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State film, TV tax credits pay off, study says

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BY RICHARD VERRIER

A new report from the nation's largest metropolitan planning organization says California's film and television tax credit program is a good investment but needs to be extended and restructured to keep the entertainment industry from fleeing the state.

The state film incentive program generated an 11% return on investment in its first three years and helped generate $4.3 billion in economic activity and 22,300 jobs, according to a study released Thursday by the Southern California Assn. of Governments.

Since 2009, California has been allocating $100 million annually to film and TV productions, using a lottery system to award 20% to 25% tax credits as an inducement to keep their business in the state.

In the first three years of funding, 109 film projects were funded and completed. Those projects — which included the feature films "The Social Network," "Bridesmaids" and "We Bought a Zoo" — generated a combined $247.7 million in state and local taxes and $1.6 billion in worker salaries, according to the report.

For every $1 of tax credit issued, $1.11 was returned to the state and local governments in the form of tax revenue, and state gross domestic product increased by $9.48, the study concludes.

"You cannot look at this program and not see it as a formidable economic and fiscal benefit," said Hasan Ikhrata, SCAG executive director. "California is very much at risk of losing its film industry, and without this program the past five years, the losses would have been more painful."

The effectiveness of the incentive program has been hotly debated. A coalition of industry and labor groups has been lobbying for legislation that would expand and broaden the incentive so that California can more effectively compete with rivals in New York, Georgia, Louisiana, London and Vancouver, Canada.

As with other recent reports, including one from the Milken Institute, the SCAG study highlights the erosion of California's homegrown entertainment industry, noting that last year alone 75% of the 41 live-action feature films with budgets in excess of $75 million were filmed outside California.

The loss of big-budget pictures cost California $410 million in state and local tax revenue, 47,600 jobs and total economic output of $9.6 billion, according to the study, which was conducted by the Los Angeles County Economic Development Corp.

"It is not hyperbole to assert that the state is losing jobs to other states and nations and is continuing to bleed out at an increasing rate," wrote Christine Cooper, the principal author of the research.

To help bring back more production, the SCAG report recommends various improvements, including lifting the current $75-million budget cap on films that may qualify for the incentive and offering a subsidy targeting the visual effects industry.

The economic development group wrote a similarly positive appraisal of the film tax credit in 2011, although that study was perceived by some critics as being biased because it was commissioned by the Motion Picture Assn. of America, the lobbying arm of the major studios.

Some state lawmakers have questioned the costs of the program, citing a study by the state's Legislative Analyst's Office that said the program caused a net loss in state revenue. A study by UCLA found the program had a more modest return on investment, generating $1.04 in

tax revenue for every $1allocated in tax credits.
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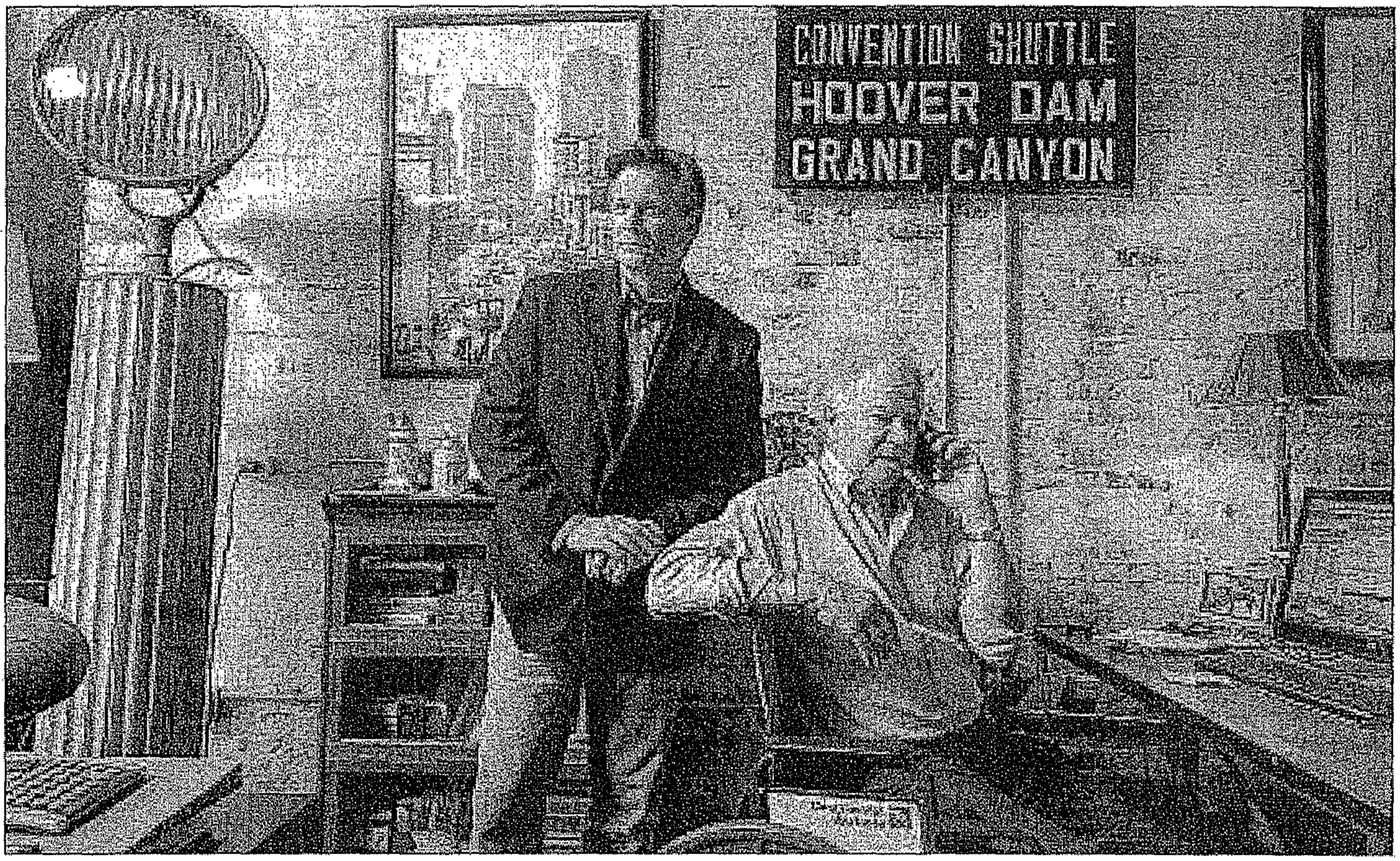
Making film deals with tax credits

