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TESTIMONY

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ON FILM TAX CREDITS

By Michael Rathbone and Jessica Stearns

Testimony before the Economic Development and Business Attraction and Retention

To the Honorable Members of the Committee:

Ladies and gentlemen, thank you for the opportunity to testify today. My name is Michael Rathbone, and I am a policy researcher for the Show-Me Institute, a nonprofit, nonpartisan Missouri-based think tank that supports free-market solutions for state policy. The ideas presented here are my own. This testimony is intended to provide information on film tax credits and their impact on economic development, specifically in regards to the proposed House Bill 803 (HB 803).

Introduction

Film tax credits are not a new phenomenon within state economic development policy. Missouri first enacted the film tax credit program in 1998.[1] At the time, Missouri was one of the first states in the nation to enact this type of tax credit. Its purpose was to stimulate the growth of the film industry in Missouri by reducing the film studio's tax liability incurred within the state. The credit applies to tax liability incurred from expenditures on payroll and goods and services purchased within the state.

The original film tax credit program included a sunset provision that required reauthorization every six years. It was reauthorized in 2007 but allowed to sunset in November 2013. During that period the credit helped finance major motion pictures such as *Up in the Air* and *Gone Girl*. The success of *Gone Girl* at least partially inspired calls for reauthorizing the film tax credit program.[2]

Most Missourians want a thriving film industry. However, the key question is whether film tax credits will generate enough economic activity in Missouri to justify their use.

Research across the ideological spectrum, including papers from the Tax Foundation and the Center on Budget and Policy Priorities (CBPP), finds that film tax credits are not effective means of economic development.

Breakdown and Costs of the Program

The reauthorized film tax credit program involves[3]:

- The program has a funding cap of $4.5 million per year.
- The credit applies to 20 percent of in-state expenses and 10 percent of qualified out-of-state expenses.
    - Qualified in-state expenses can include business services leased or purchased by the production company and compensation and wages that the production company pays to Missouri residents.
    - Qualifying out-of-state expenses include compensation and wages that the production company pays to non-Missouri residents.
- Recipients can sell, exchange, and transfer film tax credits to any third party that has tax liability within the state.[4]

The new program differs from the previous film tax credits by reducing the amount of qualifying expenses the credit can be applied against (30 percent total for the new program, 35 percent for the old program). The bill authorizing the program makes no mention of a funding cap per film, nor does it state a requirement for the minimum amount to be spent in Missouri during production.

Economic Effects of Film Tax Credits

Several studies have examined the economic impact of film tax credits. Research across the ideological spectrum, including papers from the Tax Foundation and the Center on Budget and Policy Priorities (CBPP), finds that film tax credits are not effective means of economic development. For example, the CBPP study concludes,

> "State film subsidies are a wasteful, ineffective, and unfair instrument of economic development. While they appear to be a 'quick fix' that provides jobs and business to state residents with only a short lag, in reality they benefit mostly non-residents, especially well-paid non-resident film and TV professionals."[5]

The Tax Foundation's study finds that "Movie production incentives are costly and fail to live up to their promises. . . . Among these failures, the two most important are their failure to encourage economic growth overall and their failure to raise tax revenue."[6]

There are several reasons why film tax credits are not effective tools of economic development:

1. Film tax credits fail to permanently stimulate growth of Missouri's film production industry. In its 2010 report, the State Tax Credit Review Commission noted, "There is currently no long-term opportunity for the location of production facilities for films in Missouri."[7]
2. Film tax credits do not pay for themselves. In the same 2010 report, the Tax Credit Review Commission noted that the program ". . . fails to provide a positive return on investment to the state."[8] The majority of studies examining film tax credit programs find that these programs returned only cents on every dollar.[9] The state granted the production of

Gone Girl $2.36 million in tax credits but only received $609,225 in tax revenue.[10]

3. The highest paying jobs associated with film production go to non-Missouri residents. These jobs tend to be highly specialized and require skilled professionals from out-of-state.[11]

4. Any jobs created as a direct result of film production tend to be short-lived. Film production, by its very nature, is of limited duration. Once filming is wrapped, the production leaves and the associated jobs disappear.

