified BC labor expenditure directly attributable to prescribed DAVE activities.

FISCAL IMPACT

This bill would not significantly impact the department's costs.

ECONOMIC IMPACT

<u>Revenue Estimate</u>

Estimated Revenue Impact of AB 2026 For Taxable Years Beginning On or After January 1, 2012 Enactment Assumed After June 30, 2012 ($ Millions)			
2012-13	2013-14	2014-15	2015-16
$0	$0	-$5.1	-$22

The table does not show revenue losses for later fiscal years, which are estimated to total -$473 million. This analysis does not account for changes in employment, personal income, or gross state product that could result from this bill.

SUPPORT/OPPOSITION

Support:

American Federation of Television and Radio Artists
California Labor Federation
California Taxpayers Association
Directors Guild of America
IATSE
Teamsters - Local 399
Los Angeles County Federation of Labor
Los Angeles Chamber of Commerce
Motion Picture Association of America
American Federation of Musicians – Local 47
Recording Musicians Association
Screen Actors Guild

Opposition: None at this time

ARGUMENTS

Pro: Proponents argue that the program, which launched in July 2009, specifically targets productions that are most likely to leave the state due to incentives being offered in other states and countries. It has enabled California to remain competitive and to keep many of those at-risk films in state.

Con: Opponents may say that with the state's current fiscal crisis, additional tax expenditures should be avoided.

LEGISLATIVE STAFF CONTACT

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