ANALYSIS OF AMENDED BILL

Franchise Tax Board

Author:	Nazarian	Analyst:	Jane Raboy	Bill Number:	AB 2700
Related Bills:	See Legislative History	Telephone:	845-5718	Amended Date:	April 1, 2014
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SUBJECT: CA Motion Picture Qualified Post Production Costs Credit

SUMMARY

This bill would create a credit, under the Personal Income Tax Law (PITL) and the Corporation Tax Law (CTL), for certain motion picture costs.

RECOMMENDATION

No position.

Summary of Amendments

The April 1, 2014, amendments removed the bill's provision that would have made a technical, nonsubstantive change to the existing motion picture credit under the PITL and replaced it with the provisions discussed in this analysis.

This is the department's first analysis of the bill.

REASON FOR THE BILL

The reason for this bill is to stimulate the economy by increasing the post-production industry presence in California.

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2015.

ANALYSIS

FEDERAL/STATE LAW

Existing state and federal laws provide various tax credits designed to provide tax relief for taxpayers who incur certain expenses (e.g., child adoption) or to influence behavior, including business practices and decisions (e.g., research credits or economic development area hiring credits). These credits generally are designed to provide incentives for taxpayers to perform various actions or activities that they may not otherwise undertake.

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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.

FEDERAL LAW

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

STATE LAW

For taxable years beginning on or after January 1, 2011, a qualified taxpayer, as defined, may claim a credit for qualified expenditures, as defined, that is equal to either applicable percentage:

- 20 percent of qualified expenditures attributable to the production of a qualified motion picture in California; or
- 25 percent of qualified expenditures attributable to the production of qualified motion picture that is either a television series that relocated to California or an independent film.

A qualified motion picture is defined as a motion picture produced for distribution to the public that is one of the following:

- A feature film with a production budget between $1 million and $75 million;
- A movie of the week or miniseries with a minimum production budget of $500,000;
- A new television series produced in California with a minimum production budget of $1 million licensed for original distribution on basic cable;
- An independent film, as defined; or
- A television series that relocates to California with no minimum budget and is produced for any media outlet.

The California Film Commission (Commission) administers the existing motion picture credit and authorizes the allocation of credits, establishes program guidelines, application, and certification procedures.

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

- $100 million in credits for the 2009/2010 fiscal year and each fiscal year thereafter, through, and including the 2016/2017 fiscal year, which must be allocated before July 1, 2017.
- The unused allocation credit amount, if any, for the preceding fiscal year.
- The amount of previously allocated credit not certified.

The credit is allocated by the Commission in the fiscal year that the production begins and is certified by the Commission after the production is completed. A taxpayer is required to apply to the Commission to claim the credit. The Commission is required annually to provide the Franchise Tax Board (FTB), Legislative Analyst's Office, and the Board of Equalization a list of the taxpayers and the tax credit amounts allocated to each taxpayer by the Commission.

A qualified taxpayer may sell the existing motion picture credit attributable to an independent film, to an unrelated party. The unrelated party is subject to the same requirements as the qualified taxpayer. Prior to the sale of the credit, the qualified taxpayer is required to report to the FTB all required information in the form and manner specified by the FTB.

The existing motion picture credit may not be sold to more than one taxpayer or resold by the purchaser. In the event that both the taxpayer originally allocated a credit by the Commission and a taxpayer to whom the credit has been sold claim the same amount of credit on their tax returns, the FTB may disallow the credit of either taxpayer, as long as the statute of limitations upon assessment remains open.

Like other credits under the CTL, a qualified 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.

THIS BILL

For taxable years beginning on or after January 1, 2015, a qualified taxpayer would be allowed a credit equal to 25 percent of qualified post production costs for a qualified motion picture at a qualified production facility.

This bill would define the following terms and phrases:

- "Qualified taxpayer" would mean a taxpayer who has paid or incurred qualified post production costs and has been issued a credit certificate by the Commission.
    - For pass-thru entities, a "qualified taxpayer" determination would be made at the entity level and the credit would not be allowed to the pass thru (including an "S" corporation) with respect to the tax imposed on "S" corporations under Part 10 or Part 11 but passed through to the entity's partners or shareholders.
- "Qualified post production costs" would mean amounts paid or incurred to perform post production work on a qualified motion picture including, but not limited to, amounts paid or incurred for tangible personal property purchased or leased, and used, within this state in the post production of a qualified motion picture and any payments, including qualified wages, for services performed within this state in the post production of a qualified motion picture.
- "Qualified motion picture" would mean a motion picture that is produced for distribution to the general public, regardless of medium, that is one of the following:
    - A feature with a minimum production budget of one million dollars ($1,000,000).

