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**TO THE HOUSE COMMITTEES ON ECONOMIC REVITALIZATION,
BUSINESS, & MILITARY AFFAIRS AND HIGHER EDUCATION**

TWENTY-FIFTH LEGISLATURE
Regular Session of 2010

Thursday, February 4, 2010
10:30 a.m.

TESTIMONY ON HOUSE BILL NO. 2382 – RELATING TO DIGITAL MEDIA.

**TO THE HONORABLE ANGUS MCKELVEY AND JERRY CHANG, CHAIRS, AND
MEMBERS OF THE COMMITTEES:**

My name is J.P. Schmidt, State Insurance Commissioner, testifying on behalf of the Department of Commerce and Consumer Affairs ("Department"). The Department limits its testimony to sections 4 and 5 in Part I on page 20 of this bill and submits the following comments.

Section 4 of the bill adds a new section to Part III of Article 6 of the Insurance Code, Hawaii Revised Statutes ("HRS") chapter 431, governing permitted investments. This new section allows insurers to invest any of their funds that would have been used to pay their premium tax liability in an amount equal to all or part of their tax liability in a "qualified digital media infrastructure project" as defined in section 209E-A.

Section 5 of the bill amends HRS § 431:7-204 by adding a new subsection (g) to allow an insurer to invest its premium tax liability in a qualified digital media infrastructure project.

"Qualified digital media infrastructure project" is defined in section 209E-A on page 1 of the bill as the development, construction, renovation, or operation of a digital medical production facility, a postproduction facility, or both, located within a digital

media enterprise subzone, which may include a movie theater or commercial exhibition facility.

Allowing insurers to invest funds up to its premium tax liability would appear to violate the limitations on invested assets in the Insurance Code and the National Association of Insurance Commissioners' ("NAIC") Accounting Practices and Procedures Manual.

These limitations ensure the protection of the interests of policyholders by requiring that an insurer's assets are diversified and invested in conservative, highly liquid investments to promptly pay insurance claims and obligations.

As currently drafted, section 4 of the bill adds a new section to Article 6, Part III governing permitted investments, that deems an insurer's investment in a qualified digital media infrastructure project a permitted investment.

Although it may be a permitted investment, HRS § 431:5-202 governs an insurer's assets that are not allowed to be used in the determination of an insurer's financial condition. As defined in section 209E-A, investments in a "qualified digital media infrastructure project" would fall under HRS § 431:5-202(6) and affect an insurer's financial condition, as these funds cannot be used to pay policyholder claims.

For consistency with other credits allowed under the Insurance Code, the Department respectfully requests deleting sections 4 and 5 of the bill and adding a new section to Part II of Article 7 as follows:

"§431:7- Digital media infrastructure tax credit. The digital media infrastructure tax credit provided under section 209E-B shall be operative for this chapter on July 1, 2010."

We thank this Committee for the opportunity to present testimony on this matter.

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**HOUSE COMMITTEES ON ECONOMIC REVITALIZATION, BUSINESS &
MILITARY AFFAIRS AND HIGHER EDUCATION
TESTIMONY REGARDING HB 2382
RELATING TO DIGITAL MEDIA**

*****WRITTEN TESTIMONY ONLY*****

TESTIFIER: KURT KAWAFUCHI, DIRECTOR OF TAXATION (OR DESIGNEE)

DATE: FEBRUARY 4, 2010

TIME: 10:30AM

ROOM: 312

This measure provides, among other things, the establishment of digital media enterprise zones, as well as digital media infrastructure and workforce development tax incentives.

The Department of Taxation (Department) **opposes** this measure because it is **outside the budget priorities this legislative session.**

Notwithstanding the merit of this measure, the Department cannot support the tax provisions in this measure because these tax breaks are not factored into the budget. The Department must be cognizant of the biennium budget and financial plan. This measure has not been factored into either. Given the forecasted decrease in revenue projections, this measure would add to the budget shortfall.

The Department simply cannot support this tax credit given the other more important competing priorities for general fund revenues.



UNIVERSITY OF HAWAII SYSTEM

Legislative Testimony

Testimony Presented Before the
House Committee on Economic Revitalization, Business and Military Affairs
and
House Committee on Higher Education
February 4, 2010 at 10:30am
by
James R. Gaines
Vice President for Research, University of Hawai'i

HB 2382 – Relating to Digital Media

Chairs McKelvey and Chang, Vice Chairs Choy and Nakashima, and Members of the Committees:

HB 2382 establishes digital media enterprise subzones as unspecified geographic areas surrounding University of Hawai'i campuses that are also designated as enterprise zones. This bill also establishes tax benefits for digital media infrastructure development and operation and local workforce employment; authorizes insurance companies to invest in qualified digital media infrastructure projects in lieu of paying certain state taxes.

