UNIVERSITY OF HAWAIʻI SYSTEM
Legislative Testimony

Testimony Presented to the
Senate Committee on Ways and Means
Tuesday, April 5, 2022 at 10:15 a.m.
by
Christopher P. Lee, Founder/Director, Academy for Creative Media System
on behalf of
Vassilis L. Syrmos, Vice President for Research and Innovation
University of Hawaiʻi System

HB 1982 HD2 SD1 – RELATING TO TAXES

Chair Dela Cruz, Vice Chair Keith-Agaran, and Members of the Committee:

The University of Hawaiʻi (UH) supports the intent of HB 1982 HD2 SD1 to enhance Hawaiʻi's successful motion picture/television/streaming production industry with changes to the current film production tax credit. In particular, UH strongly supports the extension of the sunset date of the credit from December 31, 2025 to December 31, 2032. A stable, reliable credit is essential to continuing the growth of this vital diversification of Hawaiʻi's economy.

Thank you for the opportunity to testify on this measure.

DAVID Y. IGE
GOVERNOR

JOSH GREEN M.D.
LT. GOVERNOR

ISAAC W. CHOY
DIRECTOR OF TAXATION

STATE OF HAWAII
DEPARTMENT OF TAXATION
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To: The Honorable Donovan M. Dela Cruz, Chair;
The Honorable Gilbert S.C. Keith-Agaran, Vice Chair;
and Members of the Senate Committee on Ways and Means

From: Isaac W. Choy, Director
Department of Taxation

Date: Tuesday, April 5, 2022
Time: 10:15 A.M.
Place: Via Video Conference, State Capitol

Re: H.B. 1982, H.D. 2, S.D. 1, Relating to Taxes

The Department of Taxation (Department) offers the following comments regarding H.B. 1982, H.D. 2, S.D. 1, for your consideration. The measure has a defective effective date of July l, 2050, and does the following:

- Establishes a 4.5 percent general excise tax (GET) withholding requirement for all payments to loan-out companies for services performed in Hawaii for persons claiming the motion picture, digital media, and film production income tax credit (Film Credit) under section 235-17, Hawaii Revised Statutes (HRS);
- Extends the repeal date of the Film Credit from December 31, 2025, to December 31, 2032;
- Authorizes the Department to impose fees of up to one-tenth of one percent of the amount of the credit for the processing of Film Credit Applications, with the fees collected going into the Tax Administration Special Fund (TASF);
- Amends the TASF to provide for the processing of Film Credit applications;
- Deletes the requirement that claimants obtain a verification review produced by a certified public accountant (CPA);
- Requires the Department of Business, Economic Development and Tourism (DBEDT) to submit a nonredacted report to the Legislature regarding Film Credit claims;
- Amends the TASF to allow for the deposit of Film Credit application fees; and
- Authorizes the Department to establish 4 FTE auditor positions to examine Film Credit claims and other tax expenditures.

First, the Department notes that there are two provisions in the measure that establish a GET withholding requirement for loan-out companies. One provision in Section 1 creates a new statute in Chapter 237, HRS, and the other adds a new subsection to section 235-17, HRS. The

Department suggest retaining the statute in Section 1 and deleting the amendment to section 235-17, HRS. Additionally, the Department suggests amending the sentence that begins on page 1, line 11, to read:

> The amounts withheld under this section shall be deemed to be a tax withholding for the benefit of the loan-out company performing the service.

Second, the Department notes that the requirement for an independent verification review by a qualified CPA has been deleted. The Department believes that this review is an important aspect in preventing inflated and/or frivolous claims of the credit, and requests that this requirement be maintained. The Department suggests retaining the CPA review for Film Credit claimants.

Third, the Department notes that DBEDT will not be able to produce a report to the Legislature with the amount of Film Credit claimed as DBEDT does not have access to the tax returns on which the Film Credit would actually be claimed. Thus, the Department suggests requiring the report to state the amount of credit *certified* instead of the amount claimed.

Fourth, the Department notes that the amendment to the TASF starting on page 16, line 12, allows for the deposit of Film Credit application fees as well as fees collected under section 231-36.8, HRS. Section 231-36.8, HRS, is the statutory authority for the erroneous claim for refund penalty and, as such, there are no application fees associated with this statute. The Department suggests deleting this provision.

Fifth, although the Department appreciates the amendment to allow for the deposit of Film Credit application fees into the TASF, the maximum amount that could be deposited is $50,000, with the annual aggregated cap for all taxpayers at $50 million. Additionally, the per production cap of $20,000 is not necessary as the per production Film Credit cap is $15 million. This means that even if a production claimed the maximum Film Credit, the fee would be $15,000. The Department suggests deleting the $20,000 per production application fee cap.

Finally, if this measure is to be advanced, the Department respectfully requests that it be made effective no earlier than January 1, 2023. This will allow sufficient time to implement the new GET withholding requirement.

Thank you for the opportunity to testify on this measure.

LATE

DAVID Y. IGE
GOVERNOR

MIKE MCCARTNEY
DIRECTOR

CHUNG I. CHANG
DEPUTY DIRECTOR

DEPARTMENT OF BUSINESS, ECONOMIC DEVELOPMENT & TOURISM

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Statement of
MIKE MCCARTNEY
Director
Department of Business, Economic Development, and Tourism
before the
SENATE COMMITTEE ON WAYS AND MEANS

Tuesday, April 5, 2022
10:15 AM
State Capitol, Conference Room 211

In consideration of
HB1982, HD2, SD1
RELATING TO TAXES.

