SB 905

Department of Legislative Services

Maryland General Assembly
2015 Session

FISCAL AND POLICY NOTE
Revised

Senate Bill 905 (Senator Kasemeyer, *et al.*)
Budget and Taxation Ways and Means

Income Tax - Film Production Activity Tax Credit

This bill repeals the termination date of the film production activity tax credit program and specifies that the amount of credits that the Department of Business and Economic Development (DBED) can award in each fiscal year beginning in fiscal 2017 cannot exceed the amount of money appropriated to a reserve fund established by the bill. The bill states that it is the intent of the General Assembly that the appropriation to the reserve fund equal the amount DBED reports as necessary to maintain the current level of film production activity in the State and to attract new film production activity to the State.

The bill takes effect July 1, 2015, and applies to all tax credit certificates issued after December 31, 2014.

Fiscal Summary

State Effect: Potential significant general fund expenditure increase beginning in FY 2017. The amount of the expenditure increase depends on the amount, if any, appropriated to the reserve fund. Based on the intent specified by the legislation, the recent amount of film production activity, and the amount DBED estimates is required to attract new film production activity, general fund expenditures will increase by $25.0 million annually beginning in FY 2017. Revenues are not materially affected.

($ in millions)	FY 2016	FY 2017	FY 2018	FY 2019	FY 2020
Revenues	$0	$0	$0	$0	$0
GF Expenditure	0	25.0	25.0	25.0	25.0
Net Effect	$0	($25.0)	($25.0)	($25.0)	($25.0)

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

Local Effect: Local highway user revenues distributed from the Transportation Trust Fund will decrease beginning in FY 2017 as a result of credits claimed against the corporate income tax.

Small Business Effect: Potential meaningful.

Analysis

Bill Summary: Under the current program, the maximum amount of credits that DBED can award in each fiscal year is specified by statute. The bill establishes a Maryland Film Production Activity Tax Credit Reserve Fund. The total amount of initial credit certificates issued by DBED in each fiscal year cannot exceed the amount appropriated to the reserve fund in the State budget. The Governor may appropriate money to the reserve fund beginning in fiscal 2017, but the bill does not require an amount. The bill states that it is the intent of the General Assembly that the appropriation to the reserve fund is equal to the amount that DBED reports as necessary to (1) maintain the current level of film production activity in the State and (2) attract new film production activity to the State. DBED is required to report these amounts to the Governor and General Assembly by July 1 of each year. Any amount of money in the fund that is not expended in the fiscal year remains in the fund and is rolled over into the next fiscal year.

The bill also requires DBED to report by January 1 of each year a list of the businesses that directly provided goods or services to a film production entity that claimed the film production activity tax credit and (1) qualified as a MBE under State procurement law; and (2) are determined by DBED to be a small business.

The production entity of a TV series or feature film that receives a tax credit is required to include for the life of the project a five-second logo that promotes the State and a link to the State's website on the project's website. For all other projects, the entity must include the State logo at the end of each project and in online promotions. In lieu of these requirements, a production entity can offer alternative marketing opportunities that promote the State. DBED is required to ensure that these marketing opportunities offer equal or greater promotional value to the State.

Current Law: The film production activity tax credit program terminates June 30, 2016.

A qualified film production entity that meets specified requirements and is approved by DBED may receive a tax credit equal to 25% of qualified film production costs incurred in the State. For a television series, the value of the credit is increased to 27%. If the amount of the tax credit exceeds the total tax liability in the tax year, the entity can claim a refund 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.

Any salary, wages, or other compensation for personal services of an individual who receives more than $500,000 in salary, wages, or other compensation for personal services in connection with any film production activity may not be included in total direct costs.

The film production entity must notify DBED of its intent to seek the tax credit before the production activity begins. A film production entity is also required to submit an application containing specified information, including the project's estimated total budget and the anticipated dates for carrying out the major elements of the film production activity.

"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 activity does not include a student film; noncommercial personal video; sports broadcast; broadcast of a live event; talk show; video, computer, or social networking game; or pornography.

DBED is required by January 1 of each year to submit a report to the Governor and General Assembly that details (1) the number of film production entities that submitted applications; (2) the number and amount of tax credit certificates issued by DBED; (3) the number of local technicians, actors, and extras hired for film production activity during the reporting period; (4) a list of companies doing business in the State, including hotels, that directly provided goods or services for film production activity; and (5) any other information that indicates economic benefits to the State resulting from film production activity.

Background: Film production incentives have gained popularity in the past decade, with 37 states and the District of Columbia offering incentives in 2014. Maryland began offering financial assistance to encourage film production activities in 2001 and adopted the current film production activity tax credit beginning in 2012. A qualified film production entity that meets specified requirements and is approved by DBED may receive a refundable tax credit of up to 27% of the qualified direct costs of a film production activity.

Pursuant to the Tax Credit Evaluation Act of 2012, the Department of Legislative Services (DLS) evaluated the film production activity tax credit and made several recommendations in a draft report issued in November 2014. The DLS evaluation report concluded that the economic development activity generated by film productions is of a short duration. As soon as a film production ends, all positive economic impacts cease too. As such, the film production activity tax credit does not provide long-term employment. Maryland has provided $62.5 million in tax credits between fiscal 2012 and 2016 while only receiving a fraction of the tax credit amounts back in revenues to the State and local governments. Additionally, states are fiercely competing with one another to draw productions into their state. This type of competition is not only expensive, but promotes unhealthy competition among states.