  - A movie of the week or miniseries with a minimum production budget of five hundred thousand dollars ($500,000).
  - A new one-hour television series of episodes longer than 40 minutes each of running time, exclusive of commercials, that is produced in California, with a minimum production budget of one million dollars ($1,000,000) per episode.
  - An independent film.
  - A television series that relocated to California.
  - A television series.
  - A pilot for a new television series that is longer than 40 minutes of running time, exclusive of commercials, that is produced in California with a minimum production budget of one million dollars ($1,000,000).
- "Qualified post production facility" would mean a post production facility located in the state and engaged in finishing a qualified motion picture.

No credit would be allowed for any qualified post production costs at a qualified production facility, if a credit for those same costs has been claimed under the existing motion picture credit.[1]

The Commission would be required to allocate and certify credits on or and after July 1, 2015, and before July 1, 2020, based on the applicable percentage of all qualified post production costs paid or incurred for a qualified motion picture. The credit would be allowed for the taxable year and in the amount specified in the credit certificate issued by the Commission.

The aggregate amount of credits that may be allocated by the Commission in any fiscal year would be an amount equal to the sum of all of the following:

- The ____amount for the 2015-16 fiscal year and each fiscal year thereafter, through and including the 2019-20 fiscal year.
- The unused allocation credit amount, if any, for the preceding fiscal year.
- The amount of previously allocated credits not certified.

A qualified taxpayer may sell the credit to an unrelated party. A party acquiring the credit would be subject to the requirements of this bill and any credit sold by an owner of a disregarded entity would not be subject to the normal credit limitation applicable to owners of disregarded entities.[2]

Prior to the sale of the credit, the qualified taxpayer would be required to report to the FTB in the form and manner specified by the FTB, all required information regarding the purchase and sale of the credit, including the social security or other taxpayer identification number of the unrelated party to whom the credit would be sold, the face amount of the credit sold, and the amount of the consideration received for the sale of the credit.

Any unused credit may be carried over for six years, if necessary, until the credit has been exhausted.

A credit may be sold to only one unrelated party and may not be resold.

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[1] Revenue and Taxation Code (RTC) Sections 17053.85 and 23685.
[2] RTC Sections 17039(g) and 23036(i).

A qualified taxpayer would be prohibited from assigning or selling any tax credit to the extent the tax credit is claimed on any tax return of the qualified taxpayer. If both a qualified taxpayer originally allocated a credit by the Commission and a taxpayer to whom the credit has been sold both claim the same amount of credit on their tax returns, the FTB may disallow the credit of either taxpayer, as long as the statute of limitations remain open.

Any standard, criterion, procedure, determination, rule, notice, or guideline established or issued by the FTB would be exempt from the requirements of the Administrative Procedures Act.[3]

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.

Under PITL and CTL, this bill would allow a qualified taxpayer to amend a tax return in a subsequent year making it difficult to verify and associate the expenditure to when the credit was earned. Additionally, elections are made on timely filed original returns and are irrevocable once made. The author may wish to amend this bill to require that the credit be claimed on a timely filed original return and specifically require for the year of sale or assignment under CTL that the sale or assignment be shown on the original return to prevent disputes between taxpayers and the department.

TECHNICAL CONSIDERATIONS

Subdivision (a) needs to be amended where the phrase "qualified production facility" appears, as it should be "qualified post production facility" to correspond to the definition in subdivision (b).

The CTL reference in the PITL provision has no legal effect and is unnecessary. On page 6, line 37, the term "assign" should be eliminated.

"Section 23695" on page 10, line 13, needs to be amended, as it should be "Section 23685" to correspond to the correct section of the law.

"Subdivision (g) of Section 17039" on page 15, line 15, needs to be amended, as it should be "Subdivision (i) of Section 23036" to correspond to the correct section of the law.

"Section 23696" on page 17, line 1, needs to be amended, as it should be "Section 17053.96" to correspond to the correct section of the law.

LEGISLATIVE HISTORY

AB 286 (Nazarian, 2013/2014) would modify the existing motion picture credit. AB 286 is currently held at desk in the Assembly.