Hollywood's new financiers sell state incentives for movie studios to people looking to cut taxes.

BY RICHARD VERRIER



DUSTIN CHAMBERS For The Times

TAX CREDIT BROKERS Ric Reitz, left, and Wilbur Fitzgerald own Georgia Entertainment Credits, which finds buyers for tax credits given to producers shooting movies, TV shows and commercials in the state.

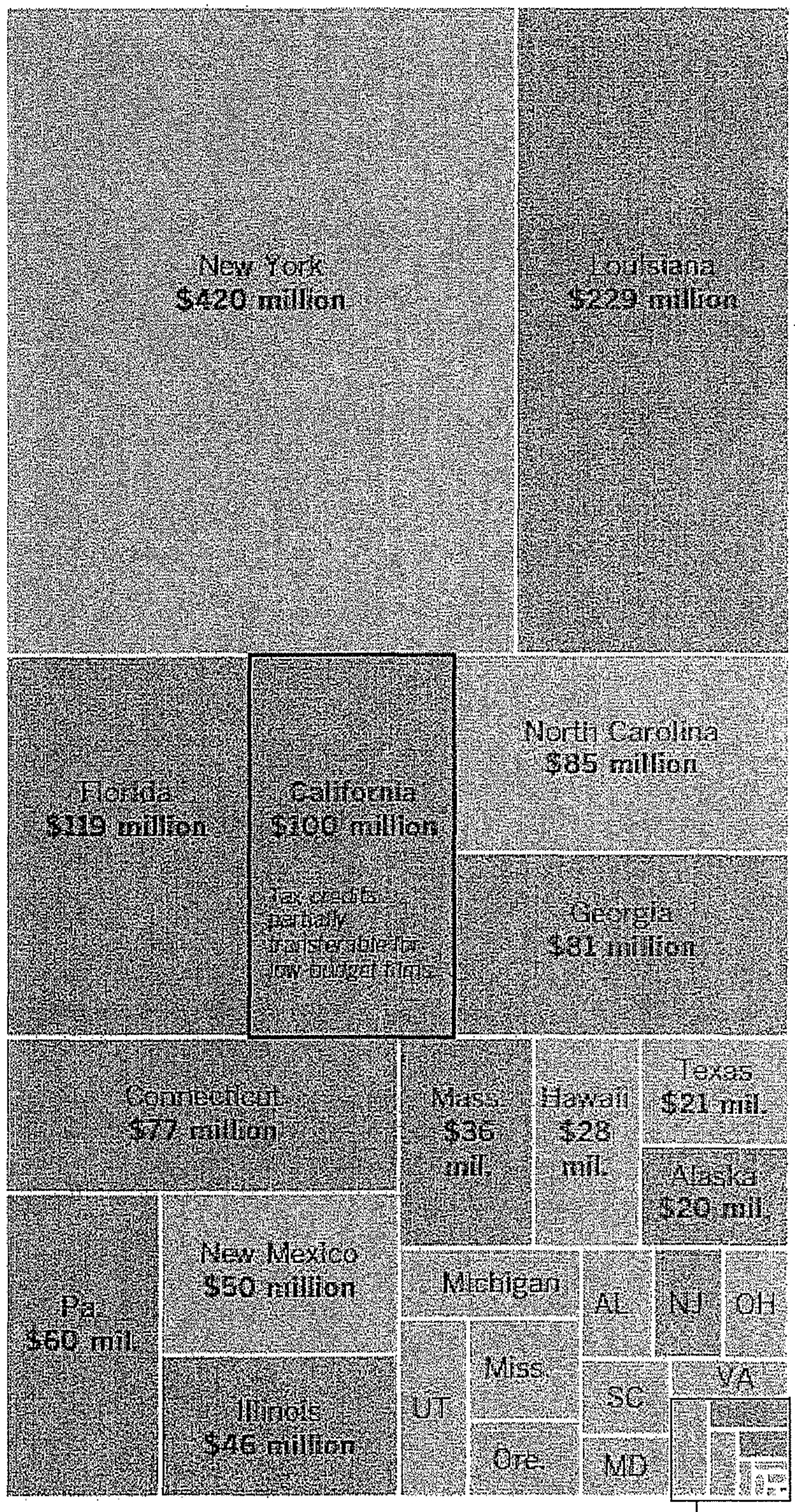
How the states stack up

As more states provide more and bigger incentives, film production has shifted away from California to New York and many other states.

Film incentives doled out in 2012

States approved or handed out $1.5 billion in tax credits and film incentives in 2012, with New York leading the way. Thirteen states allow the sale or transfer of tax credits, which Nevada will also offer starting Jan. 1.

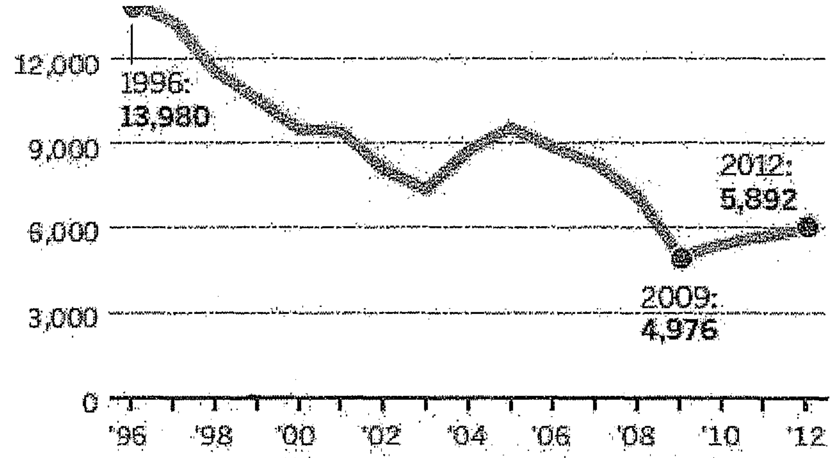
States that allow sale of tax credits



Oklahoma, West Virginia, Washington, Rhode Island, Colorado, Montana, Wisconsin, Kentucky, Wyoming, Missouri, Maine and Minnesota each distributed $5 million or less in incentives. West Virgina, Rhode Island and Missouri offer transferable credits.

Hollywood's decline in film production

Local permitted production days for feature films peaked in 1996. The local production economy has slowly started to rebound since 2009.



Note: Methodology for the counting of production days changed in 2008, but the earlier numbers are still used for comparison purposes.

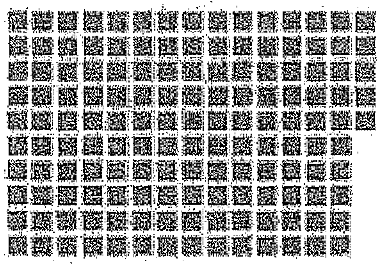
Sources: Entertainment Partners, state film commissions, FilmLA Inc. and Times research. Graphics reporting by RICHARD VERRIER, SCOTT WILSON and THOMAS SUH LAUDER

How Hollywood sells tax credits

As more states allow the sale of film tax credits, studios and producers turn to brokers to find buyers, who can cut their state tax bills as much as 15%. Here's an example of how the process works:

Tax credits: $14.5 million

The state of Pennsylvania awards Paramount $14.5 million in tax credits, or up to 30% of the qualified spending made during the filming of 2012's "Jack Reacher."