Chair Dela Cruz, Vice Chair Agaran and members of the Committee.

The Department of Business, Economic Development and Tourism (DBEDT) supports the aspects of HB1982, HD2, SD1 which amend the Motion Picture, Digital Media, and Film Production Income Tax Credit, §235-17, Hawaii Revised Statutes, extending the sunset date to December 31, 2032, providing business certainty for production and infrastructure development, additional requirements for DBEDT to provide dollar amounts claimed, name of the company, and name of the qualified production in its annual reporting to the Legislature and eliminates the required certified public accountant review process for all filers.

The department has concerns regarding the elimination of the CPA review in Section 3, item (h) and requires DBEDT to continue administering the registration and certification process. We want to note that the CPA review has streamlined the process and elimination of this may increase the time for certifications to be issued. While we understand the rationale for this change due to the introduction of the fee and impacts on industry, the department recommends further discussion to include amendments which clarify those sections of SD1 to define roles of the two departments more clearly on the administration of the credit.

We defer to industry and DoTAX on those sections changing financial requirements for obtaining the credit, including loan out specific withholding amounts and payment with filings, prohibiting the defense of erroneous claims, and amending the purpose section of the tax administration special fund.

The Motion Picture, Digital Media, and Film Production Income Tax Credit, §235-17, Hawaii Revised Statutes, is an essential tool to the state's economic recovery efforts amidst this global pandemic. 2021 was another record year for production for the state with $423M in direct expenditures and an estimated 4,500 jobs.

We recognize the value of the film tax credit program and its catalytic role in providing skilled, high paying jobs and the infusion of capital into small businesses who are not part of the industry but provide much needed resources, supplies, food products and services.

Hawaii's creative economy is anchored by the film and media industries. Extending the sunset date to December 31, 2032, is crucial to maintaining the film tax credit program to attract public and private investment to build a new multi-stage facility, as well as regional studio spaces for local production use.

The department will work with lawmakers and DoTAX to recommend further clarifying language for HB1982, HD2, SD1.

Thank you for the opportunity to testify.

Testimony of Walea Constantinau,
Film Commissioner, Honolulu Film Office
City and County of Honolulu

COMMITTEE ON WAYS AND MEANS

April 5, 2022
10:15 AM
State Capitol, via Videoconference and Conference Room 211

RE: HB1982, HD2, SD1 RELATING TO TAXES

Dear Chair Dela Cruz, Vice-chair Keith-Agaran, and members of the committees:

I **strongly support a portion of the proposed measure, the extension of the Sunset Date to 2032** which is crucial to the continued growth and development of the film industry as a key sector to diversity the economy.

The Hawaii Production Tax Credit is the fuel that drives the engine that powers the current and future development of Hawaii's film industry.

Business certainty is vital to the industry to be able to make physical production and infrastructure commitments. The extension provides that business assurance, and allows the industry the necessary time needed for planning and implementation.

It can take several years for a movie or television series to be conceived of and brought to the point of physical production. For a television series, usually a 5-year minimum run for physical production is projected. The currently requested extension to 2032 allows for a 5-year planning, development and funding phase, and a 5-year implementation and operational phase.

I also strongly encourage the committee to work closely with the industry and DBEDT to craft language acceptable to the long-standing industry practices pertaining to the loan-out section.

Thank you for your kind attention and the opportunity to provide these comments.

ISLAND
FILM GROUP

The Senate
The Thirty-First Legislature
Regular Session of 2022

COMMITTEE ON WAYS AND MEANS
Sen. Donovan Dela Cruz, Chair
Sen. Gilbert S.C. Keith-Agaran, Vice Chair

RE: HB 1982, HD2, SD1 RELATING TO TAXES

Date: Tuesday, April 5, 2022
Time: 10:15 a.m.
Conference Room 221 & Videoconference
State Capitol
415 South Beretania Street

April 4, 2022

From: Roy Tjioe and Ricardo Galindez
Island Film Group
99-1245 Halawa Valley St.
Aiea, HI 96701
808-536-7955

Aloha Chair Dela Cruz and Vice Chair Keith-Agaran, and Members of the Committee:

Our Background

Island Film Group is a locally owned and operated production company. We began working in Hawaii's film and television industry in 2001 as attorneys at Goodsill Anderson Quinn & Stifel, where we represented filmmakers and other production companies. Since our formation of Island Film Group in 2007, we have been working full-time as producers of feature films such as "Princess Ka`iulani" and "Soul Surfer", network and cable television movies and series, as well as a large number of commercial productions.

We SUPPORT

(a) The proposed withholding of income tax on payments to loan-out companies as set forth in Section 1 of the Bill.

(b) The proposed language in Section 3 that extends the year in which excess tax credits may be claimed from 2025 to 2032.

We PROPOSE

Subsection (m) on page 10 should be amended to clarify that gross revenues (i.e. project financing) received by local production companies shall be subject to a GE tax rate of 0.5%. That is the GE tax rate that governed film, television and commercial productions for the past decade until the Department of Taxation unilaterally changed the rate to 4.5% in November, 2019. Since the mainland studios do not pay any GE tax because their project financing is structured as investments into wholly owned production companies rather than payments, the amendment will help level the playing field for local independent production companies while having a minimal financial impact to the State.

