F I S C A L   I M P A C T   R E P O R T

SPONSOR SCORCS **ORIGINAL DATE** 3/5/15 **LAST UPDATED** 3/12/15 **HB**

SHORT TITLE Limit Film Production Tax Credit **SB** 565/SCORCS

ANALYST Graeser

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY15	FY16	FY17	FY18	FY19		
	**	**	**	**	Recurring	General Fund

(Parenthesis ( ) indicate revenue decreases

[**] The provisions of this bill will not materially affect the number or magnitude of the credit claims. The purpose of the bill is to push the pendulum toward somewhat more benefit to state residents than with the current provisions.

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY15	FY16	FY17	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
Total		32.0	0.0	0.0	Recurring	TRD operating
Total		0.0	0.0	0.0	Recurring	EDD operating

Parenthesis ( ) indicate expenditure decreases

While both EDD/FO and TRD would have to adjust procedures and verification methodologies somewhat, both agencies would probably expend less time processing applications because of the clarifications contained in this bill. The cost shown for TRD is for the 400 hours of GenTax effort programming the changes into the system.

SOURCES OF INFORMATION

LFC Files

Responses Received From
Economic Development Department/Film Office (EDD/FO)
Attorney General's Office (AGO)
Office of the State Auditor (OSA)
Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of Bill

Senate Corporations and Transportation Committee Substitute for Senate Bill 565 clarifies and limits direct production expenditures that may be eligible for the film credit and adds TV pilots to the types of productions eligible for the enhanced 5% credit over and above the 25% basic credit. In many respects, the bill seeks to provide incentives to encourage production companies to hire New Mexico crew and performing artists, to patronize New Mexico production facilities and to purchase goods and services from New Mexico vendors. Specifically, the bill would, (1) limit eligible payments to nonresidents, and (2) require some shooting at "qualified production facilities," such as New Mexico sound stages or film-designated standing sets."

The SCORC substitute bill contains the same provisions as the original bill, but has organized the material in more readable form. The substitute also addresses the gap from June 19, 2015 to January 1, 2016 in the original bill.

FISCAL IMPLICATIONS

Per comments submitted by EDD/FO, "Proposed changes would result in a positive fiscal impact by limiting the types and the amount of tax credit payments to nonresident performing artists and nonresident crews. The number of nonresident crew positions is also limited by provisions of the bill. The bill provides incentives for resident non-lead performing artists and resident directors, producers, and writers. These features will probably promote job opportunities. Television pilots have qualified when submitted with a series; however the stand-alone television pilots qualifying under this bill would increase the number of recruited projects."

The bill is divided into two time periods: some changes are effective for productions that begin principal shooting before January 1, 2016 and others for productions that begin shooting after January 1, 2016. This separation is consistent with the corporate income tax system processing the claims for rebate.

While the provisions of the bill may create both increases and decreases in the claims, the magnitude of these shifts will not alter the provisions of the deferred payments or the $50 million annual cap.

See significant issues below for a discussion of the effect the provisions of the bill may have on the wages, jobs and other opportunities for New Mexico residents. The best guess is that the provisions of this bill would not alter the general fund cost, but could increase the benefits for New Mexico residents and increase general fund collected revenues over a period of time outside of the budget window.

SIGNIFICANT ISSUES

The bill modifies the current Section 7-2F-1 NMSA 1978 (Film Production Tax Credit) for film production companies that commence principal photography prior to January 1, 2016. The bill then rewrites the film production tax credit for film production companies that commence principal photography after January 1, 2016. For the most part, all changes are effective June 19, 2015.

The changes to the current film production tax credit effective for the remainder of CY 2015 are as follows:

1) The basic credit percentage remains at 25%, but "a standalone pilot intended for series television in New Mexico" joins the current law "TV series … with an order for at least 6 episodes … with a budget of $50,000 per episode" in receiving an additional 5% tax

credit. [The provision that if the company receives a federal new markets tax credit, the state credit is reduced to 20% is retained.]

2) A production with defined budget and shooting days in New Mexico also qualifies for the enhanced 5% credit for expenditures directly attributed to wages and benefits paid to a New Mexico resident working as crew, producer, writer or director.
3) The "New Mexico Impact" enhanced percentage requires some number of shooting days at a sound stage that is a qualified production facility.
4) The amount of film production tax credit attributable to nonresident performing artists and featured resident principals is limited to $5 million per production. This is only a slight change and is intended to provide an incentive for hiring of New Mexico performing artists into minor roles where their wages and benefits would be creditable.
5) Clarifies the term "direct production expenditures" in fashion to encourage producers to spend a larger portion of the total budget to benefit New Mexico residents and vendors.
6) As in current law, all production companies must provide for orderly exits from the state, with all bills paid.
7) As in current law, production companies with credit claims in excess of $5 million must submit a certification from a New Mexico licensed CPA that expenditures have been made in compliance with the act and that all bills have been paid.
8) Retains the ability of TRD to disclose data to the legislature despite the confidentiality restrictions of 7-1-8 NMSA 1978.
9) The $50 million annual cap is retained and the three-year payout for larger credit claims is retained.

