Policy Matters Ohio

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Tax & Budget

Testimony on HB 525 to the House Government Accountability and Oversight Committee

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Good afternoon, Chairman Blessing, Vice Chair Reineke, Ranking Member Clyde and members of the committee. I am Wendy Patton, senior project director at Policy Matters Ohio, a nonprofit, nonpartisan research institute with the mission of creating a more prosperous, equitable, sustainable and inclusive Ohio. Thank you for this opportunity to testify today on House Bill 525, which would increase the state's cap for movie tax credits from $40 million a year to $100 million a year and broaden it to include the production of Broadway-bound plays.

The entertainment sector is not one of the nine strategic industries targeted by Jobs Ohio,[1] the privately-operated economic development entity for the state, yet the proposed increase in the motion picture tax credit would put it on par with the Job Creation Tax Credit, Ohio's biggest economic development tax credit that serves all sectors. According to the fiscal note for House Bill 525, it would cost the state's General Revenue Fund an estimated $58 million, and local governments and public libraries an estimated $2 million, in 2019. Today the Ohio motion picture tax credit ranks 43rd in size among the 129 tax breaks making up the $9 billion tax expenditure tally. With the proposed expansion, it would move up to 26, tied in 2019 with the Historical Structure Rehabilitation Credit.

The film tax credit is not a universal incentive across the 50 states and the District of Columbia. Nineteen states give tax credits. Some states provide other incentives, like grants or rebates for in-state expenditures. Eighteen states have no incentives for this sector.[2] Of the five states that share Ohio's borders, three: Michigan, Indiana, and West Virginia, have no state film tax credits or other incentives for this sector.[3]

Ohio presently offers the motion picture industry $40 million each year in tax credits which are both refundable and transferrable,[4] one of just a few states to have both of these features. Refundability means that if the approved tax credit exceeds tax liability, the state writes a check for the difference. Transferability allows motion picture companies to sell the tax credits, typically on a secondary market, raising equity for a project.

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[1] The nine targeted job creation sectors include advanced manufacturing, automotive, aviation and aerospace, biohealth, energy and chemicals, financial services, food and agribusiness, information technology and logistics and distribution. See Jos Ohio website at http://jobs-ohio.com.

[2] Bryn Elise Sandberg, Film and TV Tax Incentives: A State-by-State Guide, Hollywood Reporter, April 21, 2016 at https://www.hollywoodreporter.com/news/film-tv-tax-incentives-a-885699 and National Conference of State Legislatures, State Film production incentives and programs, January 30, 2018 at http://www.ncsl.org/Portals/1/Documents/fiscal/2018StateFilmIncentivePrograms_20189.pdf

[3] Id.

[4] Id.

Tax credit transfers have become sophisticated financial transactions, turning what should be a transparent tool into something obscure. The sale of the tax credit allows the buyers – the unintended beneficiaries of the subsidy – to escape scrutiny or accountability. The buyer of the credit needs no connection to the motion picture industry. But they have Ohio tax liability, and they buy the credits to reduce their Ohio taxes. This is why the transferrable tax credit is called "leaky" – a lot of the value of the credit leaks out to the buyer of the tax break, and to the brokers, insurers, attorneys and others who have created the market for tradable movie tax credits and who put the transaction together.

Buyers of the tax credit typically pay less than a dollar for each dollar of tax credit because of risk. Risks may include lack of information on the project and the tax credit marketplace itself: this creates the need for a secondary market with experienced brokers to facilitate the sale of the movie tax credit to unrelated entities. Buyers face the risk that the seller may be unable to comply with the state agreement, causing the state to rescind the tax credit, or legislators may change the law, or some outside force may occur that prevents project completion: the death of a star, a natural disaster.[5] Insurers such as Lloyds of London may provide insurance for these risks, but at a cost.[6] All of these costs represent leakage of taxpayer dollars intended to subsidize the motion picture industry. In 2008, then-tax commissioner Rich Levin testified on transferable tax credits proposed under House Bill 196 of the 127th General Assembly. "The tax credits are being used to offset tax liabilities in Ohio that … have nothing to do with film production," he said.[7] In vetoing House Bill 196 in 2009, Governor Strickland wrote: "A transferable credit may change hands many times, making accurate tax administration cumbersome and expensive. It is also an inefficient way to subsidize an industry, as much of the credit will be realized by those who are not involved in the film industry…."[8]

Tax credits are often premised on the claim that the economic activity they generate will more than replace the taxpayer dollars given in the subsidy. A study of Ohio's movie tax credit done by Cleveland State University in 2015 found that between 2011 and 2015, the state spent $32 million on the tax credit, and total taxes generated by the economic activity amounted to $22 million: $15.4 million was federal tax revenue and just $6.7 million was state and local tax revenue.[9] Ohio's Motion Picture Tax Credit fell far short of paying for itself in terms of tax dollars returning to the state, a common measure of the effectiveness of economic development incentives. Studies of movie tax credits in other states had similar findings. For example, Virginia's Joint Legislative Audit and Review Commission found Virginia's incentives, which include a grant program as well

[5] "For the buyers to benefit from the transaction, the tax credits have to be sold for less than their full value. Prices vary, but brokers say that it's typical for sellers to get 85 or 90 cents on the dollar." Josh Goodman, "Tax Breaks for Sale: Transferable film tax credits explained," Pew Charitable trust, December 14, 2012. http://www.pewtrusts.org/en/research-and-analysis/blogs/stateline/2012/12/14/tax-breaks-for-sale-transferable-tax- credits-explained

[6] Matthew Savare, "Beyond the Basics: The Inside Scoop on Production Credits," Filmmaker, Fall, 2009 at https://www.lowenstein.com/files/Publication/a071b8e4-744a-4d1f-9105-5a728751d845/Presentation/PublicationAttachment/90e89814-6197-4580-aca8-5cff2e2b6f94/Beyond%20The%20Basics%20MS%2010.09.pdf

[7] Testimony of Tax Commissioner Rich Levin on House Bill 196 to the House Ways and Means Committee, November 19, 2008.

