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OFFICE OF THE MAYOR
Ke'ena O Ka Meia
COUNTY OF MAUI – Kalana O Maui

TESTIMONY OF ALAN ARAKAWA, MAYOR
COUNTY OF MAUI

BEFORE THE SENATE
COMMITTEE ON WAYS & MEANS

Thursday, February 21, 2013, 9:00 a.m., Conference Rm. 211

SENATE BILL 750
RELATING TO DIGITAL MEDIA INFRASTRUCTURE

SB 463
RELATING TO FILM AND DIGITAL MEDIA INDUSTRY DEVELOPMENT

The Honorable Senator David Y. Ige, Chair
Honorable Senator Michelle N. Kidani, Vice Chair
And Members of the Committee on Ways and Means

SUBJECT: **TESTIMONY OF MAUI COUNTY MAYOR ALAN ARAKAWA ON SB750 AND SB463 RELATING TO MOTION PICTURE, DIGITAL MEDIA, AND FILM PRODUCTION**

Thank you for this opportunity to offer our testimony in **support on SB750 and SB463** relating to Motion Picture, Digital Media and Film Production tax credits. We believe that it is vital that the existing film and digital media production on Oahu be expanded and modernized; and, that the counties of Maui, Kauai, and Hawaii are able to create a new industry for its residents.

As Mayor of the County of Maui, I **strongly support** **SB750 and SB463** for the following reasons:

A. The creation and development of a new industry relating to motion picture, digital media, and film production, will:

- Create new, higher-paying jobs, as well as training, advancement and new educational opportunities for our residents.
- Provide incentives for the construction of **new** infrastructure including new sound stages; and, lead to the renovation and modernization of existing infrastructure on Oahu.

- Benefit the entire State of Hawaii by diversifying and stimulating our economy. Research has shown that each sound stage built in the state would inject nearly $140 million into our economy via the hiring of local labor and the purchasing of materials locally over a two-year period; and that each movie filmed here would create approximately 193 local jobs immediately (based on a movie with a $90 million budget).

Thank you for your consideration of our testimony supporting SB750 and SB463.

NEIL ABERCROMBIE
GOVERNOR

SHAN TSUTSUI
LT. GOVERNOR

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To: The Honorable David Y. Ige, Chair
and Members of the Senate Committee on Ways and Means

Date: Thursday, February 21, 2013
Time: 9:00 a.m.
Place: Conference Room 211, State Capitol

From: Frederick D. Pablo, Director
Department of Taxation

Re: S.B. 750, S.D. 1, Relating to Digital Media Infrastructure

The Department of Taxation (Department) appreciates the intent of S.B. 750, S.D. 1. However, as written, the Department has concerns with the potential increase in revenue loss resulting from the new media infrastructure project tax credit.

S.B. 750, S.D. 1, adds a new section to Chapter 235 of the Hawaii Revised Statutes, to create a media infrastructure project tax credit. The credit is a nonrefundable tax credit equal to 25% of the qualified infrastructure costs, beginning July 1, 2013 and ending December 31, 2015.

The Department is concerned about the broad range of costs (the development, construction, renovation, or operation of a film, video, television, or media production or postproduction facility, or any other facility that supports the project, including a movie theater or other commercial exhibition facility) that would qualify for the tax credit. Such broad wording will create administration and enforcement difficulties for the Department.

The measure requires the Department to approve an audit of the infrastructure tax credit and certify the expenditures for the project, including: a detailed description of the project, a preliminary budget, a complete detailed business plan and market analysis, an estimated start and completion dates, and a letter from the mayor and council of the county. Thereafter the Department is required to issue a final tax credit certification letter indicating the amount of tax credits certified for the infrastructure project to the investors. The Department is unable to comply with these requirements as Department staff does not have the technical background on. Currently, the DBEDT certifies all creative media type expenditures; the Department notes that they may be better suited to continue doing these certifications.

This measure could result in estimated revenue loss of $14.4 million for FY 2014, $28.8 million for FY 2015, and $14.4 million for FY 2016.

Thank you for the opportunity to provide comments.

LATE

SUBJECT: INCOME, Expand motion picture, digital media and film production credit

BILL NUMBER: SB 750, SD-1

INTRODUCED BY: Senate Committees on Economic Development , Government Operations & Housing & Technology & the Arts

BRIEF SUMMARY: Adds a new section to HRS chapter 235 to allow taxpayers, between July1, 2013 and December 31, 2015, to claim a credit of 25% of the qualified costs incurred for qualified media infrastructure projects situated in West Oahu or on the most populous island in a county with a population between 100,000 and 175,000.

