**SB 596**

# Department of Legislative Services

Maryland General Assembly
2009 Session

## FISCAL AND POLICY NOTE

Senate Bill 596 (Senator Kasemeyer, *et al.*)
Budget and Taxation

**Income Tax - Film Production Activity Credit**

This bill converts the existing Film Production Rebate Program into a tax credit program that is not subject to an annual appropriation. The value of the subsidy to each qualifying company will increase from 25% to 28% of qualified costs. There is no maximum amount of credits that can be claimed in each year or by any one entity. The bill also alters several provisions related to eligibility and reporting requirements at the Department of Business and Economic Development (DBED).

The bill takes effect July 1, 2009, and applies to tax year 2009 and beyond.

## Fiscal Summary

**State Effect:** General fund revenues decrease by $12.0 million in FY 2010 due to tax credits claimed for eligible film production expenses. General fund expenditures decrease by $2.0 million in FY 2010 due to repeal of the film production rebate program. Future year revenues reflect estimated amount of credits awarded and claimed in each year, whereas expenditures reflect the elimination of the rebate program. Revenue losses may be significantly higher than estimated and may approach $100 million in any fiscal year.

| ($ in millions) | FY 2010 | FY 2011 | FY 2012 | FY 2013 | FY 2014 |
|---|---|---|---|---|---|
| GF Revenue | ($12.0) | ($50.0) | ($64.0) | ($66.0) | ($60.0) |
| GF Expenditure | ($2.0) | ($2.0) | ($3.9) | ($3.9) | ($3.9) |
| Net Effect | ($10.0) | ($48.0) | ($60.1) | ($62.1) | ($56.1) |

*Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate effect*

**Local Effect:** None.

**Small Business Effect:** Minimal.

## Analysis

**Bill Summary:** A film producer that meets the requirements of the bill and is approved by DBED will receive a tax credit equal to 28% of qualified film production costs incurred in the State. If the tax credit exceeds the total tax liability in the tax year, the film producer can claim a refund (direct payment from the State) in the amount of the excess. In order to qualify for the tax credit, the estimated total direct costs incurred in the State must exceed $500,000.

Total direct costs include: (1) employee wages and benefits; (2) fees for services; (3) expenses for acquiring or leasing property; and (4) any other expense necessary to carry out a film production. Total direct costs does not include any salary, wages, or other compensation for personal services of an individual who receives more than $1 million in salary, wages, or other compensation for personal services in connection with any film production activity.

The film producer must notify DBED of its intent to seek the tax credit before production begins. A film producer is also required to submit an application containing specified information, including a description of the activity; a detailed budget with estimated number of employees and estimated wages; anticipated dates for carrying out major elements of the film production activity; and any other information required by DBED. DBED may require that the information be verified by an independent auditor selected and paid for by the film production entity.

Film production activity is defined as the production of a film or video product that is intended for nationwide commercial distribution and includes a(n): feature film, television project; commercial; infomercial; corporate film; music video; digital project; animation project; or multimedia project. Film production does not include a: student film; noncommercial personal video; sports broadcast; broadcast of a live event; or talk show.

By January 1 of each year, DBED must report to the Governor and the General Assembly on the number of applicants and the number and amount of tax credit certificates issued in the prior year. DBED and the Comptroller's Office are required to jointly adopt regulations to implement the bill.

**Current Law:** Chapter 96 of 2005 established the Film Production Employer Wage Rebate Grant Program. To qualify for the rebate, a film production activity must be intended for nationwide distribution and have direct costs in the State of at least $500,000, which may include wages and benefits, fees for services, or any other necessary expense. Eligible activities include, but are not limited to, films, commercials, and animation projects. The rebate is not available to sports broadcasts, live events, talk shows, or student films. DBED must determine whether the producer of the production is eligible for the rebate.

Chapter 96 also established the Film Production Employer Wage Rebate Fund, which is used to make rebate grants and pay the administrative expenses of the fund. The fund consists of money appropriated by the State, repayment of defaulted grants, and any other money made available to it by DBED. In each fiscal year, the maximum amount of subsidy payments made by DBED is limited to the amount of money appropriated to the rebate fund.