AB 1189 (Nazarian, 2013/2014) would extend the Commission's authority to allocate and certify the existing motion picture credit by five years, until July 1, 2022, and would increase the aggregate amount of credits awarded from $800 million to approximately $2.2 billion. AB 1189 is currently held at desk in the Assembly.

[3] Chapter 3.5 (commencing with Section 11340) of Part 1 of Division 3 of Title 2 of the Government Code.

AB 1780 (Donnelly, 2013/2014) would create a credit for the production of a qualified motion picture. AB 1780 is currently in the Assembly Revenue & Taxation Committee.

AB 1839 (Gatto, Bocanegra, et. al., 2013/2014) would create a new motion picture credit and would authorize the Commission to administer the credit, allocate tax credits, and establish program guidelines, application, and certification procedures. AB 1839 is currently in the Assembly Revenue & Taxation Committee.

AB 2026 (Fuentes, Chapter 841, Statutes of 2012) extended the Commission's authority to allocate and certify the existing motion picture credit from July 1, 2015, to July 2017.

AB 1069 (Fuentes, Chapter 731, Statutes of 2011) extended the Commission's authority to allocate and certify the existing motion picture credit from July 1, 2014, to July 2015.

SB 1167 (Calderon, 2011/2012) would have extended the Commission's authority to allocate and certify the existing motion picture credit two additional years, until July 1, 2017, and increased the limit on the aggregate amount of credits that could have been allocated through the 2016/2017 fiscal year. SB 1167 was held in the Senate Appropriations Committee.

ABX3 15 (Krekorian, Chapter 10, Statutes of 2009) and SBX3 15 (Calderon, Chapter 17, Statutes of 2009) established and required the Commission to administer the existing motion picture credit's allocation and certification program.

SB 1197 (Calderon, 2009/2010) would have extended, for two additional years, until July 1, 2017, the existing motion picture credit. SB 1197 was held in the Assembly Revenue & Taxation Committee.

OTHER STATES' INFORMATION

The states surveyed include *Florida, Illinois, Massachusetts, Michigan, Minnesota, and New York.* These states were selected due to their similarities to California's economy, business entity types, and tax laws.

Florida and Massachusetts do not provide a credit comparable to the credit allowed by this bill.

Illinois' Film Production Tax Credit Act offers producers a transferrable credit of 30 percent of all qualified expenditures, including postproduction.

Michigan allows a partial reimbursement for qualifying costs associated with producing motion pictures, television series, or other qualifying digital productions, including postproduction. Direct production expenditures relating to the production may be eligible for a 27 percent incentive and an additional 3 percent credit of direct production expenditures and Michigan personnel expenditures may be awarded if qualified production is produced at a qualified facility or postproduction facility.

Minnesota has a Film Jobs Production Program that offers a reimbursement of 20 percent to 25 percent of production expenditures and is available for post production expenditures. Additionally, *Minnesota* offers a commercial sales tax exemption for post production expenditures.

New York offers a refundable 30 percent credit (35 percent for an upstate production) on qualified post production costs paid for the production of a qualified film at a qualified post production facility in New York State. To be eligible for the credit, 75 percent of the total post production costs must be attributable to property or services in New York State. Only 50 percent of any excess post production credit may be treated as an overpayment and carried forward to the following year. Additionally, the New York State Film Commission offers a separate production tax credit program.

FISCAL IMPACT

This bill would impact the department's printing, processing, and systems. As the bill continues to move through the legislative process, costs will be identified and an appropriation will be requested, if necessary.

ECONOMIC IMPACT

Revenue Estimate

The bill, as amended April 1, 2014, would establish a motion picture post production credit under the PITL and CTL; however, the aggregate amount of the credits that may be allocated was left blank. Absent this information, the FTB is unable to calculate the revenue impact of this bill at this time.

SUPPORT/OPPOSITION[4]

Support: None provided.

Opposition: California School Employees Association and California Teachers Association.

ARGUMENTS

Proponents: Some supporters may argue that additional incentives are needed to expand and improve state competiveness in attracting and retaining motion picture production activity.

Opponents: Some have questioned whether motion picture credits have an appreciable long-term benefit to the state.

LEGISLATIVE STAFF CONTACT

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[4] As noted in the Assembly Committee on Arts, Entertainment, Sports, Tourism, and Internet Media bill analysis, dated May 6, 2014.