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

SPONSOR: Robinson DATE TYPED: 1-31-02 HB

SHORT TITLE: Film Production Tax Credit SB 328

ANALYST: Neel

REVENUE

Estimated Revenue		Subsequent Years Impact	Recurring or Non-Rec	Fund Affected
FY02	**FY03**			
	($3,203.0)		Recurring	General Fund
	$248.0		Recurring	Local Governments

(Parenthesis ( ) Indicate Revenue Decreases)

Duplicates/Conflicts with/Companion to/Relates to HB118, SB88, SB262, and SB273

SOURCES OF INFORMATION

LFC files
Taxation and Revenue Department (TRD).

SUMMARY

Synopsis of Bill

Senate Bill 328 amends statute to create the "film production tax credit" for up to 15 percent of the direct production expenditures made in New Mexico attributable to the production of a film. SB 328 defines "direct production expenditures" to include the cost of the story, wages and salaries for New Mexico residents, the cost of set construction, the cost of photography and related services, the cost of editing, rental of facilities and equipment, and other direct costs of producing the film, among other expenses.

To be eligible the film company must:

- Submit to the New Mexico film division (NMFD) of the Economic Development Department information required by the division to demonstrate that the film company has met all NMFD's requirements;

- Apply to TRD on a prescribed application the amount of direct production expenditures made in New Mexico.

The Film company may apply the film production tax credit against personal income tax liability or corporate income tax liability.

FISCAL IMPLICATIONS

TRD's assumptions for the fiscal impact are as follows:

From FY 94 to 01 filmmakers average annual expenditures related to production in New Mexico was approximately $30.0 million. TRD assumes that $15.0 million of the production costs will qualify under current statute (Section 7-9-86 NMSA). Provision included in SB 328 expand qualifying expenditures by an additional $12.0 million

Current Statute (Section 7-9-86 NMSA) allows film production companies to deduct gross receipts tax deduction, which TRD estimates is worth approximately 6% (average combined state and local option gross receipts tax rate) of qualified production costs. The proposed credit, under SB 328, is worth 15% of "direct production expenditures". The proposed credit cannot be claimed on expenditures for which the filmmaker has delivered a nontaxable transaction certificate (NTTC) pursuant to 7-9-86. The definition of "direct production expenditures" contained in the bill for the most part includes all qualified "production costs" in 7-9-86. However, provisions in this bill allow many ancillary costs—which do not qualify for the gross receipts deduction—to qualify for the credit. As a result, filmmakers can elect to either issue the NTTC for a 6% deduction, or claim the 15% credit for most qualifying expenditures. Logically, filmmakers will choose the refundable credit.

TRD assumes 87% of filmmakers' direct production costs will qualify for the income tax credit. The remaining 13% will be eligible for the gross receipts deduction. This split is based on the fact that definitions in the credit proposal are, in some regards, slightly more restrictive than corresponding definitions contained in 7-9-86. However, this proposal allows several indirect production costs that are not currently eligible for the existing gross receipts deduction, to qualify for the proposed credit.

The fiscal impact represents the net effect of the current gross receipts deduction and the incentives provided by the proposed credit. The more economically attractive 15% credit does not adversely affect local government revenue sources. Therefore, the expected shift from gross receipts deductions to credit claims will result in a net positive fiscal impact for local governments.

The estimate assumes no multiplier effects associated with increased filmmaking. Since the Department does not have enough information about individual businesses to determine whether a particular incentive is the key factor influencing the decision to locate in the state, we assume the level of economic activity is unaffected by the passage of any individual piece of legislation.

TECHNICAL ISSUES

TRD notes the following technical issues:

1. There are several differences between the definitions contained in Section 7-9-86 and this proposal. For the purposes of the gross receipts deduction, 7-9-86 defines "production company" and this proposal uses the same definition to define " film production company." Section 7-9-86 defines "production costs", and this bill defines "direct production expenditure." This bill restricts the definition of "direct production expenditure" to include wages and salaries only to New Mexico residents, 7-9-86 includes all wages and salaries. This proposal explicitly includes photography in the definition of "direct production expenditure", photography is excluded from the definition of "production costs" in 7-9-86. This bill defines "film" to include only national advertising messages, 7-9-86 includes all advertising messages.

2. This bill does make explicit that the tax credit is for "direct production expenditures" <u>made in New Mexico,</u> (page 1, line 21) but it is not at all clear what that means. Does it mean the payment originates in New Mexico or accrues to the benefit of New Mexico residents? This bill does restrict the definition of "direct production expenditure" to include wages and salaries paid to New Mexico residents, as well as airfare and insurance costs purchased through New Mexico-based firms. But this same restriction is not extended to other types of expenditures that could go to out-of-state vendors.

3. The provision that the excess credit claimed over and above the taxpayer's liability shall be refunded violates the anti-donation clause (Article IX, Section 14) of the New Mexico Constitution. The provisions have nothing to do with a *refund* of taxes, as money that has not been paid over to the state cannot be refunded. This is nothing less than a direct payment for doing business in New Mexico.

SN/njw