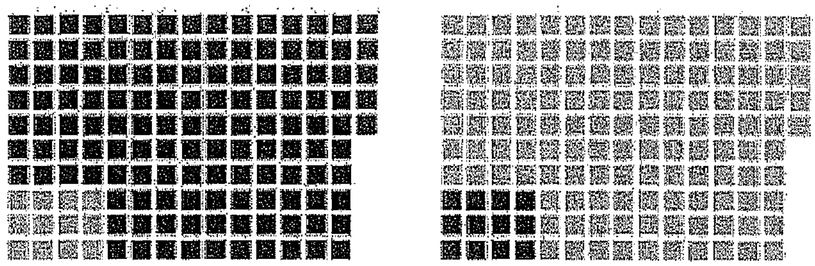
Each square represents $100,000

The broker:

Since the studio has little tax liability in Pennsylvania, it turns to a broker, GEPF, to sell the tax credits.

GEPF

The broker typically makes a 1% to 3% commission on the sale.



Payment to studio (before fees): $13.3 million

GEPF makes a deal with Apple Inc., which buys the credits for about 92 cents on the dollar, paying $13.3 million for all the credits.

Apple's tax savings: $1.2 million

By applying the full value of the tax credits to the state of Pennsylvania, Apple is able to shave $1.2 million from its own tax bill.

Sources: State of Pennsylvania, Times Research. Graphics reporting by RICHARD VERRIER and SCOTT WILSON

ATLANTA — Ric Reitz makes movies. He helped bankroll the Matt Damon thriller "Contagion," Clint Eastwood's "Trouble With the Curve" and the Robert Downey comedy "Due Date."

Reitz, an energetic 58-year-old, doesn't hang out at the Polo Lounge, red-carpet premieres or swank offices in Century City. Instead, he works out of a former cotton mill near Martin Luther King Jr.'s boyhood home, hustling for business at Chamber of Commerce dinners and Rotary Club lunches. Recently, he was looking forward to attending a meeting of prosperous chicken farmers.

Reitz is one of Hollywood's new financiers. Just about every major movie filmed on location gets a tax incentive, and Reitz is part of an expanding web of brokers, tax attorneys, financial planners and consultants who help filmmakers exploit the patchwork of state programs to attract film and TV production.

In his case, he takes the tax credits given to Hollywood studios for location filming and sells them to wealthy Georgians looking to shave their tax bills — doctors, pro athletes, seafood suppliers, beer distributors and the like.

"I've got a giant state of people who are potential buyers," he said. "It's the funniest people who are hiding under stones."

The trade benefits both sides. The studios get their money more quickly than if they had to wait for a tax refund from the state, and the buyers get a certificate that enables them to cut their state tax bills as much15%.

About $1.5 billion in film-related tax breaks, rebates and grants were paid out or approved by nearly 40 states last year, according to Times research. That's up from $2 million a decade ago, when just five states offered incentives, according to the nonprofit Tax Foundation.

Film tax credits have become so integral to the film-making process that they often determine not only where but if a movie gets made.

Studios factor them into film budgets, and producers use the promise of credits to secure bank loans or private investment capital to hire crews and build sets.

"You just follow the money," said Ben Affleck, the actor-director who said he would shoot part of his upcoming film "Live by Night" in Georgia. "What happens is that you're faced with a situation of shooting somewhere you want to shoot, versus shooting somewhere you'd less rather shoot — and you get an extra three weeks of filming. It comes down to the fact that you have X amount of money to make your movie in a business where the margins are really thin."

The credits and incentives can cover nearly one-third of production costs. In 14 states, there is an added benefit: They can be sold, typically enabling the filmmakers to get their money months sooner than if they had to wait for refunds. States that permit the sale of tax credits, including Georgia and Louisiana, are now among the most popular for location shooting.

Greasing the skids

Tax credit brokers like Reitz, although little-known outside the industry, play a key role in greasing the skids of location shooting. Reitz and his partner sold $1 million in credits in 2009, their first year in business. Their company, Georgia Entertainment Credits, did $15 million last year, and they expect to hit $30 million in 2014.

Most referrals come from entertainment industry attorney Stephen Weizenecker, whose clients include Via-com Inc. and Comcast Corp.

"He has been a great advocate for the industry," Weizenecker said of Reitz. "He gets buyers in the door."

Not everyone is such a fan. Hollywood's trade workers — the electricians, carpenters, caterers and others who work behind the scenes

— have long complained that they've lost their livelihood as states vie for film business with ever-richer incentives. The number of top-grossing films shot in California has plummeted 60% in the last15 years, according to a Times review of public records, industry reports and box-office tracking data.

