REPORT REGARDING THE ECONOMIC IMPACT OF

THE ESTIMATED PRODUCTION TAX CREDIT PURSUANT TO SECTION 235-17(i) (4)

A. INTRODUCTION:

Act 89, SLH 2013, Section 2, amended Chapter 235-17 by increasing the production tax credit to twenty percent of the qualified production costs incurred by a qualified production in any county of the State with a population of over seven hundred thousand and twenty five percent of the qualified production costs incurred by a qualified production in any county of the State with a population of seven hundred thousand or less. Act 143, SLH 2017, amended Chapter 235-17 to include a $35 million overall funding ceiling which is insufficient to serve the current number of filing entities and the total aggregate of qualified expenditures.

B. 2017 RESULTS FOR QUALIFIED PRODUCTION SPEND §235-17 HRS:

From January 1, 2017 through December 31, 2017, the Hawaii Film Office (HFO) processed registrations for 48 qualified productions that applied for the Motion Picture, Digital Media and Film Production Income Tax Credit with an estimated total of **$268,596,154**, in production expenditures and an estimated total of **$55,350,562** in tax credit claims for the calendar year. This direct spend resulted in an estimated **$29,008,385** in tax revenue generated, **$464,671,346** in sales or economic activity generated, and a key figure: **$107,438,462** in Hawaii household income generated as a result of the qualified production expenditures.

Please note that these total amounts are estimates based on the respective Hawaii Production Registration applications, not the Hawaii Production Reports (HPRs) which are submitted 90 days after the close of the production's tax filing year (filers represent a mix of calendar and varying fiscal years, so not all reports are received at the same time). Given the due date of the legislative report, the Hawaii Film Office is providing all estimated data for Calendar Year 2017, which is the data available now, until all Hawaii HPRs have been received and vetted by the Film Office.

Once all production reports are received, vetted and certifications issued, for any given year, the Film Office will provide to the Legislature a revised 2017 Actual Annual Report covering the actual reconciled expenditures for the prior year.

The documents attached reflect the estimated CY2017 data, the actual reconciled CY2016 data, along with a copy of the CY2016 estimated data which was submitted previously.

C. OVERALL PRODUCTION SPEND CY2017

In addition to the qualified production estimates for CY17, when we combine all non-qualified production expenditures, it provides a total estimated spend of **$320,000,000** for CY17; a significant boost and the largest production year in Hawaii's history since 2010. In consultation with DBEDT's Research and Economic Analysis Division (READ), it is estimated that $320M generated **$553,600,000** in sales generated/economic activity, **$34,560,000** in tax revenues, and **$128,000,000** in Hawaii household income. These are aggregate figures based on the total spend. Program will be changing reporting to reflect a more detailed breakdown by type of expenditure and applying the industry multipliers to each in order to provide a more granular set of metrics which address the percentage of leakage for out of state salaried or day player workers.

D. 2016 RESULTS for §235-17 HRS:

CY2016 totals in the attached matrix were taken from Certification Letters issued by the Hawaii Film Office and the correlating Hawaii Production Reports. The Certification Letters are the documents which filers submit to Department of Taxation (DoTAX) along with their Corporate Income Tax Forms and Tax Credit Forms for review by DoTAX and issuance of final refunds.

Based on the data from the Hawaii Production Reports, the actual figures for CY2016 show that 35 qualified productions spent a total o**f $199,004,828** in qualified expenditures and are in the process of receiving **$43,827,784** in tax credits from the State of Hawaii. Again, in consultation with READ, $199M in actual qualified expenditures for CY2016 translates to **$344,278,352** in sales generated/economic activity, **$21,492,521** in tax revenues, and **$79,601,931** in Hawaii household income.

As demonstrated in actual figures for 2013-2015, each year several productions withdraw their applications for various reasons. Therefore, the actual qualified expenditures for CY2017 and corresponding certified tax credits are likely to decrease. It is important to note that despite any withdrawals, the final actual tax credit amounts will still be significantly higher than the anticipated $35 million spending ceiling which will take effect January 1, 2019 (see section H for further detail).

E. INCREASED WORKFORCE DEVELOPMENT:

As part of the Temporary Hawaii Administrative Rules issued by the Department of Taxation on Oct. 20, 2016, the required education or workforce development contribution that

is mandated in §235-17 HRS, was significantly increased. This was done to better support the film and media arts programs in Hawaii's public and charter schools. The contribution level must now be 0.1% of a qualified spend in Hawaii or $1,000, whichever is greater. (NOTE: These contributions are determined once the Hawaii Production Report (HPR) is received, 30 days after the filing entity's tax year. For 2017, the results of workforce development contributions will be provided as part of the 2018 report to the Legislature in January 2019).

For example, a feature film or television series that spends $50 million - $60 million in Hawaii is required to make an education/workforce development contribution of $50,000-$60,000 to Hawaii's public and charter schools and universities, significantly increasing a critical funding and/or in-kind resources for our creative, media and film education programs. Contributions combine cash and in-kind including internships, professional training workshops and donation of equipment.