Specifically, section (m) as set forth in SD1 should be amended to read as follows (our proposed new text is underlined):

> (m) Every person making payment to a loan-out company shall withhold an amount equal to 4.5 per cent of qualified production costs for services performed in the State; provided that the amount withheld shall be remitted to the department of taxation to the credit of the general excise tax account of the loan-out company to whom the qualified production costs were paid or will be paid; <u>provided further that gross revenues received by qualified productions shall be subject to general excise tax at the rate of 0.5 per cent</u>. The amount withheld shall be remitted no later than thirty calendar days after the qualified production costs are paid or incurred. Taxpayers who fail to comply with this subsection shall be subject to the applicable interest and penalties pursuant to chapter 231 and section 235-104.

Me ke aloha,

Roy Tjioe and Ricardo Galindez
Co-Founders
Island Film Group

MOTION PICTURE ASSOCIATION, INC.
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WASHINGTON, D.C. 20006
(202) 293-1966

TESTIMONY OF VANS STEVENSON IN SUPPORT OF
HB1982 HD2 SD1 RELATING TO TAXES

SUPPORT WITH AMENDMENTS

April 5, 2022

Thank you, Chairman Dela Cruz, and members of the Senate Committee on Ways and Means.

My name is Vans Stevenson, and I serve as Senior Advisor, Global Government Affairs for the Motion Picture Association (MPA).

MPA proudly represents America's major producers and distributors of motion pictures, television series and streaming productions: Netflix Studios; Paramount Global, Sony Pictures Entertainment Inc.; Universal City Studios LLC; Walt Disney Studios Motion Pictures; and Warner Bros. Entertainment Inc. Our member companies' film, television, and streaming projects are creating good-paying local production jobs, supporting local businesses of all sizes, and boosting the economy, in Hawai'i, and around the United States.

Hawai'i's success as a leading film, television and streaming production destination would not have been possible without the critical cost offsets provided through Hawai'i's terrific production tax credit program.

Cost is one of the critical factors in the production location decision-making process, and this program and its cost offsets have been significant catalysts for the film, television and streaming productions that give rise to Hawai'i jobs and support Hawai'i businesses.

Accordingly, I appreciate the opportunity to provide this written testimony, on behalf of the MPA's member companies, in support of an extension of Hawai'i's successful production tax credit program to 2032.

The economic impact of the production industry has produced benefits throughout Hawai'i. It is also felt across many business sectors. New and expanded businesses have followed because there are support services, which benefit from the industry but are not eligible to claim the tax credit. In addition to camera, lighting and audio equipment, production companies use a wide range of support services during production including catering, construction, transportation, accounting/payroll and post-production. These ancillary business expansions have given rise to long-term capital investments, which help ensure the state's investments in this industry are sound.

An extension of Hawai'i's successful production tax credit program sunset to 2032 provides a necessary element to continue to advance opportunities for economic investment and enduring long-term job creation.

Thank you for your support of this industry, which has allowed the motion picture, television and streaming industry to continue to be a vibrant component of the state's economy.

In addition to expressing our support for the extension of this program, we respectfully propose some important changes to the legislation as currently drafted. These changes would preserve the objective of the bill's significant tax reporting and filing changes and also provide the administrative efficiency and fairness necessary to maintain the competitiveness of Hawai'i's production tax credit program.

The proposed amendments we seek to HB1982 HD2 SD1, included in the attached document in **bold with yellow highlight,** are as follows:

Page 1 - SECTION 1. § 237 (a) and (b) We propose changing the income tax withholding percentage rate from 4.5% to the applicable rate.

We respectfully submit it is more appropriate to include the applicable rate to be consistent with the withholding requirements imposed on other taxpayers and the withholding rate is different for each taxpayer. The forced withholding in our amendment at the applicable rate (instead of the 4.5% rate), is a significant and favorable change to the existing statute and will facilitate and ensure tax collections on loan-outs. The amendment we propose will ensure Hawai'i automatically receives the proper income tax withholding. The MPA's amendment in that same section also provides a realistic and manageable withholding reporting timeframe. The proposed amendment would require payments to be made the month following the date on which the payment was made to the loan-out company. The legislation as drafted requires payments to be filed within 30 days of the payment. This proposed 30-day reporting basis creates mandatory onerous remittance on a continual rolling basis, which is unworkable. The onerous reporting proposal may place Hawai'i at a competitive disadvantage in its efforts to attract film, television, and streaming production jobs and investment.

Page 6 - SECTION 3. § 235-17 (i) We propose vital language in this subsection to ensure the production company's final applications will be processed by the state in a timely manner.

This amendment must be included because the legislation as currently drafted strikes the existing provision, which includes certified public accounting verification in subsection (h). Production companies cannot afford a slow approval process of final applications given the statutory requirement in subsection (c), which forces all claims to be filed on or before the end of the 12th month following the close of the taxable year in which the credit may be claimed. If the application is not filed within the 12-month period, the tax credit will be forfeited. Delays in application processing will result in forfeiture of credits, and the risk of that outcome places Hawai'i at a competitive disadvantage in its efforts to attract film, television, and streaming production jobs and investment.