[8] Gongwer News Service, "Vetoed Bill," January 6, 2009.

[9] Candi Clouse and Nikki Glazer, Box Office Ohio: Analysis and Economic Impact of the Film Industry in Northeast Ohio and Ohio, Center for Economic Development, June 2015 at https://engagedscholarship.csuohio.edu/cgi/viewcontent.cgi?article=2335&context=urban_facpub

as a tax credit, provide a very low return in revenue to the state (20 cents per dollar invested for the tax credit and 30 cents per dollar for the grant.) [10]

A 2016 survey by the National Conference of State Legislatures found that 10 states had ended their film incentive programs since 2009, including Michigan, New Jersey and Alaska.[11] Since then, new incentives have been enacted. Today, the National Conference of State Legislatures lists seven states in which film tax credits have been ended or modified – like West Virginia, which ended their movie incentive earlier this year at the recommendation of Tourism Commissioner Chelsea Ruby. Ruby explained: "What we've seen in the last decade of these programs is a classic race to the bottom….There are certain productions that require specific locations, but a majority of productions can be done anywhere, and those productions always chase the largest credit."[12] West Virginia Delegate Paul Espinosa concurred, saying: "While I very much support these type of productions, I can't continue to support using these dollars when they could be used in a host of other manners in our budget for a higher benefit."[13]

The motion picture film industry is concentrated in a handful of states.[14] Growing such an industry from scratch is an expensive proposition, explains Matthew Murray, an economics professor at the University of Tennessee who studied the Alabama credit: "It's great for the headlines. It's great for the front pages of the newspapers for the politicians to say 'We made this happen.' But you're not likely to create the deep supply chain linkages in the industry that are going to build a long-term industry in the state,"[15]

In a 2010 article entitled: "Down The Rabbit Hole: The Madness Of State Film Incentives as a "Solution" To Runaway Production,"[16] author Adrian McDonald, supervising research analyst for the Los Angles film office, described the initiation of state tax credits in the 1990's and early 2000's as a problem of international competition with Canada, and found that the cost of retaining film and motion picture jobs in the United States "…has come at an astronomical and unsustainable cost." He suggests federal legislation as the way to put an end to it.

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[10] Virginia Joint Legislative Audit and Review Commission, "Evaluation of Film Incentives, Report to the Governor and the General Assembly of Virginia," November 13, 2017 at http://jlarc.virginia.gov/pdfs/reports/Rpt501.pdf

[11] Jeff Sweigart, Ohio offers millions to bring more Hollywood movies to state, Dayton Daily News, May 22, 2017 at https://www.mydaytondailynews.com/news/ohio-offers-millions-bring-more-hollywood-movies-state/lAIcIDV3qpkeSJS3E76nkK/

[12] Jake Jarvis, Gov. Justice signs film tax credit repeal bill, The State Journal, February 5, 2018 at https://www.wvnews.com/statejournal/news/gov-justice-signs-film-tax-credit-repeal-bill/article_2f84f89a-7fc1-5cbf-af26-1aac0f3a27d3.html

[13] Id.

[14] The movie production industry is concentrated in a handful of states. According to the Virginia Joint Legislative Audit and Review Commission, cited above, just 6 states have a location quotient, or a workforce concentration, of greater than 1, showing a competitive advantage in the movie industry: California (4.2), New York (2.7), Louisiana (1.3), Georgia (1.3), Hawaii (1.2). Their study argued against the tax break, for Virginia, pointing out that the location quotient for Virginia was just three tenths of one percent. (The location quotient for all other states – combined – was less than one.)

[15] Matthew Murray and Donald Bruce, " Evaluation of Alabama's Entertainment Industry Incentive Program and New Markets Development Program, March 9, 2017 at http://media.al.com/news_mobile_impact/other/AL%20ENTERTAIN%20NEWMKTS%203%209%2017.pdf cited in Sweigart, Op.Cit.

[16] Adrian H. McDonald, Down the Rabbit Hole: The Madness of State Film Incentives as a 'Solution' to Runaway Production (November 23, 2011). University of Pennsylvania Journal of Business Law. Available at SSRN: https://ssrn.com/abstract=1495091

If Ohio wishes to dedicate $100 million a year to stimulate the motion picture and theater industry, it would be far better to debate the merits of creating a new grant program[17] side by side with the need for adequate funding of schools, creating quality pre-K so more children learn to read on time, ensuring clean water, protecting vulnerable children and seniors, ending the drug epidemic and restoring funding to local communities. There are many needs in this state. Fostering new financial services for unknown investors to avoid state tax liability so as to help some private movie production firms raise equity is a purpose that pales in comparison to the need for basic public services in Ohio communities.

Thank you for this opportunity to testify. I would be glad to answer questions.

[17] At least six states had grant programs - sometimes in combination with other incentives - that used to incentivize the motion picture industry in 2016.