Working with the Department of Taxation, this section of the Administrative Temporary Rules is providing a more substantial baseline to grow our pool of film industry professionals through cash investments, workshops or seminars which augment their current coursework, providing professional, real world experience/training to grow our base of film industry professionals.

F. <u>WORKFORCE DEVELOPMENT CONTRIBUTIONS CY2017:</u>

In calendar year 2017, Hawaii public and charter schools throughout the state will be the direct beneficiaries of the education and workforce development program that is a mandate for productions to access the tax credit. These educational institutions will receive both cash and in-kind contributions that are dedicated to supporting that school's film/video and digital media programs. The data of contributions for CY2016 are still being compiled and verified. The Film Office will provide an updated tally and matrix of contributions for CY2016 in early FY19.

Since the start of the tax credit program in 2006, hundreds of Hawaii public and charter school students have participated in meaningful internships with major film, television and commercial productions. Many of the productions applying for the tax credit have presented workshops, educational seminars and mentoring opportunities which included Hollywood creative professionals and industry leaders providing students in college-level film programs access to major producers, directors, writers, and actors, advancing professional development in the creative sectors. For example, one of the major studios plans this year to sponsor a much-needed Locations Management Seminar for Hawaii's up and coming location scouts and location managers. Film and Digital Media students from the University of Hawaii's Academy

for Creative Media and Hawaii's public high schools that have dedicated film and digital media programs will be invited to attend this seminar.

G. ADMINISTRATION OF CREDIT:

The Hawaii Film Office presently has an Economic Development Specialist VI and Film Office Manager as the two regular full-time employees, working 60% and 25% respectively, on the Act 143 tax credit program. To manage the overall workload of the Film Office, both positions work on the tax credit program part-time, as the other statutory duties of film permit processing and production support comprise the balance of their time. The employees also work part-time on production crisis management, film permits and logistical support, and, together with support of READ and CID, provide analysis of this tax credit to the Legislature and industry. The program and department recommended in response to the Hawaii State Auditor, that a full-time unit of two new employees with accounting and data management skills be added to the division's budget to be on par with other states who manage this level of tax credit program.

Currently, there are no non-state, part-time employees, or contract personnel involved in the management of the motion picture, digital media and film production income tax credit.

H. UPDATES - ACT 143 SLH 2017:

The Motion Picture, Digital Media and Film production tax credit is performing as the Legislature intended: Stimulating the economy and creating high paying jobs for Hawaii residents to serve a clean industry that preserves Hawaii's natural and cultural resources and provides valuable marketing exposure for our Islands as a world-class filming and visitor destination.

The Legislature, recognizing the tremendous economic value of a thriving film industry to the state, agreed last session to grant an extension to the tax credit program to January 1, 2026. This stability is critical for studios and television networks in their production planning, especially with television series – Hawaii's core economic driver in this sector.

Of concern however, is the first-time imposition of a funding ceiling, which under Act 143 SLH 2017 is limited to the state providing $35 million in tax credit funding annually, effective January 1, 2019.

With this new element, Hawaii runs the real risk of losing business and jobs which will go to other jurisdictions that do have not funding ceilings in place. The best example of this is what happened in 2015 when Louisiana imposed a $180 million funding ceiling for this state's

booming film industry. As a result, new film business in Louisiana dropped by nearly 80 percent. Louisiana's loss was Georgia's gain. With no sunset date and no funding ceiling on its tax credit program, Georgia has become the country's top filming destination after New York and Los Angeles.

Also with the funding ceiling requirement in statute, the new unit of accounting skilled staff becomes even more critical. While there is a provision for a pre-review by a tax professional for productions $1 million and over, the imposition of the funding ceiling requires new procedures, data gathering/reporting as well as the up to date tracking of fund depletion, and tracking the carry over impact to following year. Included in this new element of the tax credit, is the critical timing of notification to projects, producers, studios, and networks when the ceiling has been reached. It's important to note that even with the carry forward option included in the statute, this will still require the film office staff to ensure the accuracy of depletion of funds in the following year's allowance, should productions opt to carry forward the credits two years out, vs. one year. This further limits the number of productions we can host, may impact the local production market adversely and reduces the jobs and economic impact these productions generate, while reducing funds available to apply to current and future productions seeking the tax credit.

Hawaii's film industry is an anchor of our state's growing Creative Economy. A spending ceiling will likely negatively impact business attraction as well as the operations in the Hawaii Film Office.

If jurisdictions such as Louisiana, Michigan and other states are any indication, it is anticipated that the state could see a decrease in production activity beginning in 2019 through all the out years. With reduction of jobs, we increase unemployment; with less production activity, planning for future infrastructure for creative media/film and television also may not go forward due to the limiting of the production landscape in the state.