Page 8 - SECTION 3. § 235-17 (n) We propose replacing the new 4.5% General Excise Tax (GET) withholding and replacing it with .5% (the previous rate/manufacturing rate).

This will make the rate consistent with similarly situated taxpayers and - until recently - the longstanding GET tax rate for film production services. This industry has always been considered a manufacturer of content and motion picture, television and streaming production should continue to be treated as such for purposes of the GET. We also added an important amendment to this subdivision to mirror the existing statutory timeframe for taxpayer information reporting, which is not tied to the proposed unworkable timeframe of 30 days from when the payment was made. The current GET filing deadline for all taxpayers is 20 days into the following month. Therefore, the change we propose mirrors that requirement to file on the 20th day following the close of the month, so it's consistent with current procedures and workable for production companies. Under the legislation as currently drafted, production companies would have to be constantly making remittances, which is completely unworkable. For example, remittances for all of a production company's June payments should be due by July 20. There shouldn't be a separate deadline for the payments made on June 1, June 6, June 12, June 19, and June 25.

Our proposed modifications to the income tax and GET reporting timelines will have no adverse impact on the state, and will allow for a stable compliance regime across the film industry, something important to state government and the film industry.

We look forward to working with you and your esteemed colleagues in the legislature to ensure the production tax credit program's continued success. I therefore urge the committee's favorable approval of HB1982 HD2 SD1 with the MPA's proposed amendments.

Attachment

ATTACHMENT TO MPA TESTIMONY WAM 4/5/2022

HOUSE OF REPRESENTATIVES
THIRTY-FIRST LEGISLATURE, 2022
STATE OF HAWAII

H.B. NO. 1982 H.D. 2 S.D. 1

A BILL FOR AN ACT

RELATING TO TAXES.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF HAWAII:

SECTION 1. Chapter 237, Hawaii Revised Statutes, is amended by adding a new section to be appropriately designated and to read as follows:

"**§237- Withholding of tax by persons claiming the motion picture, digital media, and film production income tax credit.** (a) Every person making payment to a loan-out company and claiming a tax credit pursuant to section 235-17 shall deduct and withhold an amount equal to **the applicable rate** ~~**4.5 per cent**~~ of all payments made to the loan-out company for services performed in the State. The amounts withheld shall be remitted pursuant to subsection (b). The amounts withheld under this section shall be deemed to be a tax withholding for the benefit of the loan-out company's employee performing the service.

(b) Every person subject to subsection (a) shall make a return of the amount withheld and file the return with the department of taxation no later than **the month following** ~~**thirty**~~

~~calendar days from~~ the date on which the payment was made to the loan-out company. The taxes withheld shall be remitted with the return. The department of taxation shall prescribe the forms and procedures to administer this section, including any application processing fees, as necessary.

(c) All taxes withheld pursuant to this section shall be held in trust by the person withholding for the State. If any person required to withhold and remit taxes under this section fails to withhold or remit the taxes, the person shall be liable for the failure as provided in section 235-64."

SECTION 2. Section 237-1, Hawaii Revised Statutes, is amended by adding a new definition to be appropriately inserted and to read as follows:

""Loan-out company" means a wholly-owned entity formed on behalf of a person that serves as a separate entity that constitutes the person's means of entering a contact with a third party for the purpose of providing services to the third party."

SECTION 3. Section 235-17, Hawaii Revised Statutes, is amended to read as follows:

"**§235-17 Motion picture, digital media, and film production income tax credit.** (a) Any law to the contrary notwithstanding, there shall be allowed to each taxpayer subject to the taxes imposed by this chapter, an income tax credit that shall be deductible from the taxpayer's net income tax liability, if any, imposed by this chapter for the taxable year in which the credit is properly claimed. The amount of the credit shall be:

(1) Twenty per cent of the qualified production costs incurred by a qualified production in any county of the State with a population of over seven hundred thousand; or

(2) Twenty-five per cent 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.

A qualified production occurring in more than one county may prorate its expenditures based upon the amounts spent in each county, if the population bases differ enough to change the percentage of tax credit.

In the case of a partnership, S corporation, estate, or trust, the tax credit allowable is for qualified production costs incurred by the entity for the taxable year. The cost upon which the tax credit is computed shall be determined at the entity level. Distribution and share of credit shall be determined by rule.

If a deduction is taken under section 179 (with respect to election to expense depreciable business assets) of the Internal Revenue Code of 1986, as amended, no tax credit shall be allowed for those costs for which the deduction is taken.

The basis for eligible property for depreciation of accelerated cost recovery system purposes for state income taxes shall be reduced by the amount of credit allowable and claimed.

(b) The credit allowed under this section shall be claimed against the net income tax liability for the taxable year. For the purposes of this section, "net income tax liability" means net income tax liability reduced by all other credits allowed under this chapter.

(c) If the tax credit under this section exceeds the taxpayer's income tax liability, the excess of credits over liability shall be refunded to the taxpayer; provided that no refunds or payment on account of the tax credits allowed by this section shall be made for amounts less than $1. All claims, including any amended claims, for tax credits under this section shall be filed on or before the end of the twelfth month following the close of the taxable year for which the credit may be claimed. Failure to comply with the foregoing provision shall constitute a waiver of the right to claim the credit.