The University of Hawai'i System supports the intent of this bill and, while the Title of the Bill may be too restrictive, recommends that green/renewable energy technologies be included as a subzone as well.

Thank you for the opportunity to testify.

Testimony Presented Before the
House Committee on Higher Education
and
Committee on Economic Development & Business Affairs Concerns
Thursday, February 4, 2010 at 10:30 am
by
Chris Lee, Founder and Director
Academy for Creative Media, University of Hawai'i System

HB 2382 – Relating To Digital Media

Chairs Yamashita and Chang, Vice Chairs Wakai and Nakashima, and Members of the Committees:

I write in strong support of HB 2382 which will create metric-based, measured incentives to build our digital media infrastructure and develop our local creative media workforce so that our talented students can stay here in Hawai'i.

I am the Founder and Director of the UH Academy for Creative Media (ACM). The ACM has enjoyed unprecedented growth since its approval as a system-wide program in late 2003, and I want to start by thanking the legislature for creating the position numbers and funding to hire our great faculty in the first place.

This year, our first campus, ACM-Manoa, has over 350 students and 130 majors in 39 courses

Our students have made over 700 short films and animations, many of which have played to great acclaim in festivals around the world.

“ACMMERS,” as I call them, were the first students anywhere to show films at the Shanghai International Film Festival and now students from ACM and China are making films together in Shanghai and Hawai'i.

ACM students have been interns and employees on “LOST” and we’ve just started our first system-wide internships with students from ACM-Mānoa, KCC’s New Media Arts, and LCC’s Animation Program working at the new Hawai'i Animation Studios.

These kids are at the vanguard of Hawai'i's new media economy.

Most importantly, ACM graduates have immediately started their own digital media companies—like visual effects firm Blue Water Multimedia, and production companies like HDology and Enlight which use state of the art high definition “Red” cameras.

But success in creating new jobs is not limited to ACM or UH graduates.

Makaha Studios was started and is run by five talented graduates of Waianae's Seariders – it's a production and internet content company with local and national clients and the first tech business on the Waianae coast.

And next week, the new Hawai'i Animation Studios opens on Bishop Street which is not only using our interns, but the majority of their hires have been ACM and KCC graduates. Indeed, their business plan – they've come here from Canada – is based on their ability to hire talent locally.

Moving forward, the successful incubation of the program at Mānoa allows for the expansion of ACM to other campuses within the UH system in order to serve the next generation of students in public and private schools and to continue to act as a catalyst for Hawai'i's digital media industry.

There are over 80 media programs throughout the D.O.E. and, like Waianae's Seariders, these programs are keeping our kids in school and graduating them to two- and four-year colleges.

The reason for this is that educational achievement is largely aspirational. Students need to believe in themselves and that their work will lead to meaningful employment opportunities.

This is about jobs, right here, right now, right in Hawai'i.

We are generating a talented, indigenous workforce – the most coveted kind in the global economy, what are know as “the creatives.”

Media production in all its forms: films, television, software, video games, massive multi-players, animation, visual effects, even Apple iphone applications, is America's largest economic export and offers Hawai'i our best chance of breaking open the shackles of our dependence on the service industry.

Why is this possible?

Broadband connects us to the global economy in ways that ships and planes cannot. Creative intellectual property only requires that we harness the natural talent of our students; it doesn't need endless access to greater capitol, the importation of raw materials and the physical shipping of the finished product, vast tracks of land or resources that threaten our environment, or the relocation to the mainland in success.

Some of you may be skeptical about incentives in the media sector, so here are a few of the success stories over the last decade in other states and countries who have invested in their media economies.

New Mexico introduced incentives in 2001 at which time Hollywood spent only \$1.5 million annually there. In 2007, New Mexico enjoyed \$476 million in spending in the film and digital industry and opened the \$75 million Albuquerque studios. There are also now visual effects firms like Sony Imageworks and even their supercomputer is being used by Dreamworks Animation. To jumpstart their industry, the state actually helped finance the making of certain films.

Louisiana also started tax incentives for film in 2001 when there were only two low budget pictures shot in the entire state. By 2006, 21 low budget films and 5 big budget pictures combined for \$450 million in production spending. Their incentives have also made possible the building of multiple studios.

But the industry is not just about film – indeed, the future is about anything but traditional celluloid. Electronic Arts is the biggest video game company in the world and last year various states competed for their new quality assurance center offering 200 jobs for students and 20 for adults. What do they do? Play video games around the clock looking for glitches. Where did it go? The Louisiana State University campus thanks to the efforts of their Governor and the State's specific digital media tax credit.

