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HOUSE OF REPRESENTATIVES

FISCAL RESPONSIBILITY COUNCIL
ANALYSIS

BILL #: HB 1647

RELATING TO: Entertainment Industry/Expenditures

SPONSOR(S): Representative(s) Davis; Lynn; and Murman

TIED BILL(S): HB 1649

ORIGINATING COMMITTEE(S)/COUNCIL(S)/COMMITTEE(S) OF REFERENCE:

(1) TOURISM YEAS 5 NAYS 0
(2) FISCAL RESPONSIBILITY COUNCIL YEAS 23 NAYS 0
(3) COUNCIL FOR COMPETITIVE COMMERCE
(4)
(5)

I. SUMMARY:

HB 1647 creates an entertainment industry financial incentive program within the Office of Tourism, Trade and Economic Development (OTTED) in the Executive Office of the Governor. The program's purpose is to encourage the use of Florida as a site for filming, and for providing production services for motion pictures and televisions programs by the entertainment industry.

There are two types of reimbursement incentives provided in the bill. The first is a 10% reimbursement for listed qualifying expenditures in Florida for entities that produce motion pictures or television programs. A $500,000 cap is placed on the reimbursement for a motion picture and a $100,000 cap is placed on a television program with each episode of a series considered a separate program. The second provides a reimbursement of 5% of gross billings, less sales tax, for a digital effects company that provides services or material to an entity producing a motion picture or TV program in the state. Additionally, a digital effects company that relocates to Florida is eligible for a one-time bonus equal to 5% of its billings for the year prior to relocating and for the first year of residence in Florida.

The Office of Film and Entertainment in the Executive Office of the Governor is responsible for receiving documentation for claimed expenditures, reviewing applications, and making recommendations to OTTED regarding an applicant meeting the criteria and the amount of reimbursement to be provided. OTTED is required to adopt rules to implement the incentive program. The bill provides for recovery of funds plus penalties and costs incurred by the state for investigating the claim if payment is made based upon a fraudulent claim. Penalties provided are to be in addition to any criminal penalties.

The bill appropriates $10 million from the General Revenue Fund to OTTED for the implementation of the program in FY 2002-2003.

The Tourism Committee passed the bill with a strike everything amendment. On March 8, 2002, the Fiscal Responsibility Council adopted two amendments to the Tourism Committee amendment. See Section VI for an explanation of the amendments.

II. SUBSTANTIVE ANALYSIS:

A. DOES THE BILL SUPPORT THE FOLLOWING PRINCIPLES:

1.	Less Government	Yes []	No [x]	N/A []
2.	Lower Taxes	Yes []	No []	N/A [x]
3.	Individual Freedom	Yes []	No []	N/A [x]
4.	Personal Responsibility	Yes []	No []	N/A [x]
5.	Family Empowerment	Yes []	No []	N/A [x]

For any principle that received a "no" above, please explain:

The bill creates a new program within OTTED that is to be administered by both OTTED and the Office of Film and Entertainment. The program, however, is intended to encourage economic growth in the entertainment industry in Florida.

B. PRESENT SITUATION:

Office of Film and Entertainment
Created in 1999, the Office of Film and Entertainment in the Executive Office of the Governor is responsible for developing, marketing, promoting, and providing services to the state's entertainment industry. The activities of the Office of Film and Entertainment are guided by a 5-year strategic plan developed in part by its industry advisory council. The Office is also responsible for the single application process for the upfront tax exemption certification for the sales and use tax exemption and for qualifying companies for eligibility for receipt of such certification.

The motion picture industry in Florida is comprised of over 3500 establishments, employs over 39,000 full time employees and generates approximately $3.9 billion in total revenues from all business units (in-state and out-of-state, including location filming.)

The Office has a budget of approximately $773,000 and a staff of 3 FTE and 2 OPS ($254,605 was spent on staff in 2001). The funding and staffing of such offices in Florida's competitor states is higher. For example, North Carolina has a staff of 6 and a budget of over $850,000; Texas has 6 staff with a $1 million budget; California has a staff of 10 with a $1.3 million budget; Illinois has 9 staff and over $850,000 in funds; and Maryland has 6 staff with over $1 million in its budget.

Some of the concerns brought to the Tourism Committee by the Film and Entertainment Commissioner at its January 31, 2002 meeting were as follows:

- Slowed economic growth in the entertainment industry in Florida due to national production activity.
- Lack of incentives to promote business growth and expansion.
- Level of staffing and resources don't match up with the level of statutory deliverables.
- Florida has been out-competed by Canada, Puerto Rico & Australia.

