VIRGIN ISLANDS ECONOMIC DEVELOPMENT AUTHORITY'S TESTIMONY IN SUPPORT OF BILL NO. 31-0009 AND RECOMMENDED AMNDMENTS

BEFORE THE

COMMITTEE ON ECONOMIC DEVELOPMENT, AGRICULTURE and PLANNING
31st LEGISLATURE OF THE VIRGIN ISLANDS
ST. THOMAS, U.S. VIRGIN ISLANDS
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Good morning, Chairwoman Millin Young, members of the Committee on Economic Development, Agriculture and Planning, other members of the 31st Legislature present, fellow testifiers, ladies and gentlemen gathered here, and to the viewing and listening audiences. I am Percival Clouden, Chief Executive Officer of the Virgin Islands Economic Development Authority (hereinafter "VIEDA" or "Economic Development Authority"). Here with me today from the VIEDA team are Wayne Biggs, Assistant Chief Executive Officer/Chief Operating Officer; Tracy Lynch Bhola, Legal Counsel; and Margarita Benjamin, Director of Applications. Also here as part of this team is Attorney Stephen Weizenecker, a partner in the Atlanta office of Barnes & Thornburg, who specializes in entertainment-related business and tax incentives. Attorney Weizenecker is here for his insight and expertise in working with production companies and their tax incentives.

The Virgin Islands Economic Development Authority is pleased to be able present testimony on Bill No. 31-0009, an Act repealing and reenacting with amendments title 29 Virgin Islands Code, Chapter 12, subchapter III relating to Sustainable Tourism Through Art-based Revenue Stream Production ("STARS").

For the benefit of the new Committee members, the Economic Development Authority started the process to amend Act No. 7344, the STARS Act, in 2013 after identifying what we believed were conflicting sections, a convoluted and impractical interaction between the Economic Development Authority and the Department of Tourism, and the creation of a new and unfunded division within the Economic Development Authority.

The Economic Development Authority by and through its Economic Development Commission ("EDC") was established to promote the growth, development and diversification of the economy of the U.S. Virgin Islands. In a competitive global market for business growth, tax incentives are offered to attract businesses to the Territory. The certificate of tax incentive benefits granted to a company is a contract with the Territory and in addition to the taxes paid by these entities, they provide opportunities for gainful employment of residents; contribute to numerous charitable organizations; contribute to the educational system; and many other under-reported but highly beneficial contributions to the people of this Territory.

STARS is intended as another element of the economic development package offered by the Virgin Islands to remain competitive in our efforts to attract businesses, provide jobs to our residents, bring revenues to the Territory, showcase the beauty of the Virgin Islands, and promote local talent. To accomplish the goal of revitalizing, expanding and attracting audio and music video recording, motion picture and television industries and related media productions to the Virgin Islands, STARS calls for a collaborative effort between the VIEDA and the Department of Tourism. This can be done, but we must do so with practicality and efficiency as paramount considerations to avoid a bureaucratic nightmare for investors and potential conflicts between government agencies.

We realize that there is often a perception that insofar as STARS and the EDC Program both offer tax incentives, they are equally viable options for most business categories. However, that is not the case. They have different requirements and target different

business categories. With the passage of Act 7651 in October 2014, which amended, among other things, 29 V.I.C. §§ 703(g) and 708(a), there is no category under which music recording is an approved industry for benefits under the EDC Program. Granted, 29 V.I.C. § 708(a)(1) provides that:

> The Commission may approve other such industries or businesses as may be considered appropriate by the Commission and which a finding by the Commission has determined will advance the economic well-being of the Virgin Islands and its people, and the applicant of such industry or business has agreed to the investment and employment requirements along with any other such special conditions as agreed between the applicant and the Commission.

However, the reality is that this provision is not an easy hurdle for most music recording entities to reach, and even more difficult for small "local" music recording companies to meet. The EDC Program does, however, allow for "film and print industry activities" under the designated service business category.

Recognizing that the EDC Program will not, for the most part, provide incentives for audio and music recording, we view the substantive exclusion of audio and music recording from STARS in Bill No. 31-0009, as yet another tax incentive barrier for the audio and music recording industry. We have spoken extensively to the principals of local music recording companies, and look forward to a STARS Act which includes this audio and music recording to the extent it provides for film production.