Connecticut is in the hunt. Literally. They poached Blue Sky Animation Studios ("Ice Age," "Horton Hears A Who") from New York State by opening a 106,000 square foot facility with 300 jobs thanks to tax incentives including 20% back on infrastructure costs exceeding \$1 million.

Singapore has determined that creative media is a desirable, sustainable industry and is investing hundreds of millions of dollars in infrastructure and incentives to realize their goal of 10,000 new jobs in the media sector by 2015.

Their targeted incentives have been used to get George Lucas ("Star Wars") to move his animation and video game division from San Francisco to Singapore, training a local work force which recently added 120 employees to their first 280. Lucas joined visual effects companies from London and video game companies like Ubisoft as the city state builds a mediapolis of studios, post production houses and nine film schools.

New Zealand's film and television industry is estimated by Price Waterhouse Coopers to generate \$2.5 billion a year for their economy. Most recently, the bulk of "AVATAR" was produced there, spending \$307 million dollars, and generating \$50 million in taxes.

Asked in December why New Zealand was chosen as the film's production location, AVATAR producer Jon Landau said: "to be honest, we went for the tax credit."

And he's right. Incentives are the first thing producers and studios take into consideration when deciding where to shoot. But the second consideration is infrastructure and workforce.

As one New Zealand official put it, thanks to AVATAR, "This is exactly where we need to be as a country - renowned for our technological know how, creativity, talent and positive, can-do attitude."

Hawaii can do the same. In some ways we already are with programs like ACM and the Seariders.

Passing this measure will take advantage of the natural skills of our kids and soften the cyclical blows of our aviation fuel based service economy.

In this era of the great recession, perhaps you've noticed that the two sectors of the economy that have not suffered and are actually up are education and entertainment. This bill wisely combines them both.

Thank you again for the chance to testify today.

From: Albano, Andres @ Honolulu [Andres.Albano@cbre.com]
Sent: Wednesday, February 03, 2010 11:08 AM
To: EBMtestimony
Subject: Testimony supporting HB 2382

February 3, 2010

Re: HB 2382, Hearing at 10:30 AM on Thursday, February 3, 2010, Conference Room 312, State Capitol

To: Representative Angus L.K. McKelvey, Chair of the Committee on Economic Revitalization, Business & Military Affairs
Representative Jerry L. Chang, Chair of the Committee on Higher Education

Gentlemen:

I recently served on the University of Hawaii Board of Regents as the Vice Chairman as well as serving as the Chairman of the Public/Private Partnership Task Group and the Chairman of the Committee on Long Range Planning, Budget, Finance and Facilities.

The passage of HB 2382 and the companion bill SB 2355 will go a long way in not only revitalizing the economy of Kapolei and the State of Hawaii but will be a critical factor towards helping the University of Hawaii West Oahu realize its long range goals.

I support passage of the bill.

Andres Albano, Jr. (B) | Senior Vice President
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February 3, 2010

RE: House Bill HB 2382

Honorable Representatives:

Our wholly-owned Film Studio Group (please see attached) has worked on film production facilities around the world and has been attempting to undertake a film and television studio in the Kapolei area for the past five years. It's extraordinarily challenging to build a studio in good economic times, and needless to say, there's little positive about the current economic climate.

Over 40 states and numerous foreign countries have film incentive programs and are vying for film, television and now commercial business because of the high paying jobs created together with outsized expenditures on local goods and services, not to mention positive externalities such as promoting tourism. Hawaii has much to offer, but productions have ever-increasing alternatives to choose from, most of which are less expensive.

Despite the cost differential, productions still tend to seek out Hawaii first for its tropical locations and talented crew base. Unfortunately, many productions are lost due to the State's biggest shortcoming—lack of production facilities. Over the past few years *Lost* has occupied the only sound studio in the Islands, and even with rising vacancies in the industrial sector, there have been few viable options in warehouse buildings which are not really suitable for their needs anyway.

A full-service film and television studio, such as we are proposing to build, would significantly increase production expenditures in the State by attracting projects which require some controlled-environment facilities as well as increasing the footprint of those which are primarily location-based, i.e. few productions spend more than a third of their budgets on location work. As production work increases in both number of projects and duration of each, the local workforce will expand (please see attached) and a more robust industry will flourish.

It will not be possible to build this studio without the infrastructure credit encompassed in this bill, especially in light of the turmoil in the financial markets. It is not possible to overstate the importance of this legislation if there is a desire to promote filming, a clean, high tech industry offering significant employment opportunities, in the State of Hawaii. I urge your support and would be pleased to answer any questions regarding the project or the industry.

