

The Creative Economy as “Big Business” **Evaluating State Strategies to Lure Film Makers**¹

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In an economy where manufacturing and service jobs are being lost, film and television production seems like a good prospect for knowledge economy jobs. The presence of film crews entertains tourists and residents. Movies and TV shows may help market the city or state where scenes were shot. And, because filming activity is highly visible to the public, it appeals to policy makers who want to be seen as taking action to improve their state economy.

Since the late 1990s, state policy makers across the U.S. have ramped up efforts to attract film and television production to their states through tax-based subsidies that provide producers with cost reductions, rebates, or upfront money to finance their productions. These subsidies are justified on the grounds that entertainment media production will promote economic development and inject millions of dollars into the state economy. As subsidies to film and television producers have spread (43 states across the US now offer them in some form) and state budgets have come under increasing pressure, questions are being raised about the use of public tax money to lure media producers. Skeptics ask whether the cost of attracting media producers is worth it. Does the state's economy benefit enough to warrant taking money from other important activities, such as education or infrastructure or the arts? Can new, sustainable industries really be built in cities and states that have no history of media industry investment nor a sizable skilled production workforce.

To better understand the role that tax-based financing plays in film and television production, and whether it pays off for state economies, we assessed the claims put forward regarding economic development benefits, and the assumptions underlying those claims. We examined the available evidence concerning the fiscal impacts of film and television subsidy programs, and the methods used to calculate subsidy-produced job creation and tourism impacts. We also looked at the potential for developing film and television industries outside the industry centers in Los Angeles and New York. Our findings reinforce concerns about government and industry transparency, and about the inefficient or ineffective use of public money as states compete for new investment.

The Contemporary Media Entertainment Industry

Film and television producers have always needed to find financing for their projects. In the past, that financing came from banks and from the firms that distribute film and television programs –film distribution companies, such as Disney or Universal Pictures, and the TV

¹ Highlights from a broader study of film incentives, which will be available online by Fall 2009.

networks. To understand why producers are seeking money from states to finance their projects, we need to understand how the industry has changed.

In the contemporary entertainment media industry, producers work on contract rather than as employees. They operate in an environment in which costs have risen dramatically, particularly because of the bargaining power of media “talent” (including actors, directors, and writers) and the increased cost of marketing entertainment media across multiple distribution venues – theater, network television, cable, DVD and videotape, and private exhibition. As contractors, producers are squeezed by distribution conglomerates to find financing for their projects and reduce production costs wherever possible. Media production is labor intensive and depends on a high-skilled workforce, so cost reduction means labor cost reduction. The salaries of the “talent” are a significant part of the total budget, depending on their star power, but since well-known actors and directors are important to marketing the film or television product, cost reduction pressure is typically aimed at the shooting phase of the production process and the skilled craft workforce. If the production is made under contract to the distribution arm of a conglomerate such as General Electric (which owns NBC/Universal), it is likely to be subject to cost control measures typical of the parent firm.

So, producers are pushed to look for subsidies provided by state governments as a source of project financing by the companies that distribute their products, from whom financing is harder to get.

Assessments of the Fiscal Effects of Film and Media Subsidy Programs

Fiscal impact analyses of the impact of film and TV subsidy programs overwhelmingly conclude that the subsidies have a negative impact on state tax revenues, particularly if they take the form of saleable tax credits.

For example, the tax implications of the 2008 legislation passed by the State of Michigan were assessed by the State Senate Fiscal Agency, and in a briefing to the State Senate, the Director of that agency described the program as “*more like a grant than a tax break because it provides taxpayer-funded checks to producers making movies in the state.*” The incentive program is anticipated to cost \$127 million in the 2008 fiscal year, only \$10 million of which will be offset by income and sales tax receipts.

The State of Rhode Island Department of Revenue calculated that for every dollar invested in motion picture production tax credits, the State earns back \$0.28 from direct economic investment (expenditures made in conjunction with the projects themselves).

In 2005, a highly critical assessment of the nation’s oldest transferable tax credit program by Louisiana’s chief economist Greg Albrecht found that “*Tax credits generated by the film projects are real reductions to existing tax liabilities.*” Albrecht’s fiscal analysis shows that state tax revenue gains, including those from the economic “ripple effect” of production expenditures, amount to only about 16-18% of state tax credit costs.

And, in another analysis of the fiscal impact of tax incentives to draw media producers:

When Wisconsin's incentive bill was proposed, a state Department of Revenue report suggested the net fiscal impact was ultimately "indeterminate." But it calculated a hypothetical example of a production with \$10 million in expenditures, wages of \$50,000 for 100 employees and 50 percent of expenditures subject to sales and use taxes (and thus rebates) and concluded that the state would likely see a net loss in revenue.²

A Connecticut Department of Community and Economic Development study of that state's 2007 incentive program showed a loss of \$14.5 million in State revenues. The report notes:

For every dollar spent on the tax credit, the state receives \$0.08 back in additional revenue. This will have a small favorable fiscal impact only if the state government pays for the film tax credit by reducing spending. The state will not receive enough additional revenue from increased economic activity to pay for the estimated \$16.5 million in tax credits applied for in 2007.

These analyses raise questions about what could have been supported by these lost tax revenues if they had not been spent on subsidies to film and television producers.

Broader Economic Benefits?

Proponents of subsidies to entertainment media producers argue that that despite the tax losses associated with film and television subsidies, they provide broader economic benefits to the state that include job creation. Analyses of job impacts are largely based on models, using a set of assumptions about what kinds of expenditures are made by productions shooting in the state, and what the economic "ripple effects" will be. As a result, claims about job creation are difficult to substantiate.