Chapter 87 of 2007 altered the value of the subsidy received by a company *from* a rebate of 50% of the first $25,000 of each qualified employee's wages (up to a total maximum of $2 million), *to* a maximum of 25% of the direct costs of the film production activity. This does not apply to employees earning over $1 million for a production. Chapter 87 did not cap the total amount of the award to each company and provided that the actual amount disbursed is at the discretion of DBED.

By December 31 of each year, DBED must report to the Governor and the General Assembly on the rebates granted in the prior fiscal year. The report must include:

- the number of local technicians, actors, and extras hired;
- a list of companies doing business in the State that provided direct goods or services for film production activity, including hotels; and
- any information indicating economic benefits of the rebates.

In addition to the wage rebate program, Chapter 432 of 2000 exempts the sale of tangible personal property or a taxable service that is used directly in connection with a "film production activity" from the State sales and use tax. Tangible personal property or a taxable service include items such as film, camera equipment, vehicle rentals, lighting and stage equipment, and props. The film producer or production company must apply to DBED for certification of eligibility for the exemption. DBED issues certificates to production companies filming in Maryland that provide for a sales tax exemption for the goods described above.

**Background:** In response to incentives and cost advantages offered in other countries, a handful of states earlier this decade began offering subsidies in order to attract local film production. Competition among states and other countries has led to a proliferation of subsidy programs – about 40 states offer significant subsidies to the industry. In addition, states have increased the value of subsidies in this more competitive environment.

Although the film industry has expanded outside of California and New York, employment remains concentrated in these two states. About 58% of the industry's workforce remains in California, 16% are in New York, and 1% in Louisiana.

*Maryland Film Industry and Subsidy Program*

**Exhibit 1** illustrates the estimated amount of film-related production (films, commercials, music videos, and television programs) occurring in Maryland and the amount of subsidy payments in fiscal 2006 through 2008. Except for fiscal 2006, the first year of the program, total film-related expenditures have not increased markedly under the rebate subsidy program. In fiscal 2008, expenditures totaled $40.3 million, about 3% higher than the average amount of expenditures for the four years prior to the program's inception.

**Exhibit 1**
**Maryland Film-related Expenditures and Subsidy Payments**
**FY 2002-2008**
**($ in Millions)**

| | **2002** | **2003** | **2004** | **2005** | **2006** | **2007** | **2008** |
|---|---|---|---|---|---|---|---|
| Films | $16.8 | $29.7 | $9.7 | $10.0 | $26.9 | $6.6 | $27.3 |
| Television | 9.8 | 21.0 | 16.9 | 13.3 | 35.9 | 12.7 | 2.4 |
| Commercials | 4.4 | 4.6 | 4.3 | 5.2 | 6.7 | 4.3 | 6.0 |
| Other | 3.3 | 2.7 | 3.8 | 2.1 | 3.2 | 9.0 | 4.6 |
| **Total** | **$34.3** | **$58.0** | **$34.7** | **$30.5** | **$72.7** | **$32.6** | **$40.3** |
| Subsidy Payments | $0 | $0 | $0 | $0 | $4.0 | $6.9 | $4.0 |

Source: Maryland Film Office

The Maryland Film Office estimates that, in fiscal 2009 and 2010, film-related expenditures will decline to $25 million annually. The proposed State budget includes $2.0 million in funding for the subsidy program in fiscal 2010. A recent report estimated that the film industry employed 2,200 individuals in the State; less than one-tenth of 1% of total nonfarm employment in the State. Although modest compared with other states, through fiscal 2010 a total of $19.3 million in subsidies will be paid – an annual average of $3.9 million. Although Maryland has numerous business tax incentives, few business tax credits are explicitly available to one particular industry. By comparison, an average of $6 million has been appropriated to the biotechnology investment tax credit. The State biotechnology industry employed over 26,000 individuals in 2007. Maryland faces fierce competition from other states that have dedicated substantial resources to establishing and maintaining a film industry. In 2004, production of the film *Annapolis* was relocated from Maryland to Pennsylvania in part because Philadelphia and Pennsylvania offered between $2 to $3 million in subsidies. In another example, Baltimore City was reportedly being considered as the site for the recent film *The Curious Case of Benjamin Button* before the State of Louisiana ultimately paid a $27.1 million subsidy to the film's production company.

*Programs in Other States*

The following section discusses film subsidy programs in several states along with information on the impact on state economies and government finances. **Appendix 1** lists information on subsidy programs offered in each state.