5. Every job created by these tax credits is associated with high costs. According to the Motion Picture Association of America, the production of *Gone Girl* resulted in jobs for 116 Missourians. Given that the production received $2.36 million in tax credits, the cost per full-time equivalent (FTE) job was more than $122,000.[12]

Conclusion

Film tax credits are, on the surface, an attractive economic development tool. The correlation between the issuance of the credits and the decision by film companies to locate production in the state is easy to see. Plus, the industry itself is attractive. However, as the points articulated in this testimony show, the film tax credit program is a wasteful and inefficient attempt to stimulate economic growth.

Since these tax credits do not pay for themselves, taxpayers ultimately bear the burden for subsidizing these productions. Is subsidizing DirecTV for Ben Affleck, massages for Rosamund Pike, and espresso machines for movie stars, the best way to ensure economic development in this state?

Ultimately, targeted economic development tax credits, such as the film tax credits, put the government in the position of picking winners and losers. Letting the market decide which industries will flourish in Missouri is a better strategy. The state can enact policies that would make it more attractive to all businesses, such as reducing taxes and regulatory burdens.[13]

Michael Rathbone is a policy researcher and Jessica Stearns is an intern at the Show-Me Institute.

Is subsidizing DirecTV for Ben Affleck, massages for Rosamund Pike, and espresso machines for movie stars, the best way to ensure economic development in this state?

NOTES

[1] Christine Harbin, "Up in the Air: The Film Tax Credit Program Fails to Produce Economic Growth and Job Creation in Missouri" (Unpublished manuscript, Show-Me Institute, 2010), 3.

[2] Samantha Rinehart, "'Gone Girl' Inspires Lawmaker to Revive Film Tax Credits,'" *Southeast Missourian* (September 24, 2014), http://www.semissourian.com/story/2121610.html.

[3] http://www.house.mo.gov/billtracking/bills151/billpdf/intro/HB0803I.PDF.

[4] Third parties can purchase film tax credits and apply them to tax liabilities unrelated to film production. (Missouri Revised Statute 135.750 sub section 5. http://www.moga.mo.gov/mostatutes/stathtml/13500007501.HTML

[5] Robert Tannenwald, "State Film Subsidies: Not Much Bang for Too Many Bucks" (Report, Center on Budget and Policy Priorities, December 9, 2010), 12, http://www.cbpp.org/files/11-17-10sfp.pdf.

[6] William Luther, "Movie Production Incentives: Blockbuster Support for Lackluster Policy" (Special Report, Tax Foundation, January 2010), 16, http://taxfoundation.org/sites/taxfoundation.org/files/docs/sr173.pdf.

[7] Report of the Missouri Tax Credit Review Commission (November 30, 2010), 29, http://tcrc.mo.gov/pdf/TCRCFinalReport113010.pdf.

[8] Ibid.

[9] Tannenwald, "State Film Subsidies."

[10] This is according to Show-Me Institute estimates of tax rates applied to total salaries and consumption associated with the *Gone Girl* production. We applied the state income tax rate to total payroll of the production, and we applied the state sales tax rate to economic activity generated by the film. The amount of tax revenue the state received fell far short of the amount of money it granted the production.

[11] The authors made this determination by analyzing payroll documents from the Department of Economic Development for *Gone Girl*. *See also*, Tannenwald, "State Film Subsidies."

[12] http://www.mpaa.org/wp-content/uploads/2014/10/PRODUCTION-OF-TWENTIETH-CENTURY-FOX%E2%80%99S-GONE-GIRL-CONTRIBUTES-OVER-7-MILLION-TO-LOCAL-MISSOURI-ECONOMY.pdf. Since these jobs were temporary in nature, it was necessary to convert them to their full-time equivalent to capture their true cost. Thus, we reached the figure of $122,000 by dividing the $2.36 million in tax credits granted to the production by the total number of jobs created. This total was $20,344 per job. However, since production only lasted two months, it was necessary to multiply this total by six. $20,344 x 6 = $122,064. For more information on why this is necessary, please see http://taxfoundation.org/article/important-questions-ask-evaluating-film-tax-incentive-program,

[13] Patrick Ishmael and Michael Rathbone, "Cutting the Ties That Bind Us: End Missouri's Corporate Income Tax" (Essay, Show-Me Institute, 2012), http://showmeinstitute.org/publications/essay/taxes/864-end-corp-income-tax.html, and David Stokes, "Occupational Licensing of Massage Therapists in Missouri and Kansas" (Case Study, Show-Me Institute, 2008), http://showmeinstitute.org/publications/case-study/red-tape/90-occupational-licensing-of-massage-therapists-in-missouri-and-kansas.html.