Some economists question whether these programs create long-term benefits to the local communities they are supposed to help. The sale of tax credits, meanwhile, has triggered criticism that companies and people with no connection to the film industry are benefiting from film credits.

Selling tax credits is "a particularly bad public policy because they allow purchasing corporations to shelter income from something unrelated to their activities," said Lenny Goldberg, executive director of the California Tax Reform Assn.

Most states won't say who is buying and selling tax credits, considering it to be confidential.

Illinois and Pennsylvania are exceptions, and disclosed complete lists of buyers and sellers in response to public records requests from The Times.

In Illinois, location tax credit buyers included retailers Kohl's and Macy's, ketchup maker H.J. Heinz and Bank of America. About $40 million in credits were sold last year from producers and studios including Fox and NBCUniversal.

"There's value in these programs in that some film companies, particularly smaller ones, may qualify for a tax credit but may not be able to use it," said Nicole Garrison-Sprenger of U.S. Bank, which last year bought more than $11million in Illinois state tax credits. "Rather than let those dollars go to waste, they sell the tax credit to a third-party purchaser such as U.S. Bank. As a result, the film company has the financing that they might not otherwise have for their production."

In Pennsylvania, energy company Exelon Corp. helped underwrite the Jason Statham thriller "Safe" by buying a $4.3-million tax credit (for the discounted price of $3.7 million). Other recent buyers in Pennsylvania included Apple Inc. and Richard Mellon Scaife, heir to the vast Mellon banking fortune. Scaife bought a $1-million tax credit for the Denzel Washington film "Unstoppable" for $900,000, cutting his taxes by $100,000, records show.

'Promised Land'

Pennsylvania's maximum 30% tax credit was a chief draw for producers of the 2012 drama "Promised Land." The film's creative team — producer Chris Moore, director Gus Van Sant and actor-producer Matt Damon — chose the state in part because it allowed them to sell a 30% tax credit.

Moore said he spent six weeks in meetings at his Los Angeles office and Universal Studios' Focus Features unit, where accountants laid out competing offers from New York, Massachusetts, Georgia, Oregon and Pennsylvania.

"It's like the wild, wild West with so many people promising you money," said Moore, who also produced "Good Will Hunting" and "The Adjustment Bureau." "If you have a $100-million Brad Pitt movie, you just call 15 different film offices, and you're going to have the governor calling you at home saying, 'Hey, man, here's why you should do it in Iowa.' "

Georgia was appealing because its credit covered actors' salaries, but the "look" wasn't right for the story. The filmmakers considered Oregon, but the state's 20% cash rebate wasn't competitive.

New York had a stronger credit, but skilled workers were not available upstate, where the producers wanted to film. That would mean importing a crew and paying their housing and transportation costs.

Ultimately, Moore and his partners chose a town near Pittsburgh. They could hire local crews and get $3.3 million in state tax credits. The credits were transferred in May to Comcast, owner of Focus Features.

Companies and wealthy individuals typically learn about the credits from their tax attorneys, accountants or financial advisors.

Along with cutting taxes, buyers say it's also a chance to promote economic growth in their own states.

Bryan Marshall, who owns an industrial equipment distribution company in Lawrenceville, Ga., said he saved $18,000 in taxes by buying a $150,000 Georgia film tax credit.

"It was a no-brainer in my situation," Marshall said, adding: "It's been great for Georgia to get some of that California money."

Reitz and partner Wilbur Fitzgerald began selling tax credits shortly after Georgia sweetened its tax incentives in 2008.

The men got to know each other working as character actors on TV shows filmed in Georgia, including "In the Heat of the Night." They saw their livelihood threatened by other states offering richer deals to Hollywood and joined a coalition of state film industry advocates campaigning for more attractive incentives.

The expertise they gained researching incentive programs turned into a business.

"We'd get phone calls from practically every studio in America asking us about the tax plan and how it would work," Reitz recalled. "We said:

'Maybe we should become consultants and get paid for this.' "

State tax incentive programs vary, but most are structured knowing that film and TV companies based in California or New York don't have significant tax liabilities in other states. So they either pay a rebate after production is wrapped or allow the credits to be sold.

In Georgia, the tax credit is up to 30% of the money spent on production in the state (20% plus a 10% bonus for promoting the state). That includes not just location filming costs, but money spent on salaries for actors and crews and any costs for building sets. On a movie with a $100-million production budget, the state tax credit could be up to $30 million.

