

Department of Revenue Report to the General Assembly On the Film Production Tax Credit

March 31, 2006

The Pennsylvania Film Production Tax Credit Law

On July 20, 2004, Act 95 of 2004 was signed into law, which created the Pennsylvania Film Production Tax Credit. The Pennsylvania Film Production Tax Credit became Article XVII-C of the Tax Reform Code (TRC) of 1971. The intent of the film production tax credit was to promote the production of television series and movies in Pennsylvania by offering a tax credit for certain production expenses.

The law stated that the credit was limited to only those productions where at least 60% of production expenses are incurred in Pennsylvania. Qualified Pennsylvania production expenses include only wages and salaries on which Pennsylvania Personal Income Tax (PIT) or Corporate Net Income Tax (CNIT) will be paid or accrued. The credit awarded would be equal to 20% of the qualified Pennsylvania production expenses. Originally, production companies were directed to apply to the Department of Revenue (DOR) for the credit by February 15th in each year for expenses incurred in the previous calendar year. DOR was to review applications and award credits by August 15th of the same year. The total amount of credit that could be awarded was capped at \$10 million per fiscal year. If more applications were received than could be fully funded, the amount awarded was to be pro-rated.

The original law was amended by Act 40 of July 7, 2005. Under the new legislation, the Department of Community and Economic Development (DCED) will administer the awarding of the credits on a "first come, first served" basis using the date on which principal photography in Pennsylvania starts. DCED will certify the amount of the credit to DOR. Total credit awards remain limited to \$10 million in any fiscal year.

Under the new law, credit applications are based on budgeted expenses rather than actual expenses. Filmmakers who are awarded credits and fail to incur the original budgeted amount of qualified film production expenses upon which the credits are based must refund any credit claimed. These provisions apply to any film production expenses incurred after December 31, 2004.

It should be noted that not all Pennsylvania production expenses are eligible to be included in the calculation of the film production tax credit. For instance, expenses incurred for marketing or advertising a film¹ or to purchase story rights, music rights or development costs² are excluded from the definition. Under Act 40-2005, valid production expenses include the aggregate amount of wages and salaries of individuals receiving less than \$1.0 million employed in the production of the film. Other valid expenses include "the cost of construction, operations,

¹ Act 95-2004.

² Act 40-2005.

editing, photography, sound synchronization, lighting, wardrobe and accessories; and the cost of rental of facilities and equipment.”³

For the fiscal year 2005-2006, the amount of credits that can be awarded by DCED is equal to the difference between \$10 million and the amount of credits already awarded on August 15, 2005 by DOR.⁴

Film production tax credits can be applied against CNIT, PIT and Capital Stock/Foreign Franchise Tax (CSFT) liabilities. However, in order to be applied against the PIT, the credit can only be used to offset liabilities generated by net profits. Credits can also be passed through a partnership or Pennsylvania S corporation to its owners. The credit may be carried forward for up to three years. Credit recipients are also allowed to sell or transfer any unused portion of the credit, if approved by DCED.⁵

The purchaser or assignee of an unused film tax credit must immediately claim the credit in the taxable year the purchase or assignment is made. Further, the purchaser or assignee cannot use the tax credit to offset more than 50% of a specific tax year liability. Lastly, the purchaser or assignee cannot carry forward, carry back or get a refund for the unused tax credit. It is the responsibility of the purchaser or assignee of an unused tax credit to inform DOR of the seller of the unused tax credit.

No film production tax credit can be awarded for taxable years ending after December 31, 2012.

Film Production Tax Credit Awarded and Utilized in August 2005

Table 1 lists the name of each film production company receiving the credit in August 2005 along with the amount of tax credit awarded to them. DOR awarded almost \$7.1 million in credit in August 2005. The amount of tax credit awarded to them was based on their qualified film production expenses made in Pennsylvania from July through December 2004. Since less than \$10 million in tax credits were applied for, no pro-ration was required. One company that applied for the tax credit was denied due to filing after the February 15, 2005 deadline.

Table 1 also lists the amount of tax credit that each film production company has utilized.⁶ As of March 2006, \$6.8 million of the \$7.1 million has been utilized. All of the \$6.8 million in credit utilized was sold to other taxpayers.

The ten film production companies produced a total of 17 different projects in Pennsylvania. With the 20% film production tax credit, that means that these ten companies had \$35.3 million in qualified film production expenses in Pennsylvania. It is estimated by the Pennsylvania Film Office that in 2004 the film industry spent a total of \$218 million in the Commonwealth.

³ Section 1702-B.

⁴ DCED will have awarded the remaining money by the end of FY 05-06.

⁵ DCED coordinates and approves all credit transfers in consultation with DOR.

⁶ Utilized means that the tax credit has been sold or assigned.

Under the changes made by Act 40-2005, DCED will have about \$2.9 million more in credit to award in FY 2005-06.⁷ For fiscal years after FY 2005-06, \$10.0 million in tax credit will be available to be awarded by DCED.

**Table 1. Pennsylvania Film Production Tax Credit Program
Credit Awarded and Utilized by Company**

<i>Film Production Company</i>	<i>Tax Credit Awarded</i>	<i>Tax Credit Utilized</i>
Mother B Productions, Inc	\$ 3,875,160	\$ 3,575,160
Banyan Productions, Inc.	\$ 1,309,283	\$ 1,309,283
10th & Wolf, LLC	\$ 1,126,365	\$ 1,126,365
Sandy Leaf, LLC	\$ 555,443	\$ 555,443
Little Branch LLC	\$ 128,583	\$ 128,583
White Men Can't Rap LLC	\$ 24,900	\$ 24,900
FK Hollywood Productions, LLC	\$ 18,449	\$ 18,449
Inecom, Inc.	\$ 17,821	\$ 17,821
Argentine Productions, Inc.	\$ 7,617	\$ -
Amerikan Film Society, LLC	\$ 874	\$ -
TOTAL	\$ 7,064,494	\$ 6,756,004

Film Production Tax Credits in Other States

As of December 2005, 34 other states offer some type of financial or tax incentives for film and television producers to operate in their states. This type of tax incentive is becoming increasingly popular. In 2005 alone, 14 states have either created tax rebates or incentives for film and television producers or have added to their already existing programs.

Effectiveness of the Film Production Tax Credit Program

It is not possible at this time to comment on whether or not the film production tax credit has been effective. Less than one full year of limited data is insufficient for drawing definitive conclusions.

Conclusion

In the first year that the film production tax credit was awarded, DOR issued \$7.1 million in credit to 10 different film or television production companies. Almost all of the \$7.1 million in credit award has been sold to other taxpayers. Further, since less than \$10 million was applied for, the amount of credit awarded did not have to be pro-rated. Due to the changes made by Act 40-2005, this is the first and last report that DOR will be responsible for preparing on the film production tax credit.

⁷ This represents the amount of the \$10 million cap remaining after the \$7.1 million awarded by DOR in August 2005.