(d) To qualify for this tax credit, a production shall:

(1) Meet the definition of a qualified production specified in subsection [~~(m);~~] (n);

(2) Have qualified production costs totaling at least $200,000;

(3) Provide the State a qualified Hawaii promotion, which shall be at a minimum, a shared-card, end-title screen credit, where applicable;

(4) Provide evidence of reasonable efforts to hire local talent and crew;

(5) Provide evidence when making any claim for products or services acquired or rendered outside of this State that reasonable efforts were unsuccessful to secure and use comparable products or services within this State;

(6) Provide evidence of financial or in-kind contributions or educational or workforce development efforts, in partnership with related local industry labor organizations, educational institutions, or both, toward the furtherance of the local film and television and digital media industries[~~.~~] and

(7) Submit to the department of taxation an application processing fee for the motion picture, digital media, and film production income tax credit in an amount equal to one-tenth of a per cent of the tax credit claimed by the qualified production no later than the deadline prescribed in subsection (c); provided that:

(A) The department of taxation may prescribe the form and method by which this fee is remitted, including through electronic means; and

(B) The fees collected under this paragraph shall be:

(i) Capped at $20,000; and

(ii) Deposited into the tax administration special fund established under section 235-20.5.

(e) On or after July 1, 2006, no qualified production cost that has been financed by investments for which a credit was claimed by any taxpayer pursuant to section 235-110.9 is eligible for credits under this section.

(f) To receive the tax credit, the taxpayer shall first prequalify the production for the credit by registering with the department of business, economic development, and tourism during the development or preproduction stage.

(g) The director of taxation shall prepare forms as may be necessary to claim a credit under this section. The director may also require the taxpayer to furnish information to ascertain the validity of the claim for credit made under this section and may adopt rules necessary to effectuate the purposes of this section pursuant to chapter 91.

(h) Every taxpayer claiming a tax credit under this section for a qualified production shall, no later than ninety days following the end of each taxable year in which qualified production costs were expended, submit a written, sworn statement to the department of business, economic development, and tourism[~~, together with a verification review by a qualified certified public accountant using procedures prescribed by the department of business, economic development, and tourism, identifying:~~] that identifies:

(1) All qualified production costs as provided by subsection (a), if any, incurred in the previous taxable year;

(2) The amount of tax credits claimed pursuant to this section, if any, in the previous taxable year; and

(3) The number of total hires versus the number of local hires by category and by county.

This information may be reported from the department of business, economic development, and tourism to the legislature [~~in redacted form~~] pursuant to subsection (i)(4).

(i) The department shall review and approve tax credit final applications within 10 months of receipt and are deemed to be automatically approved if the applications are not approved within 10 months of receipt of the final submission.

~~(i)~~ **(j)** The department of business, economic development, and tourism shall:

(1) Maintain records of the names of the taxpayers and qualified productions thereof claiming the tax credits under subsection (a);

(2) Obtain and total the aggregate amounts of all qualified production costs per qualified production and per qualified production per taxable year;

(3) Provide a letter to the director of taxation specifying the amount of the tax credit per qualified production for each taxable year that a tax credit is claimed and the cumulative amount of the tax credit for all years claimed; and

(4) Submit a report to the legislature no later than twenty days prior to the convening of each regular session detailing the non-aggregated qualified production costs that form the basis of the tax credit claims and expenditures, itemized by taxpayer, in a redacted format to preserve the confidentiality and which shall include the dollar amount claimed, name of company, and name of the qualified production of the taxpayers claiming the credit.

Upon each determination required under this subsection, the department of business, economic development, and tourism shall issue a letter to the taxpayer, regarding the qualified production, specifying the qualified production costs and the tax credit amount qualified for in each taxable year a tax credit is claimed. The taxpayer for each qualified production shall file the letter with the taxpayer's tax return for the qualified production to the department of taxation. Notwithstanding the authority of the department of business, economic development, and tourism under this section, the director of taxation may audit and adjust the tax credit amount to conform to the information filed by the taxpayer.

~~(j)~~ **(k)** Total tax credits claimed per qualified production shall not exceed $15,000,000.

~~(K)~~ **(l)** Qualified productions shall comply with subsections (d), (e), (f), and (h).

~~(l)~~ (m) The total amount of tax credits allowed under this section in any particular year shall be $50,000,000; however, if the total amount of credits applied for in any particular year exceeds the aggregate amount of credits allowed for [~~such~~] that year under this section, the excess shall be treated as having been applied for in the subsequent year and shall be claimed in [~~such~~] the subsequent year; provided that no excess shall be allowed to be claimed after December 31, [~~2025.~~] 2032.

~~(m)~~ (n) Every person making payment to a loan-out company shall withhold an amount equal to **.5** ~~**4.5**~~ per cent of qualified production costs for services performed in the State; provided that the amount withheld shall be remitted to the department of taxation to the credit of the general excise tax account of the loan-out company to whom the qualified production costs were paid or will be paid. The amount withheld shall be remitted **on the 20th day following the close of the month** ~~**no later than thirty calendar days**~~ after the qualified production costs are paid or incurred. Taxpayers who fail to comply with this subsection shall be subject to the applicable interest and penalties pursuant to chapter 231 and section 235-104.

[~~(m)~~] ~~(n)~~ **(o)** For the purposes of this section:

"Commercial":

(1) Means an advertising message that is filmed using film, videotape, or digital media, for dissemination via television broadcast or theatrical distribution;

(2) Includes a series of advertising messages if all parts are produced at the same time over the course of six consecutive weeks; and

(3) Does not include an advertising message with Internet-only distribution.