Mahalo,

A handwritten signature in dark ink, appearing to read "Stephan".

Stephan D. Smith
President

EXECUTIVE SUMMARY

INTRODUCTION

- Economic development through digital entertainment has been embraced by economies around the world and states throughout the mainland.
- Creative media is America's largest economic export after aerospace.
- Broadband connectivity and access to human capital has disbursed the centers of intellectual property creation. Today, it is not just Hollywood providing entertainment for the world. It is unexpected pockets of creativity from Emeryville (Pixar), Atlanta (Tyler Perry), Austin (Robert Rodriguez) and beyond providing content for screens big and small around the world.
- The common factor in this success is that technology and connectivity has made it possible for talent to work where they want to live, rather than having to live where the work is.

HAWAII

- As Hawaii assesses how best to diversify its tourism and construction based economy it faces limited choices.
 - Hawaii's fragile ecology and geographic distance limit its opportunities for traditional manufacturing and industry.
 - Development and execution of intellectual property neither threatens Hawaii's island environment nor requires the expensive importation of raw materials nor the shipping of hard finished goods.
 - And, the last decade has seen an explosion of success from local students in our educational system studying, executing, and graduating to jobs in the media industry
 - Students from across the public and private educational spectrum have demonstrated that Hawaii has a brilliant pool of talent waiting to be tapped, nurtured, and just as important, given the tools to remain in the islands to pursue their dreams
 - Companies such as Makaha Studios, Bluewater Multimedia, and HDArsenal are thriving thanks to the talent of the State's students.
- At the same time, traditional film production has reached new records but Hawaii's capacity for building on this industry is limited by the lack of resources and infrastructure.
- The only film production studio in Hawaii has just one sound stage and can, at best, accommodate one show at a time – as it has for LOST for over five years

KAPOLEI STUDIOS/ACADEMY OF CREATIVE MEDIA

Kapolei Studios at UH-West Oahu (Studio) together with the Academy of Creative Media (ACM) will be a catalyst for the creative media industry in Hawaii.

It will dramatically increase the local film and media infrastructure capacity, i.e. by five times, and provide an educational facility for work force development—together a digital media economic anchor for the West side of Oahu's second city, Kapolei (see Economic Impact attached).

The Studio campus, encompassing sound stages and production support facilities, office space, entertainment retail and a comprehensive film and digital media student center, represents an aligning of interests – affording a significantly enhanced production capability to the state and recognizing the rising success of media programs

throughout the state educational system from Waianae High School's Searider Productions to the University of Hawaii's Academy for Creative Media. And the recognition that digital media entertainment offers Hawaii one of the few opportunities we as a state have to engage the global economy while providing living wage jobs to keep our students at home in the islands.

In addition to being Hawaii's first full-fledged production facility with multiple purpose-built stages, the ACM-West Oahu Studios will offer a state of the art student production teaching facility. This facility will include smaller stages for student productions, post production facilities that can be utilized by local filmmakers as well as students and facilities for expanding our traditional production base in the growing fields of computer animation, visual effects, video games, and post production services.

In addition, long-term master planning calls for office space for the incubation of emerging media companies, dormitories for students from Hawaii and around the world, and extended stay housing for faculty and visiting talent.

Indeed, the Studio/ACM is a unique public/private partnership that recognizes the need for and facilitates the building of a post industrial economy for the state of Hawaii.

This plan (see representative conceptual master plan attached) calls for:

- 1) Four 18,000 square foot purpose-built sound stages
- 2) 95,000 square feet of production and dressing room space plus longer-term office space for entertainment industry companies
- 3) 50,000 square feet of mill and ancillary production support space.
- 4) 30,000 square feet of commissary, screening room and meeting space.
- 5) A "filmable" backlot with 32,000 square feet of retail space, offering a unique tourist destination and special event venue.
- 6) An extended-stay facility for film crews.
- 7) A digital media student facility

This studio facility will be designed to accommodate productions ranging from commercial work through all types of television (episodic, movies of the week, talk/game show, etc.) to major motion pictures which typically come to Hawaii for location filming only. It will offer facilities, services, equipment and an operational framework familiar, and comfortable to "Hollywood".

SPONSORSHIP

SHM Partners

Owner/developer Smith, Hricik & Munselle (SHM) is a multi-faceted real estate development and management company based in Downtown Los Angeles.

The firm's principals, Stephan D. Smith, Lawrence M. Hricik and Weston P. Munselle combined, have over 70 years of experience in the finance, acquisition/disposition, development and management of real estate. SHM has also planned, developed and/or operated over 6 million square feet of office, mixed use, residential and film production space.