The cost of film incentives to states has risen dramatically as a result of both the increase in the number of states offering incentives and increase in the generosity of programs as states try to remain competitive with each other. With increased competition among states, Maryland's return on investment for film production incentives has decreased over time. When analyzing incentives in other states, it is clear that the economic benefits of film production activity tax credits cannot be sustained in the absence of continued significant funding of industry subsidies each year. Since the credit does not provide sustainable economic development and provides a small return on investment to the State and local governments, DLS recommended that the General Assembly allow the film production activity tax credit to sunset as scheduled on July 1, 2016.

If the General Assembly decides to extend the film production activity tax credit beyond July 1, 2016, the report included several recommendations to improve the credit. These recommendations include requiring DBED to provide additional information about the tax credit. Considering the General Assembly's interest in providing business opportunities for small, minority- and women-owned businesses, DLS recommended that the General Assembly require DBED to report the number of these businesses that qualify. In addition, if the data collected suggests that these firms consist of only a small percentage of the vendors, DLS recommended that DBED consider methods by which film production entities can provide opportunities for small, minority-, and women-owned businesses.

The DLS evaluation of the film production activity tax credit can be found on the DLS website.

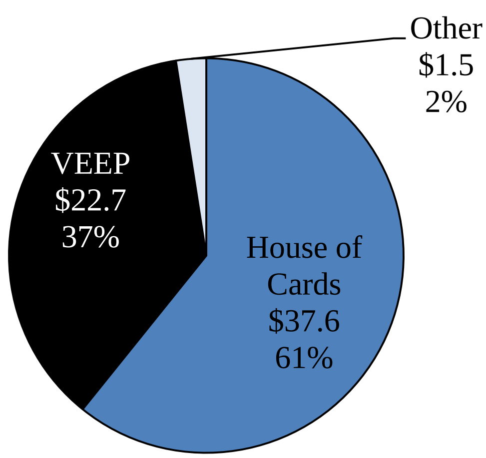
State Fiscal Effect: The bill provides that the Governor may appropriate funds to the reserve fund but does not require an amount that should be appropriated. The bill does, however, state that it is the intent of the General Assembly that the amount appropriated to the fund equal the amount that DBED reports as necessary to (1) maintain the current level of film production activity in the State and (2) attract new film production activity to the State. VEEP and House of Cards received a total of $23.8 million in film production tax credits for each production's last series. DBED estimates that approximately $22.0 million is necessary to maintain the current level of film production activity in the State and an additional $3.0 million annually to attract new film production activity to the State. A total of $11 to $12 million in film production activity would qualify for a $3.0 million credit, which translates to either one or several small-budget independent films or one television series production with total production expenses equal to about two-thirds of the average amount spent by VEEP and about one-fifth of the average amount spent by House of Cards. If the program is funded at these levels, general fund expenditures will increase by $25.0 million annually beginning in fiscal 2017.

To the extent that the Governor provides less or no money to the reserve fund in any year, the increase in general fund expenditures will be less. However, there is no limit on the amount that can be appropriated to the reserve fund. Legislative Services notes that programs in other states receive significantly higher levels of funding; accordingly, general fund expenditures would be significantly higher if the program is funded at a similar level in order to attract additional film production activity to the State.

Local Revenues: Local highway user revenues will decrease as a result of credits claimed against the corporate income tax. If $25.0 million in credits are claimed in each year with 75% of the amount claimed against the corporate income tax, local highway user revenues will decrease by $262,700 annually.

Small Business Impact: From fiscal 2012 to 2016, approximately $62.5 million in film production activity tax credits have been authorized by the General Assembly. Of that amount, $60.3 million, or 96.5% of the total, has been awarded to two productions – House of Cards and VEEP. During that time period, only three other productions have been awarded tax credits, for a total of $1.5 million. **Exhibit 1** shows the distribution of the tax credits by production.

Exhibit 1
Distribution of Maryland Film Production Tax Credits
Fiscal 2012-2016
($ in Millions)



Source: Department of Business and Economic Development, Department of Legislative Services

According to DBED, small businesses benefit as film production companies use local vendors for purchases. In addition, the Maryland Film Office reports an increased interest from other production firms to locate in Maryland and "if this is sustained, it will surely lead to the creation of a cluster of related industries, which has a ripple effect in job creation, larger consumer base, and revenue collection."

DLS notes that the primary beneficiaries of the tax credit are the film production entities and that the majority of tax credits have been awarded to or encumbered for companies that are not Maryland small businesses. An increase in local film production expenditures leads to additional purchases from local vendors, an unknown number of which are small businesses.

The DLS evaluation of the film production tax credit concluded that for every $1 in film tax credits awarded, the State recoups just over 6 cents in tax revenue from the associated economic activity and local governments receive 4 cents. Thus, the film production credit produces an estimated 10 cents in total State and local taxes for each dollar of credit granted to film productions. While the credit may produce economic benefits that accrue to certain businesses and individuals, the credit does not pay for itself. The Maryland Constitution requires the Governor to submit, and the General Assembly to pass, a balanced budget. Any benefit to small business local vendors as a result of increased tax credits must be measured against the negative impact to small businesses from decreases in State spending or increased taxes.

Additional Information

Prior Introductions: None.

Cross File: Although designated as a cross file, HB 753 (Delegate Luedtke, *et al.* - Ways and Means) is not identical.

Information Source(s): Department of Business and Economic Development, Comptroller's Office, Department of Legislative Services

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