"Digital media" means production methods and platforms directly related to the creation of cinematic imagery and content, specifically using digital means, including but not limited to digital cameras, digital sound equipment, and computers, to be delivered via film, videotape, interactive game platform, or other digital distribution media.

"Post-production" means production activities and services conducted after principal photography is completed, including but not limited to editing, film and video transfers, duplication, transcoding, dubbing, subtitling, credits, closed captioning, audio production, special effects (visual and sound), graphics, and animation.

"Production" means a series of activities that are directly related to the creation of visual and cinematic imagery to be delivered via film, videotape, or digital media and to be sold, distributed, or displayed as entertainment or the advertisement of products for mass public consumption, including but not limited to scripting, casting, set design and construction, transportation, videography, photography, sound recording, interactive game design, and post-production.

"Qualified production":

(1) Means a production, with expenditures in the State, for the total or partial production of a feature-length motion picture, short film, made-for-television movie, commercial, music video, interactive game, television series pilot, single season (up to twenty-two episodes) of a television series regularly filmed in the State (if the number of episodes per single season exceeds twenty-two, additional episodes for the same season shall constitute a separate qualified production), television special, single television episode that is not part of a television series regularly filmed or based in the State, national magazine show, or national talk show. For the purposes of subsections

(d) and (j), each of the aforementioned qualified production categories shall constitute separate, individual qualified productions; and

(2) Does not include:

(A) News;

(B) Public affairs programs;

(C) Non-national magazine or talk shows;

(D) Televised sporting events or activities;

(E) Productions that solicit funds;

(F) Productions produced primarily for industrial, corporate, institutional, or other private purposes; and

(G) Productions that include any material or performance prohibited by chapter 712.

"Qualified production costs" means the costs incurred by a qualified production within the State that are subject to the general excise tax under chapter 237 or income tax under this chapter and that have not been financed by any investments for which a credit was or will be claimed pursuant to section 235-110.9. Qualified production costs include but are not limited to:

(1) Costs incurred during preproduction such as location scouting and related services;

(2) Costs of set construction and operations, purchases or rentals of wardrobe, props, accessories, food, office supplies, transportation, equipment, and related services;

(3) Wages or salaries of cast, crew, and musicians;

(4) Costs of photography, sound synchronization, lighting, and related services;

(5) Costs of editing, visual effects, music, other post-production, and related services;

(6) Rentals and fees for use of local facilities and locations, including rentals and fees for use of state and county facilities and locations that are not subject to general excise tax under chapter 237 or income tax under this chapter;

(7) Rentals of vehicles and lodging for cast and crew;

(8) Airfare for flights to or from Hawaii, and interisland flights;

(9) Insurance and bonding;

(10) Shipping of equipment and supplies to or from Hawaii, and interisland shipments; and

(11) Other direct production costs specified by the department in consultation with the department of business, economic development, and tourism;

provided that any government-imposed fines, penalties, or interest that are incurred by a qualified production within the State shall not be "qualified production costs"."

SECTION 4. Section 235-20.5, Hawaii Revised Statutes, is amended to read as follows:

"**§235-20.5 Tax administration special fund; established.** (a) There is established a tax administration special fund, into which shall be deposited:

(1) Fees collected under sections 235-20 and 235-110.9;

(2) Revenues collected by the special enforcement section pursuant to section 231-85; provided that in each fiscal year, of the total revenues collected by the special enforcement section, all revenues in excess of $2,000,000 shall be deposited into the general fund; [~~and~~]

(3) Fines assessed pursuant to section 237D-4[~~.~~]; and

(4) Application processing fees collected under section 231-36.8 and 237- .

(b) The moneys in the fund shall be used for the following purposes:

(1) Issuing comfort letters, letter rulings, written opinions, and other guidance to taxpayers;

(2) [~~Issuing certificates under [section] 235-110.9;~~] <u>Processing qualified production applications for the motion picture, digital media, and film production income tax credit provided under sections 235-17 and 237- ;</u>

(3) Administering the operations of the special enforcement section;

(4) Funding support staff positions in the special enforcement section; and

(5) Developing, implementing, and providing taxpayer education programs, including tax publications."

SECTION 5. The department of taxation may establish four full-time equivalent (4.0 FTE) tax auditor positions to examine claims for the motion picture, digital media, and film production income tax credit pursuant to section 235-17, Hawaii Revised Statutes, and other tax expenditures.

SECTION 6. Statutory material to be repealed is bracketed and stricken. New statutory material is underscored.

SECTION 7. This Act shall take effect on July 1, 2050.