Under its Film Studio Group banner, SHM has been involved in the planning, development, adaptive reuse and/or management of film and television production facilities on five continents, in countries such as Canada, Mexico, Spain, Czech Republic, U.K., South Africa, Thailand, Australia and New Zealand and numerous states in the U.S.

SHM also created Skyline Locations, one of the largest and most diversified location companies based in Los Angeles as well as B2B-TV, a unique provider of cost-effective, high quality HD television programming to businesses in multi-tenant commercial buildings.

Principal and founder Stephan Smith, who spends at least one week per month in Hawaii, has been in the real estate business for the past 30 years and in studio development for over 12 years. He received his B.A. from Yale University and M.B.A. from the Wharton School.

May 12, 2009

Economic Impact
Of
The Kapolei Digital and Film Studios

The Kapolei Digital and Film Studios are a project slated for a 22 acre site in Kapolei, Oahu, Hawaii. Current plans call for a two phase build-out that would include:

- 4 – 18,000 sq ft purpose built, state of the art sound stages
- 57,700 sq ft of office, dressing rooms, set construction and production support
- 18,000 sq ft Student Annex film and digital studio
- 32,000 sq ft of retail and back lot activities supporting a unique tourism venue
- 125 suite extended stay workforce housing

The complex would be built out in two phases over four to five years with sound stages, dressing rooms, office space, and set construction facilities in phase I, all other facilities in phase II. Two sites are being considered, the existing site, adjacent to the Kapolei Business Park, and a possible site adjacent to the University of Hawaii West Oahu Campus, to tie into the Academy of Creative Media at the University. If the UH site is chosen, the Student Film Annex would be built in Phase I.

The Kapolei Digital and Film Studios (KDFS) will directly employ 1,645 personnel of which 45 are studio staff and 1,600 are production personnel with an annual payroll of \$79.8 Million dollars. Additionally, KDFS will also contract with 15 to 20 local area companies for supplies, support, and associated market goods.

I Direct Employment

Studio Staff	45
Film Crew Members	1,600
Average KDFS Wage:	\$ 48,500
(Hawaii's Average Wage \$ 37,023)	
Annual Payroll	\$ 79,800,000

II Indirect Salary Impact (external suppliers + subcontractors + induced)

1645 jobs (@ \$48,500) x 1.27 x \$37,023)	\$ 77,346,000
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III Total Annual KDFS Salary Impact: **\$157,146,000**
(Direct and indirect salaries combined)



IV	Total Projected tax impact: (GET + payroll + state income)	<u>\$ 15,489,000</u>
V	Total Annual KDFS production Goods and Services:	\$ 18,000,000
VI	Total Annual KDFS Market Expenditures: (\$18,000,000 x .24 Source DBEDT IO model)	\$ 4,320,000
Total Annual Economic impact of KDFS:		<u>\$194,955,000</u>
VII	Total Construction Jobs	
	Phase I \$63,000,000	300 FTE jobs
	Phase II \$46,000,000	250 FTE jobs
VIII	Employment Value of Construction Jobs	<u>\$ 47,960,000</u>
	Phase I \$63m x .44	\$27,720,000
	Phase II \$46m x .44	\$20,240,000

Sources: Department of Labor Statistics, DBEDT input output model for Hawaii

Current state film and digital industry growth is constrained by the lack of sound stages and digital infrastructure, requiring production crews to shoot exteriors in Hawaii then adding interiors, sound stage, and post production on the mainland or elsewhere. The Kapolei Digital and Film Studios would increase state film and digital production capacity by 250%. This would not affect existing state owned facilities which historically have been continuously in use and have little room for expansion.

Situated in the second city of Kapolei, the facility would provide quality employment along the west coast of Oahu, drawing from Waipahu to Makaha, including the SeaRider Academy and the University Of Hawaii Academy Of Creative Media. This would add jobs in the region and provide a greater live-work-play option to Kapolei.

If situated on the UH West Oahu Campus, KDFS would help grow the Academy of Creative Media through the Student Film Annex and internship programs tied directly to the University. Additionally, workforce housing required for the KDFS project could be expanded to also provide extended stay housing for UH faculty, visiting professors, and research participants. This would also locate the studio at the end of the Honolulu Mass Transit Rail system making it easy to access the facilities from Leeward Oahu.

Hawaii has a variety of digital and film facility requirements that are marginally being met through temporary facilities and the addition of the KDFS facilities will provide a home base for the many production companies doing business or based in Hawaii. This will allow for growth in full-time Hawaii based film and digital employment with an average wages 40% higher than the Hawaii State average wage.