Georgia doesn't pay a rebate, so if studios don't have a tax liability there they must sell the state tax credit to gets its benefit. That reduces the value of the credit to the studio, because it must give a slice of the credit to the buyer and pay a commission to brokers like Reitz. So in the case of a $30-million credit, a studio that decides to sell it would net about $26 million, after broker fees and other costs.

'It's an easy sell'

Spending an afternoon with Reitz in his Atlanta office gives an insight into how the process works.

On this day, Reitz was working to sell off a $147,000 chunk of a multimillion-dollar tax credit Viacom was getting for filming a variety of movies and TV shows in Georgia. Viacom owns the BET, MTV and Nickelodeon cable channels as well as Paramount Pictures, which shot the movies "Footloose" and "Flight" in Georgia.

He had jotted down a list of half a dozen potential buyers on a yellow notepad, including an NFL player, a Middle Eastern investor, a Florida-based retailer and an oncologist, who had been referred to him by an accountant friend.

Reitz, wearing bluejeans and resting on a leather sofa next to an antique movie light, called the doctor first.

"Let me tell you what you're going to save," Reitz said, pausing to punch some numbers into his laptop. "I can get you 88 cents on the dollar," he said moments later. "We can knock this down by $11,000."

The oncologist didn't take long to give his answer. He agreed to wire Reitz $81,699. In return, the doctor will get a tax credit voucher with a face value of $92,840, which he can apply toward his 2013 Georgia state income tax bill.

Reitz, meanwhile, will earn a commission of 2%, or $1,857, for his short phone call with the oncologist. As is often the case, he'll split the commission with another broker who worked on the deal. After the commission and other fees, Viacom will end up with $79,842 from the transaction.

"In the early days, people were very skeptical," said Fitzgerald, Reitz's partner. "Now it's an easy sell."

Big deals can be lucrative. The going rate for, say, a $20-million credit would be $17.6 million before fees. Reitz and Fitzgerald would pocket a $200,000 commission, or 1% of the credit amount, and probably share some of that with others who worked on the deal.

Such large paydays are rare, however. A few minutes after his call with the doctor, Reitz got an urgent email from Weizenecker, the entertainment industry attorney. Viacom and TV One, a cable network co-owned by Com-cast, had sold off more than $6 million in film tax credits to various investors but had $325,000 remaining. Did he have any buyers?

Reitz scanned his list of buyers and quickly called Weizenecker.

"I can commit them to a contract by tomorrow," said Reitz, whose authoritative voice has led to his being cast as TV judges, policemen and lawyers. "If you can scare up another $400,000 to $500,000 from Viacom, I can sell that just as quickly."

Consultants' boon

Although tax credits have been blamed for loss of production in California, they have been a boon for Hollywood's financial consultants.

Burbank-based Entertainment Partners, a big payroll-services provider, says it has handled the transfer of more than $200 million in tax credits for 100-plus projects since 2011. Most of the buyers are Fortune100 companies.

Entertainment Partners has doubled to more than 800 employees in the last eight years, opening offices in Georgia, Louisiana, North Carolina, Utah and Alabama. Most of the employees work in Burbank, where a team of 18 workers advises companies on how to apply for, sell or monetize their credits. The company employed just one person to do that in 2006.

"We get 2,000 to 3,000 phone calls a year from clients," said Senior Vice President Joe Chianese, who launched the tax credit department.

The team draws up budgets and summaries of each state's incentives — eight budgets for a single film is not uncommon — while keeping tabs on any legislative changes that could affect film funding.

Entertainment Partners keeps a list of 25 companies that regularly purchase credits and has three full-time brokers who handle the sales.