*Louisiana*

Louisiana was one of the first states to aggressively subsidize the film industry. The Motion Picture Incentive Act of 2002 created a tax credit for up to 15% of all production dollars (including out-of-state) and up to 20% for wages paid to residents. Legislation in 2005 altered the program by restricting the production credit to in-state production (now a 25% tax credit) and an additional 10% for wages paid to Louisiana residents. A tax credit was also created for interactive media and film production infrastructure. In 2007, a state law tightened oversight of the program after the state film commissioner was investigated, and later pleaded guilty, for accepting bribes to help inflate tax credits. The 2007 legislation also clarified that construction related to condominiums and golf courses did not qualify for the infrastructure tax credit.

A recent study prepared for the Louisiana Economic Development Department analyzed the economic impact of the program. The study determined that the film production program increased film industry employment substantially through 2007. About 215 films produced in Louisiana were awarded credits between 2002 and 2008. In 2007, the industry had an estimated annual economic impact of $763 million. Employment in the film industry increased from 926 in 2001 to 3,056 in 2007 with an average wage of $37,200. The study noted that many jobs in the industry are often characterized by seasonal, short-term projects and not traditional full-time employment. The study likely over-estimates the net impact to the state as it did not consider any potential negative impacts from a decrease in state revenues.

Since the program's inception, Louisiana has issued nearly $500 million in tax credits, of which about one-half have been utilized to date. A total of $115.1 million in credits were issued in tax year 2007 and, after accounting for expanded economic activity, the net state fiscal impact was estimated to be a reduction in state tax revenues of between $59.7 and $91.3 million. The range in the estimate was mainly due to assumptions on the amount of credits that will actually be claimed in the year. The estimated impact on the state's revenues is similar to those found by analyses of the program conducted by the Louisiana Legislature's chief economist. A 2005 analysis concluded that after accounting for the dynamic effects on the economy of the additional film and production activity, the state can expect to recoup 16% to 18% of the tax revenue dedicated to the program.

*Pennsylvania*

Pennsylvania established a film production subsidy program in 2004. Legislation enacted in 2007 expanded the subsidy program by allowing a credit for 25% of a wide range of film production expenditures that occur in the commonwealth. In order to qualify, a minimum of 60% of the film's total production costs must be qualified Pennsylvania expenditures. The maximum $75 million in credits was awarded in fiscal 2009. The Pennsylvania Department of Community and Economic Development estimated that the credits generated $18.3 million in new state revenues.

*Michigan*

In April 2008, Michigan enacted the Michigan Film Production Incentive Program which provides a refundable, assignable tax credit of up to 42% of the amount of a production company's qualified expenditures incurred in producing a motion picture or other media entertainment project in the state. This credit is in addition to a 25% tax credit for companies that invest in new film and digital media studios in the state and a 50% tax credit for on-the-job training expenses. Under the production credit, a credit can be claimed for 40% of qualified Michigan expenditures and an additional 2% for purchases and transactions in 103 "core communities." Qualified expenditures include wages and salaries paid to Michigan residents and goods and services purchased from Michigan businesses. In addition, expenses paid to creative talent qualify for a 40% credit while expenses paid to noncast crew members qualify for a 30% credit. As of February 3, 2009 credit certificates have been issued to 32 productions with qualified expenditures of $126.4 million. If all of the approved film projects go into production, a total of $164.4 million in credits will be awarded for $435.7 million in expenditures. The current Michigan revenue forecast projects that the production credit will decrease revenues by $100 million in fiscal 2009 and by $150 million in fiscal 2010. Including other film-related tax credits, total revenues are projected to decrease by $107.5 million in fiscal 2009 and by $160.0 million in fiscal 2010.

*New York*

The New York Legislature created the Empire State Film Production Credit in 2004. Subsequent legislation enacted in 2008 expanded the program by increasing the credit rate from 10% to 30% of qualified production costs, making the credit fully refundable in the first year, and increasing the total amount of credits that can be awarded. A total of $65 million in credits can be awarded in 2008, $75 million in 2009, $85 million in 2010, $90 million in 2011 and 2012, and $110 million in 2013. To qualify, 74% of film production expenditures must be spent in a New York production facility. In 2004 through 2007, a total of $117.3 million in credits have been awarded at the previous rate of 10% for approximately $1.2 billion in qualified costs. In addition, New York City offers an additional 5% credit for qualified production in the city. A total of $30 million per year has been allocated to the city program.