Report Title:
Motion Picture, Digital Media, and Film Production Tax Credit; Loan-out Companies; Qualified Productions; Withholdings; Tax Administration Special Fund; Positions

Description:
Requires every person making payment to a loan-out company and claiming the film tax credit to withhold payments to loan-out companies. Removes the requirement for productions to submit a verification review by a qualified certified public accountant

using procedures prescribed by the Department of Business, Economic Development, And Tourism (DBEDT) when applying for the film tax credit. Requires the report by DBEDT to include the dollar amount claimed, name of the company, and name of the qualified production of the taxpayer. Extends the period during which excess income tax credits may be claimed to 12/31/2032. Requires qualified taxpayers to withhold a certain amount and remit that amount. Amends the use of the tax administration special fund. Authorizes the Department of Taxation to establish four full-time equivalent tax auditor positions. Effective 7/1/2050. (SD1)

TAX FOUNDATION OF HAWAII

126 Queen Street, Suite 305 Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: INCOME, GENERAL EXCISE, ADMINISTRATION, Withholding of Tax by Persons Claiming Film Credit

BILL NUMBER: HB 1982 SD 1

INTRODUCED BY: Senate Committee on Energy, Economic Development, and Tourism

EXECUTIVE SUMMARY: Requires every person making payment to a loan-out company and claiming the film tax credit to withhold payments to loan-out companies. Removes the requirement for productions to submit a verification review by a qualified certified public accountant using procedures prescribed by the Department of Business, Economic Development, And Tourism (DBEDT) when applying for the film tax credit. Requires the report by DBEDT to include the dollar amount claimed, name of the company, and name of the qualified production of the taxpayer. Extends the period during which excess income tax credits may be claimed to 12/31/2032. Requires qualified taxpayers to withhold a certain amount and remit that amount. Amends the use of the tax administration special fund. Authorizes the Department of Taxation to establish four full-time equivalent tax auditor positions.

SYNOPSIS: Adds a new section to chapter 237, HRS, requiring every person claiming a credit under section 235-17, HRS, to withhold 4.5% of all payments to loan-out companies for services performed in Hawaii and to remit the withholding to the Department of Taxation within 30 days from the date of payment.

Amends section 237-1, HRS, by adding a new definition of “loan-out company” as a wholly-owned entity formed on behalf of a person that serves as a separate entity that constitutes the person's means of entering a contact with a third party for the purpose of providing services to the third party.

Amends section 235-17, HRS, to add a provision allowing the department of taxation to charge a processing fee of 0.1% of the credit claimed on the application, with the fee to be deposited in the tax administration special fund.

Amends section 235-17(h), HRS, to delete the requirement of a review of the expenses claimed on the credit application by a CPA firm.

Makes additional technical and conforming amendments.

EFFECTIVE DATE: July 1, 2050

STAFF COMMENTS:

Withholding Income Tax for Payments to Loan-Out Companies: Apparently, this provision is meant to collect tax at the source because employees of loan-out companies have not been following the requirement to file a general excise tax return. At present, this provision appears twice, once in section 235-17, HRS, and once in a new section to be added to chapter 237. We recommend that one of the references be stripped of substantive language and replaced with a cross-reference to the other, with all substantive language consolidated into one location.

User Fee for Credit Application: For the application fee to be a legitimate user fee, there must be some linkage between the fee amount and the amount it is going to cost the Department to process the application. Percentages are rarely justifiable in this context.

Tax Administration Special Fund: The Tax Administration Special Fund was established by Act 215 of 2004, one of the major purposes of which was to rein in the High Technology Business Investment Credit, a whopping incentive for the high technology industry and others that was rapidly spiraling out of control. The thought at the time was that because the Department of Taxation was spending a lot of time issuing rulings on the applicability of the credits, the Department should be allowed to charge user fees for the rulings and thereby pay for a few more bodies to review the cases and pump out the rulings. The special fund was enacted for that purpose. Its authorizing statute was placed in the Income Tax Law because the high technology credit was an income tax credit.

In 2009, Act 134 created a special enforcement section within the Department that was primarily targeting "cash economy" transactions, typically those where the buyer pays in cash and the seller "conveniently forgets" to pay General Excise Tax (GET). This Act amended the special fund statute so that whatever the special enforcement section brought in the door, up to $500,000, would go to the special fund; any more would go to the general fund like most tax collections. The fund was then allowed to pay for the employees in the special enforcement section.

In 2015, Act 204 enacted new compliance requirements aimed at transient vacation rentals, such as bed and breakfast operators who "conveniently forget" to pay both GET and transient accommodations tax (TAT). The bill imposed fines upon those who failed to comply, and allowed those fines to go into the special fund.

At this point, the fund was fed by activity relating to the income tax, the GET, and the TAT, but the statute authorizing the fund remained in the Income Tax Law.

On the expense side, the Department apparently found itself with too much money in the special fund, so it asked the legislature for authority to spend the fund money on taxpayer education programs and publications. That bill breezed through the legislature and became Act 89, SLH 2014. In the meantime, different acts through the years allowed DOTAX to hoard more money and fund more positions, increasing the special enforcement section collection threshold from $500,000 to $700,000 (Act 204, SLH 2015) to $2 million (Act 123, SLH 2018).

In the Office of the Auditor Report No. 17-10, the Auditor reviewed the Tax Administration Special Fund and found that its ending balance had started rising significantly, from just under $1 million in FY2013 to $5.7 million in FY2017.

In Act 87, SLH 2021, the Legislature found that this fund had accumulated significant monies in excess of its requirements and authorized raiding the fund to the tune of $15 million.

Allowing this fund to swell further is not good policy. Tax collections, from whatever source, are government realizations under the law imposing the tax. Penalties and fines are treated as additional taxes (see, for example, section 231-39(b), HRS, providing that penalties “shall be added to and become a part of the tax imposed by such tax or revenue law, and collected as such”). These tax collections rightfully belong to the general fund. Allowing them to get swept into special funds, no matter which department, program, or service “owns” the special fund, is a subversion of the budgeting and appropriation processes. Special funds should not be allowed to spiral out of control. The fact that this fund was deemed worthy of a $15 million raid just last year indicates that it was out of control and should be reined in, not allowed to spiral further and faster.