Beginning with productions that begin principal shooting after January 1, 2016, the film production credit is further restructured:

1) Production companies producing a standalone pilot intended for series television in New Mexico or a TV series with an order for at least six episodes and a budget of $50,000 per episode qualify for an additional 5% credit, except that payments to a nonresident performing artist in a pilot would not qualify for the enhanced credit. Payments to a nonresident artist performing in a qualified TV series would qualify for the enhanced 5% tax credit after one season has been completed and with a declaration from the producers that the production company intends to produce a subsequent season in the state.
2) A second path to an enhanced 5% tax credit is provided in the bill, similar to the second path provided for CY 2015 above. If the production company shoots a defined number of days at a qualified production facility, then the direct expenditures attributed to wages and benefits and other costs paid to New Mexico residents are eligible for the enhanced credit. This second path is mutually exclusive. Either the TV series/pilot enhancement or the "Hire New Mexico Artists and Crew" enhancement is possible, but not both.
3) The bill provides for a 15% credit for nonresident industry crew. There are a number of provisos for this credit, including a contingent limit on the number of nonresident crew that will be allowed at any level of production effort.
4) The bill also requires production companies to the extent possible to contract with New Mexico specialized service providers.

The AGO previously provided a detailed list of provisions of the original bill that is still relevant to this substitute bill:

1) Adds TV series stand-alone pilot productions as eligible for additional 5 percent tax credit (tax credit increase).

2) Eliminates the 5 percent credit for direct production expenditures for nonresident performing artists (tax credit decrease and shift to New Mexico benefits).
3) Restrict additional 5 percent credit for production expenditures paid to a New Mexico resident who has filed NM state income tax returns as a resident in the previous two taxable years (uncertain fiscal and administrative effect).
4) Clarifies that the additional 5 percent tax credit is available based on total "New Mexico" budgets, not a production budget total that includes costs incurred outside of the state (tax credit decrease but unlikely to cause shift to New Mexico shooting or post-production).
5) Requires a company seeking the 5 percent credit to shoot a minimum number of days of principal photography days within New Mexico depending upon the total New Mexico budget eligible for the tax credit. This provision also includes photography be shot at either a sound stage or standing set classified as qualified production facilities, including a minimum number of days at a sound stage, and that each eligible day must include at least eight hours of work done by an industry crew (probably technical, but may serve to increase credit amounts by requiring a minimum quantity of crew days to be paid).
6) Creates a new category providing for a 15 percent tax credit for direct production for wages, fringe benefits, and per diem for nonresident industry crew for services rendered in New Mexico. This provision excludes payments for a production designer, directors of photography, line producer, costume designer, still unit photographer, and drivers. This clause also places restrictions on the number of positions eligible for the credit depending upon the production's final New Mexico budget (if this provision supplants the regular 25 percent credit, then tax credits would decrease. However, it may simply shift effort and costs from non-resident to resident crews).
7) Incorporates television episodes to the existing requirement on films to include an acknowledgement in the screen credits that the production was filmed in New Mexico (no change).
8) Changes application requirements to align with the tax year instead of the calendar year (no change).
9) Reduces reporting requirements for the division to post on its website quarterly, instead of monthly, the projected amount of credits claims made for the fiscal year (no change).
10) Adds an exception to the $5M limit placed on tax credits for expenditures for services of performing artists, which would exclude expenditures for services by "background artists and resident performing artists who are not cast in standard industry principal lead roles (may encourage a shift to employ New Mexico artists in these non-leading roles, thus increasing the benefits with no corresponding increase in tax costs)."
11) Clarifies and change the definition of "direct production expenditure." This includes limiting nonresident expenditures to only include wages and per diem and adding services provided by an accounting firm conducting an external audit (modest decrease in tax credit amounts).
12) Adds "industry crew" as a definition
13) Amends the definition of "personal service business" to include businesses without a physical presence (i.e.: virtual presence).
14) Amends the definition of "qualified production facility" to exclude "back lot facilities" not owned or controlled by the same entity that owns actual associated building. Also adds that a qualified production facility must contain either a sound stage or standing set used on a continual basis and located on at least 50 acres of space (may shift production to major facilities rather than cheaper and smaller shooting venues. This may be counterproductive if New Mexico post-production facilities are more expensive than out-of-state facilities).

15) Amends the definition of "vendor" by eliminating an enumerated list of exceptions and broadly defining the scope of a vendor's goods and services to those "related to a standard industry category of inventory . . ."

The AGO subsequently noted the few substantive changes between the original bill and the substitute. For the most part, the changes are stylistic for readability.