*Connecticut*

The Connecticut film tax credit, enacted in 2006, awards credits for 30% of qualified production expenses incurred in the state. In 2007, the state added separate tax credits for film infrastructure investment and digital animation production activity. The Connecticut Office of Fiscal Analysis estimates that $115 million in credits will be claimed in the current fiscal year. This will represent the state's largest single corporate income tax expenditure. The governor's proposed budget limits the total annual amount of credits to $30 million. According to published news reports, several industry representatives and advocates opposed the limit at a recent hearing and stated that $30 million in annual subsidies will not be sufficient to entice additional expansion of the industry in the state.

*Recent Developments*

Programs have been recently enacted or proposed in several states. California recently enacted a tax credit program for 20% to 25% of qualified expenses incurred by film and television productions. A total of $500 million in credits are available over five years. The Governor of Texas recently proposed expanding the state's program by authorizing a total of $60 million in credits over two years.

In contrast, several states in addition to Connecticut have proposed or have recently limited film industry subsidies. Rhode Island tightened its requirements and capped the program to $15 million annually primarily after a straight-to-DVD film received a $2.7 million tax credit and was later determined to have only $1.9 million in state vendor or resident expenditures. The proposed budget in Wisconsin eliminates the 25% production credit and replaces it with a $500,000 annual grant program for projects that create permanent jobs in the state. A recent audit determined that the program awarded $4.6 million in credits to a project that generated $5 million in economic activity to the state.

*Program Economic Impacts*

Film subsidy proponents indicate that the programs create jobs and generate substantial economic benefits throughout the economy that could offset the cost of the subsidy payments. Opponents question the effectiveness of the programs and the appropriateness of subsidizing a private firm in one industry for its production and wage costs, particularly when states are facing significant fiscal deficits.

Several studies have concluded that state film subsidy programs offer sizable economic benefits through increased jobs and economic activity and that tax credits or subsidies "pay for themselves." Independent analyses have highlighted the difficult task of determining the full economic impact of film production subsidy programs and have identified several potential flaws in these studies and a failure to consider other important impacts.

A policy analyst for the Federal Reserve Bank of Boston recently noted some of the important considerations in analyzing the impact of the Connecticut film tax credit:

- Benefits associated with film tax credits cannot be measured simply by adding up the in-state production expenditures for projects receiving credits. Expenditures occurring in the state will have a "multiplier" or "ripple" effect that is often larger than the initial expenditures.
- Film production activity that was actually induced by a credit should be distinguished from activity that would have taken place even without the credit. Only economic activity stemming from induced film production should be attributed to the credit. In addition, some production expenditures induced by the credit such as salaries paid to out-of-state residents may not have multiplier effects.
- The estimated net cost of a credit program reflects the amount of tax credits approved minus any increased revenues and changes in state spending due to economic activity generated by the credit.
- Balanced budget requirements will require state governments to either cut spending or increase other taxes to offset tax credit revenue losses. These actions are likely to have negative multiplier effects that offset the economic benefits generated by the credit.

Studies that fail to consider these impacts will not accurately characterize the tax credit economic impacts. The uneven distribution of the film industry across states might pose additional challenges as it is not clear that a tax credit program in a state with a high industry concentration such as New York will have the same impact as a state with a limited industry base.

In addition, a significant portion of jobs created and of increased additional economic activity generated in each state is merely a reallocation of economic activity among states. According to the New York State Governor's Office for Motion Picture and TV Development, during the 12 months following July 2006, as the Connecticut, Rhode Island, Massachusetts, and Pennsylvania programs became fully functional, New York experienced a $750 million drop in feature film applications compared to the previous 12 months. During the same period, Connecticut alone experienced an increase in feature film production of approximately $400 million. Instead of film production activity taking place where it is most efficient to do so, film subsidies lead to an inefficient allocation of capital and labor among and within states. The net economic gain should also be measured against the effectiveness of alternative economic development strategies.