Use of Incentives for Entertainment Industry: Nationally & In Florida
The US Dept. of Commerce's 2001 study on the US motion picture industry indicated that the industry is especially significant for several state economies: California, New York, Florida, Texas, Illinois and North Carolina. These six states account for about 88% of national revenues generated

directly by the motion picture industry in the US. They also account for almost four-fifths of total employment and 65% of the total number of establishments classified in the industry.
According to the 2001 Annual Report on the Motion Picture Tax Exemption prepared by the Florida Office of Film and Entertainment, countries, states and local communities have developed policies that include governmental incentives as key selling tools to recruit and retain production business. Decisions on where to begin a project have become increasingly driven by the cost parameters, rather than creative ones.

The incentives offered by other countries plus lower exchange rates have been part of the reason for what is referred to as "runaway" productions and the loss of industry activity in the United States, in general, and Florida, in particular. An example of incentives offered by other countries is that of Canada which offers federal and provincial tax credits of 22% to 46% of labor expense (yielding up to a 10% reduction in overall production expense), and Australia offers more than a 10% labor tax credit in certain cases.

Several states have begun to look again at their incentives package. Alabama recently enacted changes in its sales tax exemptions to allow for certain entertainment industry exemptions. South Carolina is reexamining what it offers as well as what is being done in other competitive states. California Governor Gray Davis has been advocating what is referred to as "the first sizable tax credit" to be offered to entice the film and TV shows to stay in California. According to articles concerning the proposal, he is seeking a 15% tax credit on the first $25,000 earned by a worker on lower budget projects (less than $10 million) if substantially all of the production takes place in the state.

The Florida Office of Film and Entertainment stressed the need to retain Florida's current tax exemption for the entertainment industry as an incentive both to recruit such businesses to bring their work to Florida and to retain such businesses in the state. More than 22 states now offer similar sales and use tax exemptions with 13 of those states, including Florida, offering a point of sale exemption. The return on investment (ROI) analysis of the Florida point of sale exemption in Calendar Year 2001 showed that for $1,441,129 in tax exemption, the economic impact to the state was approximately $162.4 million for a return on investment of 113:1.

The 2001 Annual Report stated that "to effectively compete in this environment, Florida's motion picture industry must address the cost of conducting motion picture and television business in the State of Florida."

Florida Exemptions & Tax Advantages

Currently, Florida provides a single application process for qualified entertainment industry production companies to obtain a certificate of exemption to take advantage of exemptions under ss. 212.031, 212.06, and 212.08, F.S.

1. **Lease or rental of real property:** Section 212.031(1)(a)9., F.S., provides that property used as an integral part of performance of any activity or service performed directly in connection with the production of a qualified motion picture is tax exempt. Examples of things included in exempt services are photography, sound & recording, casting, location managing and scouting, shooting, creation of special and optical effects, animation, adaptation, etc.
2. **Fabrication labor exemption for motion picture producers:** Section 212.06(1)(b), F.S., provides that fabrication labor is not taxable when a motion picture producer uses his or her own equipment and personnel to produce a qualified motion picture defined in Florida law.
3. **Master tapes, records, films, or video tapes (partial exemption):** Section 212.08(12), F.S., provides that gross receipts from the sale or lease of, and the storage, use, or other consumption in Florida of, master tapes or master records embodying sound, or master films

or master video tapes are exempt from taxation. Amounts paid to studios for the tangible elements of such masters are taxable.

4. **Equipment exemptions:** POINT OF SALE EXEMPTION—Section 212.08(5)(f), F.S., provides an exemption on the purchase or lease of certain equipment used exclusively as an integral part of production activities in Florida. This pertains to motion picture equipment, video equipment, and sound recording equipment. In order to be exempt at the point of sale, the production company must apply for a certificate of exemption to be presented to a registered Florida sales and use tax dealer when making purchases and rentals of qualified production equipment.

Section 288.1258, F.S., provides the single application process for qualified entertainment industry production companies to obtain a certificate of exemption from sales and use taxes on the lease or rental of real property used as an integral part of the performance of qualified production services; motion picture or video equipment and sound recording equipment that are purchased or leased for use in this state in certain specific entertainment production activities; and, part of the sales price of master tapes, records, films, or video tapes. The Office of Film and Entertainment is responsible for determining if a company is a "qualified production company" and is, therefore, eligible for exemption certification. The Department of Revenue provides the certificate of exemption. The Office and the Department of Revenue work together on the implementation of this application and certification process.