That said, we support the repeal of Act 30-0417 and applaud this legislative body for putting forth Bill No. 31-0009, which is, without question, a step in the right direction towards laws that make this Territory competitive with other jurisdictions offering production incentives. The Economic Development Authority is certain that our location, the natural beauty of these islands, the United States flag that governs and its

laws to which we are bound, coupled with the production incentives we seek to offer, will make the U.S. Virgin Islands an attractive destination for production companies.

Having established this framework, the Economic Development Authority offers the following points for further consideration as to Bill No. 31-0009:

Section 747a(h) of Bill No. 31-0009 defines a "Production Company" as,

> a company primarily engaged in qualified production activities which have been approved by the Economic Development Commission and the Film Office of the Department of Tourism. The term does not include any form of business owned, affiliated, or controlled, in whole or in part, by any company or person that is in default on any tax obligation of the Territory, or a loan made by the Territory or a loan guaranteed by the Territory.

We recommend that the definition of a "Production Company" should end after the first sentence. The second sentence, which provides that a Production Company "does not include any form of business . . . that is in default on any tax obligation of the Territory, or a loan made by the Territory or a loan guaranteed by the Territory" may be better placed under *Section 747d (Qualification for tax benefits)* as a specific requirement for granting of benefits under the STARS Act.

Section 747a(k)(8) As to subsection (k)(8), I simply note that, to my knowledge, there is currently no bonding company in U.S. Virgin Islands. Therefore, any such bonding will likely be purchased through insurance agencies outside the Territory, and hence, not included as a "Qualified Production Activity" for most production companies.

Bill No. 31-0009 provides that the "[t]otal aggregate payroll; airfare, if purchased through a Virgin Islands based travel agency or travel company; insurance costs and *bonding, if purchased through a Virgin Islands* ***based*** *insurance agency*;

VIEDA proposes that the Section 747a(k)(8) be amended to provide that the "[t]otal aggregate payroll; airfare, if purchased through a Virgin Islands based travel agency or travel company; insurance costs and *bonding, if purchased through an insurance agency* ***licensed*** *in the Virgin Islands;*

Section 747a(m): In subsection (m), I seek confirmation that the intent is to define a "Resident Production Company ***Program***" versus a "Resident Production Company".

Section 747b(a). "Office of ***Film*** Tax Incentives" -- The name suggests a focus on film.

When STARS was initially enacted in 2012, the Economic Development Authority was mandated to have a "Department" which would "assist" the Department of Tourism's "Office of Filmmaking *and Music Recording* Promotion." Then in December 2014, with the passage of Bill No. 30-0417, there was established within the VIEDA an "Office of *Film* Tax Incentives" that in participation with the "*Film* Office" of the Department of Tourism, would be responsible for managing applications for tax incentives under STARS. There is no change in the name of the office between Bill No. 30-0417 and the proposed legislation, Bill No. 31-0009, but I urge this legislative body to move toward a name for the office within VIEDA that is more reflective of film and music. By making this

recommendation, I do not presume to speak for the Department of Tourism as to the name of its office.

Section 747b(b) Mandates that the Assistant Chief Executive Officer of the VIEDA oversee the Office of Film Tax Incentives. I recommend that the best approach would be to designate the Chief Executive Officer of VIEDA as the person with oversight of the Office of Film Tax Incentives. Then, consistent with 29 V.I.C. § 706, which outlines the duties of the Assistant Chief Executive Officer ("ACEO"), the Chief Executive Officer would have the discretion to designate the ACEO to oversee the office and manage applications for STARS tax incentives.

Section 747b(c) creates an unbudgeted "Office of Film Tax Incentives" for which the Economic Development Authority will require an appropriation.

However, as an important component of the Economic Development Authority's mission is tax incentives under the EDC Program, there is no need for a separate division, known as the Office of Film Tax Incentives, within the VIEDA specifically for STARS. What the VIEDA will undoubtedly require to fulfill this mandate is additional personnel.

While the Department of Tourism will be in a better position to comment regarding its ability to pay rebates funded from the Tourism Advertising Revolving Fund (33 V.I.C. § 3072), I caution this body against the inclusion of a rebate offer within this Bill, and I propose that we focus more on tax credits and offsets, and less on rebates.

Section 747c(b)

First, I note that § 747c(b) provides that, "[o]nce a complete application has been received by the Economic Development Authority, the application for Incentives under this subchapter must be forwarded to the Film Office no later than 10 business days after the receipt of the completed application for its review, analysis, *and recommendation **to** the Economic Development Authority.*"

Is this intent of the statute to provide for "recommendation **by** the Economic Development Authority's Office of Film Tax Incentives?"