Problems of transparency and accuracy increase because information on the *actual* expenditures of film and television producers "on-location" is not made public. State Film Office directors frequently present total dollar figures and job estimates to the media without an independent accounting. Some studies supporting tax-based subsidies include *all* productions in a state in estimating the economic benefit of the incentive program, and claim all associated jobs to be a result of the tax incentives. Productions are included even when they did not qualify for the tax incentives, or when they would have shot their production in the state even without an incentive.

Studies making estimates of job creation use very different assumptions about: 1) the types and duration of jobs created; 2) the wages paid to film and television crew members; 3) where the film crew members live and spend their wages; and 3) the "ripple" effects of production expenditures. Consequently, they come to dramatically different conclusions about economic impact. Advocates of film incentives find big job gains and strong multipliers, while analysts such as those working for the U.S. Federal Reserve Bank or for state revenue departments and legislative committees find only modest job creation.

² Cobb, Kathy. 2006. "Roll the Credits...and the Tax Incentives" in *Fedgazette*. Minneapolis MN: Federal Reserve Bank of Minneapolis, September.

The job creation picture is made even more cloudy because people employed on production crews are employed only for the duration of that film or television “project”. When it ends, they move on to another project, perhaps in another state. A study conducted for the Connecticut legislature found that average employment on projects in Connecticut was under six weeks, and could range from a week to a year.

The “on-again/off-again” nature of employment on film and television projects in turn creates a problem in attracting new productions, because producers entering the state want to know that there will be skilled people available exactly when they need them. The conundrum of “crew depth” has dogged the states trying to compete for productions for 35 years. A state has to get multiple projects to keep skilled crew employed consistently (so that they won’t leave for greener pastures or take a job outside the industry), but it also has to have enough skilled crew *unemployed* and available so that they can attract new productions. This problem has hampered Louisiana’s ability to turn significant subsidies into an industry presence.

Can States Capture Footloose Production By Investing in Studios?

Even if they agree that short-term impacts are negative or minimal, proponents justify subsidy expenditures as “loss-leaders” necessary to build an industry in the long term. They compare the expenditures on film and television production to those made to attract tourists and business visitors. But the kind of infrastructure investments made to attract tourists and business visitors, such as Main Street renovation programs or harbor developments or aquariums, also benefit local residents. The infrastructure investments being proposed to “stabilize” production in the film and television industry would only benefit the users of those facilities.

Moreover, the only study that has ever been conducted on the economic benefits of studio construction concluded that for studios to be self-supporting, they had to be owned by a production company. A studio can cover overhead only if the owner is in a position to continuously channel productions into the facility. This reality is what shaped the media incentive program in New York; only productions using “approved facilities” can tap the incentive program. There the goal is to keep studio facilities (which are not owned by production companies) continuously occupied with long-term, high budget users. New York’s program is intended to maintain the profitability of its production facilities, not to build an industry.

While construction of a studio by a production company could have potential economic benefits, state investment in studios to be leased by productions receiving subsidies could lead to a situation in which subsidies would be needed *in perpetuity* to cover the overhead in the facility.

Finally, facilities are not the only kind of infrastructure necessary to a sustainable industry. One of the reasons that production companies may be hesitant to build and operate a studio facility in a state with only a small production base is that studios, production companies and producers rely on a complex concentration of specialized businesses that serve them. These include specialized lawyers and accountants, payroll companies, equipment rental companies, casting companies, agents, and technical specialists in all the fields that go into film and television production. Without that infrastructure, producers may be able to relocate certain types of low-

end television productions, but those are unlikely to justify state investments or meet policymakers' hopes for a glamorous high road industry.

What Measures Would Help Us Make Effective Decisions

This overview of what is known about the economic impact of state programs to subsidize film and television productions leads to three conclusions.

First, the fiscal impacts of the subsidies are overwhelmingly negative. More tax money is paid out than comes back to the states in revenue produced directly -- and by most assessments, indirectly -- by the presence of film and television productions in a state.

Second, the indirect impact of expenditures made in conjunction with subsidized film and television productions cannot be gauged accurately without public access to information on the budgets, actual expenditures, and the labor force (wages and place of residence) of subsidized productions over a period of years. In the absence of such information, we are left with a continuous battle between reports based on wildly different assumptions.

Third, further public investment in studio facilities is a high-risk proposition in an industry organized around short-term projects and dependent on an immense and intricate network of facilities, services and specialized skills.

We live in an era in which the need for transparency in government has once again become evident. The first step in effectively evaluating the long-term impact of state subsidies to film and television producers is to make budgets, expenditures, and the assumptions behind claims of public benefit available for scrutiny and independent analysis. Analyses may still differ in their conclusions, but at least they will be working in the light, off the same body of information.

In addition, state policy makers need to take stock of whether they have assets suited to building a media industry niche that is sustainable. While entertainment media production is growing, entertainment media employment is *increasingly* concentrating in California. States as diverse as Texas, Florida, Illinois, North Carolina, and Massachusetts do have sizable media industries, but they are rooted in commercial production, digital design, education programming, documentaries, training, simulation, and "industrials" as well as conventional film and television. Those products are not as glamorous as Hollywood entertainments, but they may provide a better basis for sustainable employment and export revenue.

Finally, we need to revisit the question of competition. If a state gets off the "subsidy train", will it lose? From an economic development perspective, the answer may be no. The state will have more tax dollars for economic development investments that benefit multiple industries or provide more reliable long-term payoffs, such as building the skilled workforce of the future. The information that policymakers and citizens need to make this calculation has not been available to them, and it should be. So at this point, the signals are not clear, but the "subsidy train" keeps picking up steam.