In addition to any other tax exemptions that are specific to the entertainment industry, Florida offers certain tax advantages to persons coming to the state for a specific project or for companies considering relocation. Some of those tax advantages are as follows:

- No personal income tax (41 states do have a personal income tax),
- No corporate income tax on limited partnerships,
- No corporate income tax on subchapter S-corporations,
- No assessment of property taxes at state level,
- No property tax on business inventories,
- No property tax on goods-in-transit for up to 180 days,
- No sales and use tax on goods manufactured or produced in Florida for export outside the state,
- No sales tax on purchases of raw materials incorporated in a final product for resale, including non-reusable containers or packaging,
- No sales/use tax on boiler fuels, and
- No sales/use tax on electricity used in the manufacturing process.

Florida also offers incentives through Enterprise Florida, Inc., for the relocation of corporate headquarters that afford a certain number of new jobs to Floridians.

C. EFFECT OF PROPOSED CHANGES:

HB 1647 creates an entertainment industry financial incentive program within the Office of Tourism, Trade and Economic Development in the Executive Office of the Governor. The program's purpose is to encourage the use of Florida as a site for filming, and for providing production services for motion pictures and television programs by the entertainment industry.

There are two types of reimbursement incentives provided in the bill. The first is a 10% reimbursement for listed qualifying expenditures in Florida for entities that produce motion pictures or television programs. A $500,000 cap is placed on the reimbursement for a motion picture and a $100,000 cap is placed on a television program with each episode of a series considered a separate program. Eligible expenditures used in determining reimbursement include:

- Salaries and benefits paid to state residents;
- Rental of real and personal property used in production;
- Payments to state residents or state-domiciled entities for preproduction, production, and postproduction services; and,
- Costs of set construction.

The second provides a reimbursement of 5% of gross billings, less sales tax, for a digital effects company that provides services or material to an entity producing a motion picture or TV program in the state. Additionally, a digital effects company that relocates to Florida is eligible for a one-time bonus equal to 5% of its billings for the year prior to relocating and for the first year of residence in Florida.

The Office of Film and Entertainment in the Executive Office of the Governor is responsible for receiving documentation for claimed expenditures, reviewing applications, and making recommendations to OTTED regarding an applicant meeting the criteria and the amount of reimbursement to be provided.

The bill provides for recovery of funds plus penalties and costs incurred by the state for investigating the claim if payment is made based upon a fraudulent claim. Penalties provided are to be in addition to any criminal penalties.

OTTED is required to adopt rules to implement the incentive program.

The bill appropriates $10 million from the General Revenue Fund to OTTED for the implementation of the program in FY 2002-2003.

D. SECTION-BY-SECTION ANALYSIS:

See "Effect of Proposed Changes".

III. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT:

A. FISCAL IMPACT ON STATE GOVERNMENT:

	FY 02-03	FY 03-04	FY 04-05
1. Revenues:			
	Indeterminate	Indeterminate	Indeterminate
2. Expenditures:			
General Revenue	$10 million	Unknown	Unknown

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

	FY 02-03	FY 03-04	FY 04-05
1. Revenues:			
	Indeterminate	Indeterminate	Indeterminate
2. Expenditures:			
	N/A	N/A	N/A

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

Through the appropriation, the bill could bring additional television, motion picture and digital effects work to the state. Such an increase could assist in the employment of Florida residents in the entertainment and related industries; thereby increasing spending by residents and increased sales tax revenue. The bill is intended to encourage the relocation of digital effect entities which could bring additional employment and tax revenues to the state.

D. FISCAL COMMENTS:

Section 2 of the bill appropriates $10 million from the General Revenue Fund to OTTED to implement the act in FY 2002-2003. The strike everything amendment by the Tourism Committee increases the appropriation to $20 million. There will be an increased workload on both OTTED and the Office of Film and Entertainment in implementing the program in FY 2002-03 and continuing the program in subsequent years. If the funding needed for additional staff is not included as part of the appropriation, there will be a need for additional resources for the Office of Film and Entertainment to carry out its responsibilities outlined in the bill as well as for OTTED.

The Fiscal Responsibility Council adopted two amendments to the strike everything amendment by the Tourism Committee. These amendments remove the appropriation and make the creation of the program subject to a specific appropriation.

IV. <u>CONSEQUENCES OF ARTICLE VII, SECTION 18 OF THE FLORIDA CONSTITUTION</u>:

A. APPLICABILITY OF THE MANDATES PROVISION:

This bill does not require counties or municipalities to expend funds.

B. REDUCTION OF REVENUE RAISING AUTHORITY:

This bill does not reduce the authority of counties or municipalities to raise revenue.

C. REDUCTION OF STATE TAX SHARED WITH COUNTIES AND MUNICIPALITIES:

This bill does not reduce the percentage of a state tax shared with counties or municipalities.

V. <u>COMMENTS</u>:

A. CONSTITUTIONAL ISSUES:

None.

