# STATEMENT TO THE COMMITTEE ON ECONOMIC DEVELOPMENT, AGRICULTURE AND PLANNING ON BILL NO. 31-0009

February 23, 2015

Madame Chairwoman, Senators, fellow Testifiers and those present in chambers and listening and viewing audience:

My name is Erika Kellerhals. Thank you for allowing me and my colleague, David Bornn, the opportunity to be here with you today to talk about Bill No. 31-0009. During my testimony, which echoes that testimony which I gave last year in August 2014, I will focus mostly on the technical side of the incentives, but I did want to spend a brief moment on the importance of tax incentives for film, television and music production activities as well as measuring the economic

The use of tax incentives and credits for film and television production is a relatively recent phenomenon as the number of states offering film production incentives grew from just a handful in the early 2000s to a majority of states by 2010. Currently thirty-nine states and Puerto Rico have film production incentives on their books for 2014. Beginning January 1, 2014, Nevada's new transferrable tax credit became available for productions that shoot at least 60 percent in-state and spend a minimum of $500,000. Over half of states with incentive programs require a production to spend a minimum amount on goods and services in the state.

I personally have been researching and studying state incentive regimes for over 8 years. What we have attempted to do with this legislation is cull the most feasible components of incentive legislations from the most successful state programs and crafted a statute that works well with our "mirror Code". In doing so we have created a program with three separate components, a transferable tax credit, a straight rebate and a reduction in taxes where appropriate. I will briefly walk you through each component and will then be available to take any questions you might have.

I will address the simplest component of the statute first, namely the hotel tax reduction. As you know, Title 33, section 54 imposes a hotel tax at a rate of ten (10%) percent. The legislation would reduce the hotel tax on a sliding scale from 8% to 1.5% dependent upon the production expenditure and the total room nights booked in the territory. It is anticipated that through regulations, the mechanism for a direct reduction in the applicable hotel tax rate would be applied by the hotel. This does not create an additional outlay of funds for the Government.

The second component is an income tax credit equal to an amount up to 17% of the total compensation paid to residents of the territory. The applicable credit percentage is dependent upon the percentage of territory residents employed on the project. Due to the fact that the production companies who will be filming in the territory will not necessarily have an income tax obligation to the territory, the determination was made to allow the credits to be transferrable. By transferrable, we mean that the credit amount can be sold to a third party that does in fact have an income tax obligation to the territory. For the production company, if the value of a company's credits is higher than its tax liability, it can sell the excess credits to another taxpayer who owes the territory taxes. For the buyers to benefit from the transaction, the tax credits have to be sold for less than their full value. Prices vary, but tax credit brokers say that it's typical for sellers to get 85 or 90 cents on the dollar. The buyer is then able to utilize the credit on its own tax return to reduce its own outlay for taxes.

The third component of the legislation is an actual rebate which would be paid utilizing funds from the Department of Tourism Advertising Revolving Fund. The available rebate to each production is up to 9% of qualified production expenditures. "Qualified production expenditures" means preproduction (including scouting activities), production, and postproduction expenditures incurred in this Territory that are directly used in a qualified production activity. Upon submission of substantiation of qualified production expenditures, a production company is entitled to a cash rebate of up to 9% of the expenditures.

Additionally, the statute has mechanisms intended to increase activity in St. Croix. In particular, the statute increases the qualified production expenditures rebate by an additional 10% if the qualified production activities are undertaken on the island of St. Croix.

The hotel tax reduction, income tax credit and expenditure rebate are all targeted to increase amounts spent in the territory. These incentives are targeted to create both short and long term economic and fiscal benefits that extend beyond the production activities that qualify for the credit. These benefits include increased tourism, development of film industry infrastructure such as studios and service providers, and attraction of production activities not eligible for the credit.

How does this actually work?

Let's assume Production Company X obtains a business license in the USVI and undertakes filming a portion of a motion picture in the USVI. X submits an application to the EDA and the Film Office. The EDA & Film Office have determined that the production is in fact a "qualified movie production" as it includes credits that denote filming took place in the USVI. In connection with the filming of the movie, it is determined that X will have total qualified production expenditures of $5,000,000 which includes: $4,000,000 in compensation paid and hotel room costs for 251 room nights.

In order to qualify for the benefits available under this statue, X must show the following:

- That it has registered to do business in the USVI and that it has obtained a business license;
- That a minimum of 20% of the employees working on the production are USVI residents;
- That the executive production crew have made themselves available to the EDA to speak to local schools and university students about film production;
- That filming will start within 180 days of issuance of the Certificate.

As noted above, X has spent $5,000,000 in qualified production expenditures. In addition, 25% of the crew working on the movie are USVI residents. X would be eligible for the following incentives:

- Income Tax Credit: $400,000.00 (10% of the $4,000,000 in actual compensation paid).
- Rebate for QPE: $450,000.00 (9% of $5,000,000 in QPE)
- Hotel Tax Waiver: Reduction in hotel tax to 6%.

As the cash rebate is not in excess of $500,000, X would be entitled to receive the entire $450,000.00. X will not have an income tax obligation to the USVI, therefore it is eligible to transfer the income tax credit to a third party, allowing it to recoup some of its costs associated with the production. If X included "Filmed in the USVI" in the credits it would be available for additional 10% rebate of QPE – however, in this circumstance, the maximum that X would be eligible for is $500,000 due to the rebate cap we have built into the statute.

We are happy to take any questions you have on this Bill.

Thank you,

Erika A. Kellerhals