Second, the proposed Bill provides that, "[t]he Film Office shall have *7 business days* from receipt of the application in which to submit its analysis and recommendation to the Economic Development Authority.

VIEDA proposes that the film office review should be ***5 business days*** instead of 7.

Section 747d. Qualification for tax benefit

- First, this section switches to numbers instead of letters as has consistently been the format throughout the Bill.
- Second, Section 747d(3) introduces the percentage of minimum labor requirement. It has the 20% minimum labor requirement but has a waiver ability, which should be reflected throughout.

Bill No. 31-0009 provides that in order to qualify and remain eligible for tax incentive benefits under this subchapter, an applicant must "[e]mploy residents of the Virgin Islands as defined in section 703(e) of this title such that a minimum of 20% of the total employees working on the

production in the Virgin Islands, including extras, day players, and a maximum of three paid interns who must be residents of the Virgin Islands, UNLESS a documented waiver request is submitted to the Economic Development Authority upon a requisite showing according to regulations promulgated.

Section 747d(4) further provides that in order to qualify and remain eligible for tax incentive benefits under this subchapter, an applicant must, "[i]nclude in the credits of any production the following language "Made or Filmed in the Virgin Islands" or some other designation where the entire production is not completed in the U.S. Virgin Islands, that footage was shot in the territory: "Portions Made in the U.S. Virgin Islands" or in the case of a footage shot in St. Croix "Portions Made or Filmed in St. Croix" and an acknowledgement to the VI Economic Development Authority and the Film Office of the Department of Tourism;

The VIEDA opines that we should include a credit provision, but also recognize that this credit provision can be further defined in rules and regulations. .

Section 747d(5). The proposed legislation generally provides that the executive production crew shall make themselves available to the Economic Development Authority to speak to local school and university students about music/film/entertainment topics pertinent to the film or video industry, where practicable.

It would perhaps be more feasible to require that "*one or more of the executive production crew be available*" to accommodate the work schedules and practical realities of production, and also to include *music* as a pertinent industry topic.

Section 747d(7). Bill No. 31-0009 provides that the Economic Development Authority shall prescribe regulations, including a procedure for review of that department's denial or revocation of Territory certification, necessary to carry out the provisions of this section.

1) The Film Office within the Department of Tourism should have similar regulations, with a procedure for its review of an application consistent with the requirements of the proposed *Section 747c(b)*.

2) Use of the language, "denial or revocation of *Territory certification*," is unclear, and this team proposes that the legislation simply read, "denial or revocation of certification . . . ."

Section 747d(8). "The Qualified production must begin within 180 days of issuance of the Certificate; and the certificate shall expire 180 days after issuance, *unless an extension is granted*."

The law should specify which film office shall grant the extension. It stands to reason that it would be the Office of Film Tax Incentives, but it is necessary for clarity where, as here, there will be a film office in VIEDA and one in Tourism.

Section 747d(9). "Each applicant shall pay an Application Fee as set in the regulations to this chapter."

First, "Application Fee" is capitalized, but not defined. We recommend that this legislation either include language similar to 29 V.I.C. § 708a, which establishes fees for application and compliance within the Economic Development Commission Program, or empower the Economic

Development Authority to establish and assess application and other pertinent fees.

Second, there is an Economic Development Authority audit component to STARS under § 747g(b) and (c), which states in subsection (b) that the "Economic Development Authority shall promulgate such regulations as are necessary to administer this section" and in subsection (c) that "Each qualifying Production Company granted a certificate is subject to an audit on completion of the qualified project to ensure that the Qualified Production Company has met the terms of its application and certificate."

We recommend language that which clearly states in subsection (c) which government office will be responsible for the audit, and further empowers the responsible office to assess fees and fines, as appropriate.

Third, will there be a specific fund into which application fees and compliance fines shall be deposited once collected?

Sections 747e(a)(2)(A), (B) and (C). In these subsections, we propose eliminating all of the different forms of the production incentive and streamlining the process. It should simply state, if you are a Qualified Production Company that you are entitled to a tax incentive equal to 25% of your total Qualified Spend. The tax incentive should go against income tax and payroll tax.