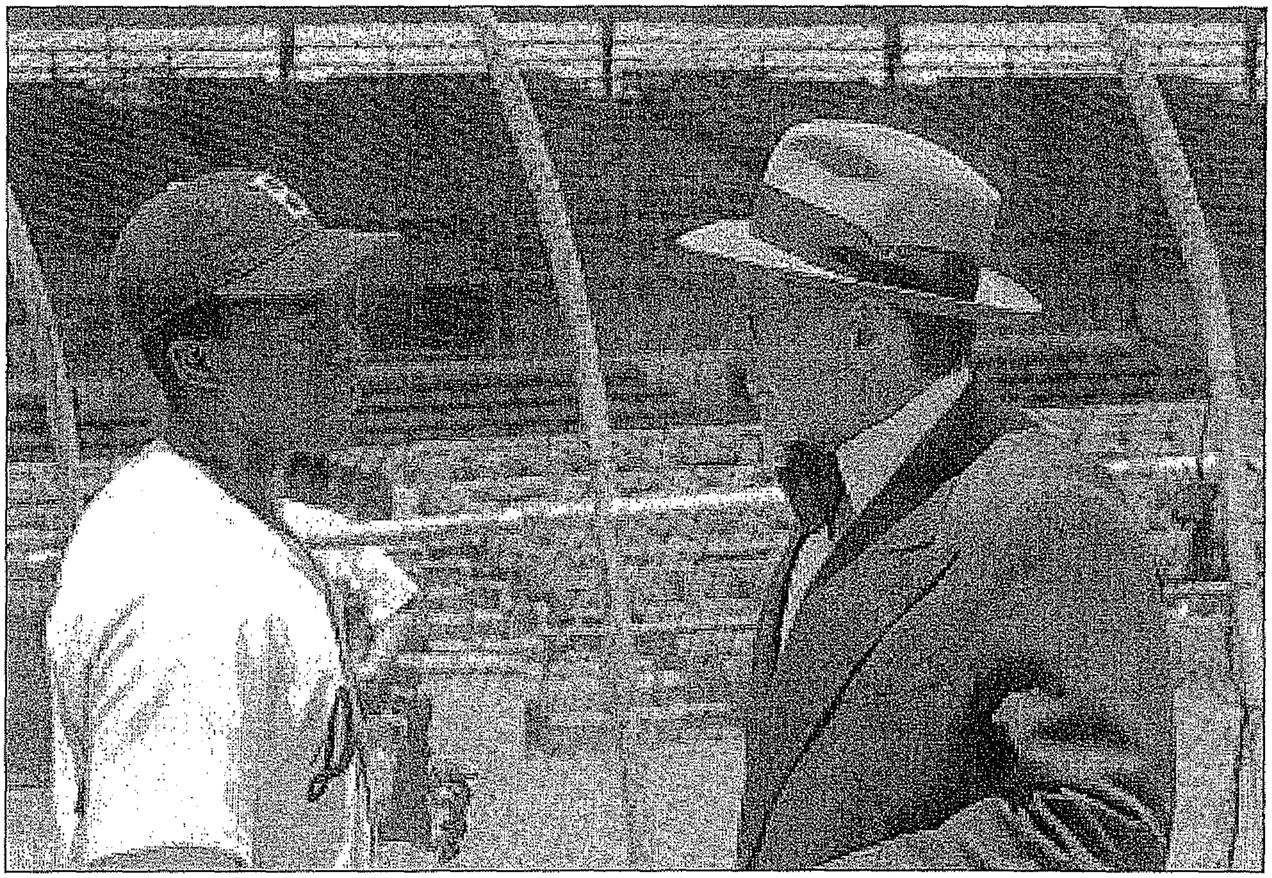
"It's not just a phone call and handshake. There's a lot of work and discussion involved," Chianese said. "It can take weeks, it can take days."

Chianese also makes cold calls to prospective buyers and relies on leads from his staff, many of whom worked for major accounting firms with clients searching for tax breaks.

"Eight or 10 years ago it was, 'I want a beautiful mountain, should I go to Montana or Colorado?'" said Mark Goldstein, chief executive of Entertainment Partners. "Now it's, 'I can recreate anything. Just tell me where the money is.' " richard.verrier@latimes.com Times researcher Scott Wilson contributed to this report.

Film tax credits rip off states

MICHAEL HILTZIK



D. STEVENS Warner Bros. Pictures

CHADWICK BOSEMAN, left, and Harrison Ford star in "42," which was filmed using states' tax credits. Then the score was produced overseas.

The movie "42" arrived in theaters this spring swaddled snugly in the American flag.

Studio marketers declared the film to be "the true story of an American legend." With good reason: It's hard to find a more uplifting sports story than Jackie Robinson's battle against racism on his way to becoming one of the greatest ballplayers in history.

"42" evoked its bygone era by filming extensively in Georgia, Alabama and Tennessee. The filmmakers collected millions in subsidies from those states' taxpayers, who proudly followed the production via local newspaper stories detailing its step-by-step progress from location to location.

And then the producers of this all-American story co-financed by American taxpayers recorded its soundtrack in London.

"It's a classic story of corporate greed," says Paul Frank, a spokesman for the American Federation of Musicians, which represents unionized musicians in the film industry. "Taxpayers are subsidizing the outsourcing of jobs."

The problem of "runaway production" — California's loss of shooting days to other states, largely due to the generous tax credits and other incentives offered elsewhere — is a staple of industry panel discussions.

But there's much less discussion about the impact of filmmakers' incentive-hunting on the business of postproduction, including music recording and digital effects. Many of Hollywood's franchise pictures are scored abroad, including the "Hunger Games," "Iron Man" and "Avengers" features.