Digested: 4/3/2022

HB-1982-SD-1
Submitted on: 4/3/2022 7:38:47 AM
Testimony for WAM on 4/5/2022 10:15:00 AM

Submitted By	Organization	Testifier Position	Testify
Ty Sanga	Individual	Support	Written Testimony Only

Comments:

Aloha,

My name is Ty Sanga and I am a Native Hawaiian filmmaker that has been working in the industry for the past 15 years.

I support HB1982 and request your consideration of an amendment to reduce the amount of production costs necessary to qualify for the tax credit from $200,000 to $100,000. This would incentivize more LOCAL INVESTMENT into LOCAL filmmakers, writers, directors, producers, and other technical support positions - thus, helping to grow our LOCAL film production industry.

HB-1982-SD-1
Submitted on: 4/3/2022 1:45:02 PM
Testimony for WAM on 4/5/2022 10:15:00 AM

Submitted By	Organization	Testifier Position	Testify
Ann Chung	Individual	Support	Written Testimony Only

Comments:

Support HB1982 and request your consideration of an amendment to reduce the amount of production costs necessary to qualify for the tax credit from $200,000 to $100,000. This would incentivize more LOCAL INVESTMENT into LOCAL filmmakers, writers, directors, producers, and other technical support positions - thus, helping to grow our LOCAL film production industry.

Possible amendment to Section 4(d)(2) or simply change the threshold to $100,000.

(2) Have qualified production costs totaling at least $200,000; Except in instances where the writer, director, and producer are Hawai'i State residents, and have been residents for at least 5 years prior. In those instances, a production shall have qualified production costs totaling at least $100,000.

Mahalo for your consideration.

HB-1982-SD-1
Submitted on: 4/3/2022 4:54:34 PM
Testimony for WAM on 4/5/2022 10:15:00 AM

Submitted By	Organization	Testifier Position	Testify
Laiana Kanoa-Wong	Individual	Support	Written Testimony Only

Comments:

Aloha kākou,
My name is Lāiana Kanoa-Wong and I am a Hawaiian filmmaker and a partner in a Hawaiian owned Production company. I support HB1982 and request your consideration of an amendment to reduce the amount of production costs necessary to qualify for the tax credit from $200,000 to $100,000. This would incentivize more LOCAL INVESTMENT into LOCAL filmmakers, writers, directors, producers, and other technical support positions - thus, helping to grow our LOCAL film production industry. Mahalo for your consideration.
Aloha 'Āina,
Lāiana Kanoa-Wong

HB-1982-SD-1
Submitted on: 4/3/2022 8:31:18 PM
Testimony for WAM on 4/5/2022 10:15:00 AM

Submitted By	Organization	Testifier Position	Testify
Ciara Leinaala Kwock	Individual	Support	Written Testimony Only

Comments:

As a local, independent filmmaker, I support HB1982 and request your consideration of an amendment to reduce the amount of production costs necessary to qualify for the tax credit from $200,000 to $100,000. This would incentivize more LOCAL INVESTMENT into LOCAL filmmakers, writers, directors, producers, and other technical support positions - thus, helping to grow our LOCAL film production industry. I have personally found it difficult to reach the minimum requirement on my projects, and would very much benefit from the kind of support that outside studios and companies-- with more resources than me -- receive.

Thank you for your consideration!

HB-1982-SD-1
Submitted on: 4/3/2022 9:28:16 PM
Testimony for WAM on 4/5/2022 10:15:00 AM

Submitted By	Organization	Testifier Position	Testify
Kekama	Individual	Support	Written Testimony Only

Comments:

Aloha:

My name is Scott W. Kekama Amona; I have worked in the film industry for the past 10 years for large network television, large studio and streaming film, and smaller independent productions. I am also a writer, director, producer invested in creating more local content for local and worldwide audeinces.

Working in the film industry has been very rewarding for me and my family and is one of the few business in the islands that has continued on during the pandemic. It continues to thrive and invest millions of dollars into the local economy and will continue to do so.

I support HB1982 and request your consideration of an amendment to reduce the amount of production costs necessary to qualify for the tax credit from $200,000 to $100,000. This would incentivize more LOCAL INVESTMENT into LOCAL filmmakers, writers, directors, producers, and other technical support positions - thus, helping to grow our LOCAL film production industry.

Mahalo piha,

Scott W. Kekama Amona

HB-1982-SD-1
Submitted on: 4/4/2022 9:10:29 AM
Testimony for WAM on 4/5/2022 10:15:00 AM

Submitted By	Organization	Testifier Position	Testify
Amber Espinosa-Jones	Individual	Support	Written Testimony Only

Comments:

I work for Sundance Institute and have been a diversity and inclusion professional in the film industry for over 5 years.

I support HB1982 and request your consideration of an amendment to reduce the amount of production costs necessary to qualify for the tax credit from $200,000 to $100,000. This would incentivize more LOCAL INVESTMENT into LOCAL filmmakers, writers, directors, producers, and other technical support positions - thus, helping to grow our LOCAL film production industry.