To qualify for the credit: (1) the base investment for a qualified media infrastructure project shall be in excess of $_______; (2) the qualified media infrastructure project tax credit shall be non-refundable so any tax credit that exceeds the tax liability of the taxpayer may be carried forward to offset net income tax liability in subsequent tax years for up to ten years or until exhausted, whichever occurs first; the director of taxation may require the tax credits to be taken or assigned in the tax period in which the credit is earned or may structure the tax credit in the initial certification of the project to provide that only a portion of the tax credit be taken over the course of two or more years; (3) the total qualified media infrastructure project tax credit allowed for any state-certified infrastructure project shall not exceed $_______; (4) if any portion of an infrastructure project is a facility that may be used for other purposes unrelated to production or post production activities, then the project shall be approved only if a determination is made that the multiple use facility will support and will be necessary to secure production or post production activity for the production and post production facility; provided that no tax credits shall be earned on such multiple use facilities until the production or post production facility is complete; (5) tax credits for infrastructure projects shall be earned only if: (a) construction of the infrastructure project begins within six months of the initial certification and shall be ___% completed within a ___ year time frame; (b) expenditures shall be certified by the director of taxation and credits shall not be earned until certification is received; (c) the tax credits shall be deemed earned at the time the expenditures are made, provided that all requirements of this subsection have been met and the tax credits have been certified; (6) for state-certified infrastructure projects, the application for a qualified media infrastructure project tax credit shall include: (a) a detailed description of the infrastructure project; (b) a preliminary budget; (c) a complete detailed business plan and market analysis; (d) estimated start and completion dates; and (e) if the application is incomplete, additional information may be requested prior to further action by the director of taxation; (7) an application fee of ___% times the estimated total incentive tax credits shall be submitted with the application for a qualified media infrastructure project tax credit; (8) prior to any final certification of a tax credit for a state-certified infrastructure project, the applicant for the infrastructure project tax credit shall submit to the director of taxation an audit of the expenditures certified by an independent certified public accountant as determined by rule. Upon approval of the audit, the director of taxation shall issue a final tax credit certification letter indicating the amount of tax credits certified for the state-certified infrastructure project to the investors. Bank loan finance fees applicable to the qualified media infrastructure project expenditures, as certified by the director of taxation, and any general excise taxes that have been paid on the bank loan finance fees and remitted to the state may be included as part of the tax credit.

Further requires the taxpayer claiming the credit to file a progress report of a qualified media project with DBEDT, deliver a performance bond in a form prescribed by DBEDT in an amount equal to 100% of total projected expenditures determined upon initial certification; and either: (1) pledge of a lien on the qualified media infrastructure project in favor of the state; or (2) collateral security.

Also requires any taxpayer eligible to claim a qualified media infrastructure project tax credit to file with DBEDT an annual report by March 1 following each taxable year for which the credit is claimed delineating: (1) the amount of general excise tax paid; (2) the amount of transient accommodations tax paid; (3) the amount of tax credits claimed under this section; (4) gross proceeds of each project; (5) number of full-time employees, part-time employees employed on each qualified media infrastructure project; (6) number of independent contractors contracted to work on each qualified media infrastructure project; (7) amount disbursed as payroll on each qualified media infrastructure project; and (8) list of job classifications with average wage level.

Defines “qualified media infrastructure project” as the development, construction, renovation, or operation of a film, video, television, or media production or post-production facility and the immovable property and equipment related thereto, or any other facility that supports and is a necessary component of the proposed infrastructure project, that is located in the state; provided that the facility may include a movie theater or other commercial exhibition facility to assist in offsetting operating costs of the production or post-production facility. The facility may not be used to produce pornographic matter or a pornographic performance.

A taxpayer may claim the media infrastructure project tax credit for investments made on a qualified media infrastructure project prior to January 1, 2016 if construction of the media infrastructure project commenced prior to January 1, 2016. Delineates recapture provisions if the qualified media infrastructure project no longer qualifies for the tax credit and the recapture shall be equal to 90% of the amount of the tax credit claimed in the preceding five years.

EFFECTIVE DATE: Tax years beginning after December 31, 2012

STAFF COMMENTS: The legislature by Act 107, SLH 1997, enacted an income tax credit of 4% for costs incurred as a result of producing a motion picture or television film in the state and 7.25% for transient accommodations rented in connection with such activity. The credit was adopted largely to address the impost of the state’s general excise tax on goods and services used by film producers.