Although the American Federation of Musicians' contracts with major studios such as Disney, Fox, Universal and Warner Bros. require that the scores of those studios' productions be recorded in the U.S. at union scale, the contracts generally don't apply to studio subsidiaries or specialty film units such as Fox Searchlight, Universal's Focus Features and Disney's Marvel Entertainment.

Lionsgate, which produces the "Hunger Games" and "Twilight" movies, isn't an AFM signatory, and union officials say their attempts to reach an agreement have been rebuffed. They got the same cold shoulder from Legendary Pictures, the Wall Street-backed studio that brought out "42," when they objected to its plans to record music overseas after pocketing millions in taxpayer handouts. Lionsgate, Marvel and Legendary Pictures all refused to comment.

Hollywood's fretting about runaway production prompted the state Legislature to create a $100-million annual program to pay tax credits of up to 25% of California spending for some smaller-scale feature films and certain TV movies and series; last year the program, which originated in 2009, was extended through 2015.

But the postproduction parts of the business don't get any special help from the state program. Although in-state spending on music and digital effects by eligible productions is subject to the tax incentives, nothing in the rule book requires that these crucial functions be performed in California, or at least in the U.S. That's a change that the American Federation of Musicians thinks should be on the table.

"We've had lots of conversations about how to make postproduction a part of the incentive," said John Acosta, vice president of AFM Local 47, which serves most of Southern California.

The fact that the conversation is still taking place shows how half-baked the California program has been. Producers applying for the credit don't have to show that they would film outside the state without it. Productions are accepted into the program by lottery — first come, first granted.

And obviously no effort has been made to figure out which segments of the film industry are most at risk, and aim the money in their direction.

But those are typical flaws in the deeply flawed concept of film incentives. These tax-financed handouts are a mug's game in which Hollywood has played state legislators nationwide for suckers. More than 30 states pony up more than $1billion a year in subsidies to lure star-laden productions, based on the fantasy that they're creating permanent job growth.

They're wrong. An objective study of Louisiana's pioneering incentive program found that in 2010 the state paid out $7.29 in incentives for every dollar in revenue brought in. "People are getting rich on this deal, and it's not Louisiana taxpayers," concluded the study's sponsor, the Louisiana Budget Project.

California's program, which was enacted as a defensive bulwark against poaching by the other states, doesn't pay its own way either, according to the state Legislative Analyst's Office. That nonpartisan body concluded last year that state and local tax revenue almost certainly came to "well under $1for every tax credit dollar in many years."

That said, there's no question that film musicians need help. About 2,000 California musicians rely on film score work as their main source of income, according to Marc Sazer, head of the recording musicians caucus of Local 47. For a feature film they'll earn roughly $550 to $640 for a typical recording day comprising two sessions of three hours each. Producers pay an additional10.9% into the musicians' pension fund and $48.54 per day for health insurance.

Although Los Angeles is still the world center of recorded film scores, it's lost ground to European locations, especially London. From 2000 to 2010, the number of the100 top-grossing features with L.A.-recorded scores each year fell from 68 to 55, while London's share rose from19 to 27.

Big money is hidden within those statistics: The "Twilight," "Hunger Games" and "Avengers" franchises alone account for tens of millions of dollars in wages, Sazer estimates, as well as foregone contributions to retirement and health benefits.

The trend toward recording offshore may not be due strictly to wage scales, which the AFM says are roughly comparable in L.A. and London. One difference is in residual payments for such secondary markets as home video and broadcast and cable TV showings. Under the U.S. contract the musicians divvy up1% of the producers' gross license fees; in London, their share is nothing.

It's been suggested that the AFM could bring more recording home by giving up its residuals. "L.A. has to become competitive or in10 to15 years there will be no industry here," argues Richard Kraft, an agent for film composers (who aren't covered by the union).

Responds Dennis Dreith, a composer who oversees the AFM fund that collects residuals for the musicians: "Giving that up would be devastating in many ways." Musicians on a successful picture could still receive income into their retirement years; Dreith says some are still collecting for "E.T. the Extra-Terrestrial," released in1982.

As long as states compete with one another to hand over millions to movie moguls while cutting essential services for their own citizens, film incentives will continue to foster a race to the bottom.

California could be different, if it only aimed its fire where it's needed. As Dreith told me, "We shouldn't be allowing people to use our tax incentives to employ foreign workers."

Michael Hiltzik's column appears Sundays and Wednesdays. Reach him at mhiltzik@latimes.com, read past columns at latimes.com/hiltzik, check out facebook.com/hiltzik and follow @hiltzikm on Twitter.