1) Increasing the number of days shooting at a soundstage from six to seven for a production company seeking the 5% credit with a total New Mexico budget less than thirty million dollars and from eight to ten days for a company with a New Mexico budget greater than thirty million.

ADMINISTRATIVE IMPLICATIONS

EDD/FO notes that, "The clarifications in this bill will streamline the program for productions and reduce administrative efforts. The film office would now be able to expedite the determination of many aspects of eligibility, included in the submission to TRD; and the film office will be able to reduce the need to liaison between the industry and TRD."

TRD reports a moderate ITD GenTax Impact (400 hours). In order to implement this, the following require changes: GenTax and TAP documents and configuration changes to the Business Credit Module. In addition, TRD would need to modify the forms, instructions and publications related to the film production tax credit. Audit and approval procedures will need to be developed. Department personnel and taxpayer education will be needed.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

- HB 216 – Assignment of Film Production Tax Credits
- HB 325 – Remove Some TV Shows From Film Tax Credit Cap

In addition the following two bills would provide additional requirements for claiming these deductions or would repeal the provision:

- HB 18 – Separate Tax Deductions & Exemptions
    - Amends NMSA 1978, Section 7-9-86, Deductions on gross receipts tax for sales to qualified film production companies.
- SB 346 – Tax Reform

TECHNICAL ISSUES

The bill has been carefully drafted to provide seamless transition across the January 1, 2016 boundary. The bill does not contain an effective date – assume 90 days after adjournment, or June 19, 2015. Neither an effective date, nor an applicability date is necessary.

The AGO points out some inconsistencies in the substitute bill:

1) Terms are now defined in three locations, 7-2F-1(U) and (V), the prior definitions section 7-2F-2, and the new additional definitions section (section 4 of the bill). It is clear why definitions are different between those defined in 7-2F-2 and in the new additional definitions section of the bill, but it may be helpful to remove terms that are defined in 7-2F-1 and place them with the other definitions in either 7-2F-2 or the new section, or both, un-

less the definitions in 7-2F-1 are explicitly intended to only be used within that section alone and not anywhere else in the Act.

2) There are multiple references throughout the act regarding the “total budget” and the “New Mexico budget.” Some of these references should be reviewed for consistency and determine if there is an intention to differentiate between each use and whether the some of the references should be uniform with one another.

3) Section 10 of the bill may be difficult to interpret without defining what a “specialized vendor” is or otherwise clarifying the use of the term. The current language is vague in multiple regards.

OTHER SUBSTANTIVE ISSUES

The SAO notes that this is merely one among a number of bills that have largely ignored the provisions of 9-15-56 NMSA 1978, which requires, among other provisions for economic development tax incentive legislation, the statement of a purpose or goal and an annual or periodic report to the legislature.

In the wake of the very competent 2014 TRD Tax Expenditure Report that covers the costs of virtually every active tax expenditure in statute, this further statement of costs and utilization may not be necessary.

In addition to the TRD Tax Expenditure Report, EDD/FO contracted with EPS (see the analysis of HB 325 of this session) for a phase 1 analysis of the costs and benefits of the film production tax credit.

SUGGESTED AMENDMENTS

SAO suggests conforming the bill to the requirements of 9-15-56 NMSA 1978 by including a standardized accountability section:

“The taxation and revenue department shall compile an annual report on the ______________________________ (name of tax credit or deduction) created pursuant to Section __ (Section/Subsection) that shall include the number of taxpayers approved by the department to receive the tax credit/deduction, the aggregate amount of credits/deductions approved and any other information necessary to evaluate the effectiveness of the tax credit/deduction. Beginning in ______ (year) and every ___ (number of years) thereafter that the tax credit/deduction is in effect, the department shall compile and present the annual reports to the revenue stabilization and tax policy committee and the legislative finance committee with an analysis of the effectiveness and cost of the tax credit/deduction and whether the tax credit/deduction is performing the purpose/purposes for which it was created.”

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL?

EDD/FO clearly indicates support for the provisions of this bill. If the bill is not enacted, it notes that, “The current program requires productions to add a percentage of contingency in their budget which decreases recruitment opportunities and the ability to increase jobs and support services for residents.”

"In addition, if this bill is not enacted:

- Some payment structures for qualifying expenditures would remain complex and anticipating a qualifying payment would remain unclear to productions when developing a budget (a vital step when determining which state in which to produce).
- Without limiting qualifying percentage pertaining to nonresident actors, and payment types, on TV projects, the credit payments are higher.
- Resident, non-lead actor's job opportunities would not be increased as compared to nonresident actors.
- Stand-alone TV pilots may not be considered for series in New Mexico which otherwise may under the 30 percent for series.
- If the definition of a "qualified production facility" is not included, use of infrastructure is less incentivized.
- The program would exclude payments to resident producers, writers and directors for the extra 5 percent when utilizing a qualified production facility for a required number of days."

"The more streamlined and comprehensive the program, there is an increased time value of staff and repeat business with productions with positive economic impact for the state."

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