The Connecticut Department of Economic and Community Development analyzed the impact of $16.7 million in credits awarded during 2007. The analysis found that for every $1 in tax credits, over the long-term personal income grew by $0.49, and economic activity within the state increased by $1.20. Another preliminary analysis found that the economic benefits are likely to be short-lived and evidence suggested the film tax credit may be less cost-effective than other economic development programs. An analysis of Massachusetts' program found a higher impact on economic activity but a similar net cost per job of $22,443 to $34,380. The average net cost to the state of each job created was $37,200. Studies funded by film offices in New Mexico and New York have estimated higher economic impacts in these states.

As highlighted earlier, independent analyses have concluded that a film tax credit program does not "pay for itself." Increases in economic activity spurred by the tax credit generate additional revenue that only partially offsets the cost to the State of the program. **Exhibit 2** shows the estimated state fiscal impact of tax credit programs in four states. Every $1 in tax credits awarded in these states is estimated to results in between $0.11 to $0.21 in additional state revenues.

**Exhibit 2**
**Estimated Tax Credit Fiscal Impacts in Other States**
**($ in Millions)**

| State | Year | Total Credits | Positive State Fiscal Impact Total | Positive State Fiscal Impact Percentage | Net Cost |
|---|---|---|---|---|---|
| Connecticut* | 2007 | $16.5 | $1.8-$3.3 | 11%-20% | $13.2-$14.7 |
| | 2005 | 66.3 | 8.2 | 12.4% | 37.1-58.1 |
| | 2006 | 87.6 | 11.4 | 13.0% | 49.9-59.7 |
| Louisiana | 2007 | 115.1 | 14.6 | 12.7% | 59.7-100.5 |
| Massachusetts** | | 100.0 | 17.9-23.0 | 20.5% | 82.1-77.0 |
| | 2009 | 107.5 | 19.1 | 17.8% | 88.40 |
| Michigan | 2010 | 160.0 | 28.7 | 17.9% | 131.3 |

*Analysis of $16.5 million in credits awarded early in the program. The credits were determined to reduce spending or increase revenues by $0.20 cents per dollar of credits in 2007, but decrease by $0.11 over the long-term

**Massachusetts analysis was a preliminary analysis of the impact if $100 million in credits were awarded.

**State Revenues:** The bill converts the existing Film Production Rebate Program to a tax credit program that is not subject to an annual appropriation. There is no cap on the maximum amount of credits that can be awarded to one production or in aggregate. Legislative Services advises that converting the rebate program to a conventional tax credit program without a limit on the total amount of credits that can be awarded will significantly increase the uncertainty over the total impact and timing of program's fiscal impact.

The Maryland Film Office estimates that the bill could be expected to generate $100 million in film production activity in Maryland beginning in fiscal 2010 and up to $150 million in subsequent years. Based on this information and tax credit programs in existing states, general fund revenues may decrease by $12 million in fiscal 2010, $50 million in fiscal 2011, and around $60 million annually beginning in fiscal 2012. This estimate also assumes that 60% of credits are claimed in the fiscal year in which they are earned with the remaining amount claimed in the following fiscal year. Revenue losses may be significantly higher than estimated.

*Indirect Revenue Impacts of the Program*

Increasing film production subsidies will increase industry employment. In addition, multiplier effects will lead to indirect job creation in other industries. The increase in jobs, however, relative to the amount of credits awarded will likely be modest. Competing state programs will require sustained subsidies above and beyond the $3.9 million committed annually under the existing program in order to retain industry job gains.

Increased economic activity resulting from the program will be insufficient to offset tax credit revenue losses awarded for film production activity. The exact impact will depend on how the credit interacts with the State's economy and the extent that other states respond by offering enhanced subsidies. Based on existing research, the tax credit program could return a maximum of 15% in additional "new" revenues and reduced state spending. For example, if $50 million in credits are claimed in each year, State spending will decrease by a minimum of $42.5 million or revenues will be required to be raised by an additional $42.5 million in order to balance the budget. Changes in State spending also have a multiplier effect on the economy. The Congressional Budget Office recently estimated that federal stimulus money provided to states for purposes other than infrastructure will increase gross domestic product by between $0.70 and $1.90 for each dollar by reducing spending cuts or the need to raise taxes. Economic development resulting from the credit will be at least partially offset by the decrease in economic activity resulting from reduced State spending or increased taxes assessed on Maryland businesses and/or individuals.