In the alternative, after taking into consideration the available workforce in the Territory, we recommend that the proposed legislation provide as follows:

The percentage of available tax credit in paragraph (1) is determined in accordance with the following subject to a waiver as described in promulgated hereunder:

(A) Where ***up to 10%*** of the total workforce, including paid interns, of the production company employed in the Territory are Virgin Islands residents, the allowable percentage is ***15%***;

(B) Where ***10.1 to 15%*** of the total workforce, including paid interns, of the production company employed in the Territory are Virgin Islands residents, the allowable percentage is **20 %**; and

(C) Where ***15.1% or greater*** of the total workforce, including paid interns, of the production company employed in the territory are Virgin Islands residents, the allowable percentage is ***25%***.

Section 747e(a)(3). This section provides that "[a] production company that has submitted an application for incentives is allowed a cash rebate for qualified production expenditures made in connection with a Territory Certified Production. The rebate allowed under this section is equal up to 9% of the total Qualified Expenditures incurred in connection with the Territory Certified Production during the tax year up to a maximum of $500,000."

First, I propose the deletion of the word "equal" in the second sentence of Section 747e(a)(3). The sentence will now begin, "The rebate allowed under this section is up to 9% of the total Qualified Expenditures . . . ."

Second, this section provides a rebate of up to $500,000 *for any production.* However, if we are in fact going to provide this rebate, we should consider offering it specifically for "resident" productions, and define those terms.

Section 747e(a)(4) of Bill No. 31-0009 provides that "[t]he production company and its affiliates are allowed an additional cash rebate equal to 10 percent of the total qualified production expenditures if the qualified production activities include a Qualified Virgin Islands Promotion."

VIEDA proposes deleting the phrase "and its affiliates," and also proposes making this subsection an addition to the percentage tax incentive delineated in subsection 747e(a)(2) above, which would amend subsection 747e(a)(4) to state as follows:

"The production company is allowed an additional tax credit equal to five percent of the total qualified production expenditures if the qualified production activities include a Qualified Virgin Islands Promotion."

Section 747e(a)(5). Again, we recommend the deletion of the words "and its affiliates," which would amend subsection 5 to state as follows:

"The production company is allowed an additional tax credit equal to 4 percent of the total Qualified Production Expenditures if the Qualified Production Activities are undertaken on the island of St. Croix."

Section 747e(a)(6). As it pertains to the Hotel Tax Waiver, I note that while hotel stays will be necessary and certainly encouraged, the reality is

that companies tend to rent homes, villas, condos and the like for longer term stays.

Section 747g(a)(1)(c). "Each qualifying Production Company granted a certificate is subject to an audit on completion of the qualified project to ensure that the Qualified Production Company has met the terms of its application and certificate."

For consistency and accuracy, we recommend the deletion of the term, "*qualifying Production Company" and replacing it with the term, "Territory Certified Production".*

The amended section would now provide that, "Each Territory Certified Production Company is subject to an audit on completion of the qualified project to ensure that the Qualified Production Company has met the terms of its application and certificate."

In conclusion, Bill No. 31-0009 focuses primarily on film and video recording industries, establishes another division within the Virgin Islands Economic Development Authority, "the Office of Film Tax Incentives." However, as stated earlier, there is no need for a separate division.

In the proposed dual review process, it would be beneficial to know the criteria and focus of the review to be performed by the Department of Tourism's Film Office. Understanding that the Department of Tourism is in the business of promoting this Territory and a significant portion of the VIEDA's mission is to administer tax incentives, I can assure this body that the VIEDA will work closely with Tourism to ensure that we avoid any duplication of efforts in light of the extensive review currently undertaken by the Economic Development Authority in its tax incentives program.

As to the incentives offered, we have no objection to tax exemptions and tax credits. However, offering rebates in our current fiscal condition is not advised. However, because the rebates are to come from the Tourism Revolving Fund the Department of Tourism would be in a better position to determine the effect of rebates on its operations.

With regard to the section of this Bill that allows for the sale or transfer of earned tax credits to another Virgin Islands taxpayer, the Bureau of Internal Revenue would be in the best position to assess the impact on our tax rolls and whether this practice is in the best interest of the Territory. As to the timelines imposed on the respective government agencies mentioned in this Bill, I am certain each agency will comment as to the feasibility.

The Economic Development Authority is committed to STARS and we appreciate this opportunity to share our views on Bill No. 31-0009. My team and I will be available to answer any questions.

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