The legislature by Act 88, SLH 2006, increased the 4% credit to 15% in a county with a population over 700,000 and to 20% in a county with a population of 700,000 or less. Act 88 also repealed the income tax credit for transient accommodations and expanded the credit to include commercials and digital media productions, and limited the credit to $8 million per qualified production. The proposed measure would allow taxpayers to claim a media infrastructure project tax credit in West Oahu or on the island of Maui.

These motion picture credits have been morphing and expanding into full-blown tax credits since they "got their foot in the door" in 1997. It should be remembered that the perpetuation and expansion of the motion picture credits are a drain on the state treasury. It is incredulous how lawmakers can bemoan the fact that there are insufficient resources to catch up on the backlog of school repairs and maintenance, to fund social programs and not being able to provide tax relief to residents and yet they are willing to throw additional public resources at a subsidy of film production and media infrastructure. Taxpayers should be insulted that lawmakers can provide breaks for film productions but refuse to provide tax relief for residents, many of whom work two or three jobs just to keep a roof over their head and food on the table.

There is absolutely no rational basis for perpetuating these tax credits other than that other states are offering similar tax credits. Then again those states can't offer paradise, year-round good weather during which to film. Instead of utilizing back door subsidies through tax credits, film industry advocates need to promote the beauty that is synonymous with Hawaii. Income tax credits are designed to reduce the tax burden by providing relief for taxes paid. Tax credits are justified on the basis that taxpayers with a lesser ability to pay should be granted relief for state taxes imposed.

Instead of handing out a tax credit to build the film infrastructure, be it a studio or a sound stage, lawmakers should appropriate a specific sum of money and issue a request for proposals to build such a project and see which bidder would come forward with the best proposal and offer to match the state's share. This way each bidder could be evaluated as to what they have to offer and what benefit the state would get. Inasmuch as the state would probably be able to offer the land for such a facility, it could also offer a streamlined permitting process which would also be an in-kind contribution. Based on the responses to the request, a careful review done by experts in the field could be made and the best proposal selected. The persons responsible for making the final selection would then be held accountable for their selection and provide the justification for the selection. Another alternative would be the use of special purpose revenue bonds. These alternative would be far more efficient and transparent than the tax credit proposed by this measure.

Merely handing out a tax credit to entice an economic activity is the "easy way" out for lawmakers. To really insure the success of this venture, it will take creative thinking and hard work. An appropriation of funds, perhaps the issuance of special purpose revenue bonds, a joint venture, contributions of land or acceleration of the permitting process are but a few ways government could incentivize such a project without spending one cent of cold hard cash. If, in fact, lawmakers believe this infrastructure to be critical to the development of this industry, then lawmakers need to take a more active role as opposed to sitting back and letting the tax credit drive the activity.

Digested 2/20/13

Testimony to

Senate Committee on Ways and Means

Thursday, February 21, 2013

By: Stephan D. Smith

President, SHM Partners/Film Studio Group

SB 750, SD1 —Relating to Digital Media Infrastructure

Senator David Y. Ige; Senator Michelle N. Kidani, Vice Chair

As Section 1 of SB 750 points out, the positive impact of film and television production on the State is irrefutable. The primary reason that there's not more of it is the lack of studio space. Given a stable production tax credit regime, there's no reason that production expenditures in Hawaii would not meet or exceed the high-water level of 2010, over $400 million, every year if the proper infrastructure were built. Without it, production expenditures in the State will continue its seesaw pattern as it is so heavily based on location-based shooting, thereby missing many project entirely and losing over half the spending of others that leave the Islands for their stage work.

Passage of SB 750, with the following revisions, would provide an essential building block for providing the proper studio infrastructure and ensuring the long-term viability of the film industry in the State:

1) The qualified media infrastructure project tax credit must be refundable. The pool of qualified, and interested, taxpayers to utilize the credits is not deep enough to impose this restriction, and the discount on the 25% credit becomes steeper as the limited taxpayer demand is satiated. In addition, the taxpayer loses the federal tax deduction on State the tax credits taken which reduces their benefit by at least a third, further depressing demand.

2) It should be clarified that land acquisition or leasing costs is included in the definition of "Qualified media infrastructure project". Land is scarce, and, therefore, relatively expensive in Hawaii, and it's simply not feasible to build a studio on a small lot. Stages are single-story structures and considerable parking and circulation space is needed.

Another building block for ensuring the sustainability and growth of the film industry is the production tax credit. As has been starkly demonstrated in other states and countries, the stability of this credit is critical to attracting productions. Beyond that, a modest increase in the credit and significant increase in the per-project cap would attract more productions as well as more private capital for infrastructure improvements. A new studio would be able to attract $100 million productions; it would be a shame for the production tax credit to be the limiting factor.

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