B. RULE-MAKING AUTHORITY:

The bill requires OTTED to adopt rules to implement the newly created s. 288.1254, F.S., including rules relating to records to be submitted in substantiation of an application.

C. OTHER COMMENTS:

Some identified questions concerning the language in the legislation follow:

1. What is meant by “entity”? Is it a production company?

2. Does the digital effects company that receives a 5% reimbursement for providing materials and services to an entity producing a motion picture or television program in Florida have to be domiciled in Florida? Is this money paid to an out-of-state company?
3. Does any other type of company relocating to Florida get a state incentive on its prior year's billings in another state or country as is proposed for digital effects companies?

Film Florida, Inc., which is the statewide organization composed of Florida's local film commissioners and representatives of other segments of the entertainment industry, sent the following comments concerning the legislation:

- There needs to be an employment trigger in the bill language so that there would be a requirement to hire Floridians in order to receive the incentive (suggestions ranged from 60% to 80%). Certain positions could be excluded such as above the line.
- Commercial production and music videos should be included in the language with perhaps a $50,000 cap on their rebate, also to be based on 10% of qualifying expenditures.
- Conform the appropriations, single motion picture cap, and television program cap in HB 1647 to that of SB 2242, its companion.

At the February 20, 2002 meeting of the Tourism Committee, the Committee Members were given some general return on investment information on the impact of the bill and the amendment. The Members requested that the Office of Film and Entertainment prepare more detailed return on investment information on the investment being proposed in the amendment that was adopted. The information is being prepared and not available as of this date.

VI. <u>AMENDMENTS OR COMMITTEE SUBSTITUTE CHANGES</u>:

On February 20, 2002, the Tourism Committee passed HB 1647 with one strike everything amendment. The amendment addresses issues raised in the Comment section of the analysis and differs from the original bill in the following ways:

- Amends s. 288.125, F.S., to extend the definition of "entertainment industry" to cover all of the provisions in Chapter 288 pertaining to the Office of Film and Entertainment and the entertainment industry.
- Expands the purpose of the incentive program to include production services for commercials and music videos as well as motion pictures and television programs.
- Creates the incentive program within the Office of Film and Entertainment versus the Office of Tourism, Trade, and Economic Development.
- Provides definitions for terms used in the amendment. Omits use of terms that were identified as too nebulous. Terms defined: filmed entertainment, production costs, qualified expenditures, qualified production, qualified relocation project, and relocation.
- Broadens the incentive reimbursement program to include commercials and music videos.
- Requires that at least 70% of production costs are spent in Florida and that at least 75% of the production workforce are Florida residents or are state-domiciled entities in order to be a qualified production eligible for reimbursement. The bill had no requirements regarding workforce and used the words "wholly or substantially" when referring to production costs.
- Requires a minimum of $1 million in qualified expenditures in order to be considered for eligibility for reimbursement. The bill had no minimum.
- Provides a maximum reimbursement for any single motion picture to be $2 million, subject to appropriation, unless the total qualified expenditures exceed $50 million in which case the maximum is $2.5 million, subject to appropriation. The maximum for any single television pilot, television series, made for television movie, music video or commercial is $200,000, subject to appropriation. The bill provided $500,000 per motion picture and $100,000 per television program; however, each episode of a television series was counted as a television program.

- Qualified expenditures are the same as in the bill.
- Provides that a digital effects, finance, distribution, or post production company in the state that furnishes services or digital material to a qualified production is eligible for a payment in an amount not to exceed 5% of its gross billings, less sales tax. The bill only provides a reimbursement to a digital effects company and does not specify that the company must be a Florida company nor that the productions it serves are ones that are qualified productions.
- Expands the incentive for relocation to Florida to finance, distribution and post production companies located in other states or countries. The bill limits this just to digital effects companies. Limits the one-time bonus incentive to such companies that are certified as qualified relocation companies and the amount of the incentive to 5% of its billings for the first 12 months of doing business in its Florida domicile. There is no requirement for certification in the bill and the incentive includes an additional 5% of billings for the 12 months prior to coming to the state and limits the foreign country to Canada.
- Requires that double reimbursement of reasonable costs is included in penalty for fraudulent claims.
- Appropriates $20 million from General Revenue for implementation of the program. The bill appropriates $10 million.

On March 8, 2002, the Fiscal Responsibility Council adopted two amendments to the strike everything amendment by the Tourism Committee. These amendments remove the appropriation and make the creation of the program subject to a specific appropriation.

VII. SIGNATURES:

COMMITTEE ON TOURISM:

Prepared by:	Staff Director:
Judy C. McDonald	Judy C. McDonald

AS REVISED BY THE FISCAL RESPONSIBILITY COUNCIL:

Prepared by:	Staff Director:
Kurt Hamon	David K. Coburn