**State Expenditures:** Repealing the film production rebate program will eliminate general fund expenditures to the rebate program fund. It is assumed that if the bill passes any amount of money appropriated to the fund in fiscal 2010 will be rescinded through the budget process or the Board of Public Works. General fund expenditures will decrease by $2.0 million in fiscal 2010 and 2011 and by $3.9 million annually beginning in fiscal 2012.

---

## Additional Information

**Prior Introductions:** None.

**Cross File:** HB 908 (Delegate Hixson, *et al.*) - Ways and Means and Economic Matters.

**Information Source(s):** Department of Business and Economic Development, Comptroller's Office, Connecticut Office of Fiscal Analysis, Congressional Budget Office, Economics Research Associates, New York State Department of Taxation and Finance, Pennsylvania Department of Community and Economic Development, Federal Reserve Bank of Boston, Massachusetts Department of Revenue Office of Tax Policy Analysis, Michigan State Senate Fiscal Agency, State of Louisiana Legislative Fiscal Office, Maryland Film Office, Department of Legislative Services

**Fiscal Note History:** First Reader - March 10, 2009
mcp/hlb

---

Analysis by: Robert J. Rehrmann

Direct Inquiries to:
(410) 946-5510
(301) 970-5510

## Appendix 1

| State | Production Tax Credit | Caps per Year | Wage Credits | Sales Tax Exemption |
|---|---|---|---|---|
| Alabama | | | | |
| Alaska | 30% (T) | $100 million | 10%, plus 2% rural | n/a |
| Arizona | 20-30% (T) | $50 million | | X |
| Arkansas | | | | |
| California | 20-25% | $500 million / 5 years | | X |
| Colorado | 10% CR | $0.6 million | | |
| Connecticut | 30% (T) | | | X |
| Delaware | | | | |
| Dist. of Columbia | 10% (G) | $1.6 million | | Grant may apply |
| Florida | 15% + bonus CR | $5 million | | X |
| Georgia | 20% + 10% bonus (T) | | | X |
| Hawaii | 15%-20% R | | | |
| Idaho | 20% CR | | | X |
| Illinois | 20% (T) | | 15% | |
| Indiana | 15% R | $5 million | | X |
| Iowa | 25% (T) | | | |
| Kansas | 30% | $2 million | | |
| Kentucky | | | | |
| Louisiana | 25% (T) | | 10% | |
| Maine | | | 10%-12% | X |
| Maryland | 25% G | $2.5 million for FY 09 | | X |
| Massachusetts | 25% R,T | | 25% | X |
| Michigan | 40-42% R, T | | 30% | |
| Minnesota | 20% CR | | | X |
| Mississippi | 20% CR | | 20-25% | X |
| Missouri | 35% (T) | $4.5 million | | |
| Montana | 9% R | | 14% | n/a |
| Nebraska | | | | X |

| State | Production Tax Credit | Caps per Year | Wage Credits | Sales Tax Exemption |
|---|---|---|---|---|
| Nevada | | | | X |
| New Hampshire | | | | |
| New Jersey | 20% (T) | $10 million | | |
| New Mexico | 25% R | | | |
| New York | 30% R | $65 million in FY 08 | | |
| North Carolina | 15% R | | | X |
| North Dakota | | | | X |
| Ohio | | | | X |
| Oklahoma | 5-15% CR | $5 million | | |
| Oregon | 20% CR | | 16.2% | n/a |
| Pennsylvania | 25% T | $75 million | | |
| Rhode Island | 25% T | $15 million | | |
| South Carolina | 30% CR | $5.5 million FY 08 | 10-20% | X |
| South Dakota | | | | X |
| Tennessee | 13-17% + R | | | X |
| Texas | 5%+ G | | | X |
| Utah | 15% CR | $5.5 million FY 09 | | X |
| Vermont | | | | |
| Virginia | discretionary CR | $0.2 million FY 09 | | X |
| Washington | 20% CR | $3.5 million | | X |
| West Virginia | 27% (T) + bonus | $10 million | | X |
| Wisconsin | 25% R | | | |
| Wyoming | 12-15% CR | $2 million | | |

T= Transferable, R=Refundable, CR = Cash Rebate, G = Grant

Source: Economic Research Associates