

June 5, 2019

Honorable Mike Crapo
Honorable Ben Cardin
Co- Leads
Senate Finance Committee
Cost Recovery Task Force
Washington D.C.

Re: Independent Film and Television Alliance Submission to the Senate Finance Committee Cost Recovery Task Force on domestic film and television production incentives

The Independent Film & Television Alliance (IFTA) represents **more than 145 companies**, the majority of which are **small to medium-sized U.S.-based businesses**¹ that have financed, produced and distributed many of the world's most prominent films, including over 60% of the Academy Award® winners for "Best Picture" since the Association was formed in 1980, including this year's Best Picture, *Green Book*.

Independents are companies that organize the financing, production, and exploitation of films and television programming relying primarily on outside sources and on third party distributors in each territory and for each medium in which the project is distributed. This is in sharp contrast to many of the major players in the industry, who are able to self-finance and who own or control their own distribution outlets worldwide. Since independents bankroll the projects and engage in the lengthy process of production and securing distribution to reach the worldwide audience, cash flow is always an issue. IFTA has supported **IRC Section 181** since its inception and continues to advocate for its permanent extension because Section 181 addresses this need and serves a fundamental purpose in encouraging the U.S. independent production industry to remain in the U.S. Section 181 has resulted in enhanced U.S. economic activity, jobs and exports to worldwide marketplaces.

Last year's amendment of **IRC Section 168(k)** to provide bonus depreciation to film and television investment was a significant event for our industry – but as more fully explained below, it did not achieve Congress' purpose of consolidating Section 181's benefits into the more extensive bonus depreciation provisions.

As the Task Force on Cost Recovery considers the extension of Certain Temporary and Disaster Relief Tax Provisions², IFTA asks the Task Force to keep in mind that Section 181 was not made redundant by new Section 168(k) because of the difference in the type of depreciation treatment (accelerated versus bonus) and when the depreciation can begin.

¹ A complete list of IFTA Members is available online at: <http://www.ifta-online.org>.

² <https://www.jct.gov/publications.html?func=startdown&id=5188> at Page 33.

IFTA urges the Task Force to recommend the following regarding the two incentives for U.S. domestic production:

(1) The extension of **IRC Section 181** *retroactively* for 2018 and *prospectively* for 2019 (and to make this tax incentive permanent) to provide much needed stability and certainty for the film and television industry. Section 181 was the clearest and most effective tax incentive offered to independent producers and should be made a permanent part of the tax code.

(2) A clarification to be made to **IRC Section 168(k)** as amended last year regarding the “placed in service” language³ since independent producers do not control their own distribution.

We thank the Committee Members and Task Forces for their thoughtful approach in gathering information on these tax incentives and how each has and will impact U.S. independent production activities, contribute to the U.S. domestic economy and grow the independent sector’s already sizable contribution to net exports of intellectual property. IFTA provides more information below regarding the success of Section 181 and the need to extend it permanently based on the economic and creative output that has occurred since its enactment in 2004. The submission also provides information on a necessary clarification needed to Section 168(k) so that independents can meaningfully use that incentive. Of course, Section 181 provides that it is an election of tax treatment, so there is no double dipping as between the two incentives.

The Success of IRC Section 181 and its Positive Impact on the Independent Film and Television Industry and the U.S. Economy

Congress enacted **Section 181** of the Internal Revenue Code in 2004 as part of the *Jobs Act* with a singular focus to provide a federal tax incentive designed to encourage independent film and television production to remain in the United States. Congress has approved the extension of the provision six times, most recently by the Bipartisan Budget Act recognizing that the independent sector is responsible for over 70% of all films produced in the U.S. each year and the jobs generated by that economic activity, but is often hindered by a lack of up-front cash and reliance on third-party investment and distribution. **Section 181** allowed production entities in the U.S. to immediately expense qualifying production costs up to \$15 million (up to \$20 million in certain circumstances) in the year incurred. *It worked!*

Since its enactment and continued extensions, Section 181 has proved to be of real value in keeping independent production and jobs here in the U.S. For calendar year 2018, U.S. independent production companies shot 507 feature films. This resulted in 35,967 full time jobs directly related to this production activity and another 108,455 full time jobs for the various vendors that service the film industry. Combined, both classes of employees earned over \$15.14 billion. Total business revenue that resulted from this production activity totaled nearly \$23.12 billion in economic output. Independent production generated over \$3.15 billion in income and sales tax for both the federal government and individual state governments. Federal government share of income tax received was nearly \$1.99 billion. Just as importantly, U.S. independent producers were responsible for \$2.3 billion in exports to the worldwide marketplace.

³ As defined in Section 168(k) and comparable to a provision in the Treasury Regulations (26 CFR §1-181.1)

Section 181's costs were modest since it merely accelerated those deductions (otherwise subject to depreciation over the film or television program's income generating life), but offered a significant stimulus for independents to keep production in the U.S. and to give small businesses the cash flow to keep producers investing in new production and keep production crews working.

IRC Section 181 is the Preferable Incentive for Independents Because Independent Producers Do Not Control Their Own Distribution, and 'Accelerated Depreciation' is More Desirable than 168(k)'s 'Bonus Depreciation'

Our industry welcomes Congress' inclusion of film and television programming in amended Section 168(k) of the Tax Cuts and Jobs Act, acknowledging that investment in these productions generates long-term economic value and thus should qualify for 'bonus depreciation.' However, as currently drafted, amended Section 168(k) does not succeed in continuing the unique benefits of Section 181 for independent film and television producers because it ties the availability of depreciation deductions to the date when the qualifying film or television program is placed in service, *i.e.*, "at the time of initial release or broadcast" – which legislative history notes to be "first commercial release" – a test borrowed from a provision in the Treasury Regulations (26 CFR §1-181.1) relating to other issues (not limiting the date on which deductions are taken). This is in sharp contrast to the provisions of Section 181 which allowed the producer to elect to accelerate depreciation to the year of production expenditure.⁴

For independents, there is often a substantial period of time between when production funds are spent and when the film or television program is eventually released. From production to release may be a year or more apart while the producer is accumulating more costs and debt and for which the **cash flow benefit of Section 181 provided necessary relief.**

Additionally, in contrast to the large, integrated major studios, independent producers in general do not own exhibition or distribution outlets and cannot control when the "initial release or broadcast" will occur. As a result, for example, a producer of six television episodes may find that only a few are scheduled by the broadcast network in year one while others are deferred until a different season. Similarly, a film producer may find that his movie's release is delayed for many months (and another tax year) in consequence of the booking schedule established by third party distributors⁵.

IFTA does not anticipate that these fundamental characteristics of the independent sector will change in the future so **securing IRC Section 181 on a permanent basis and advocating for an adjustment in Section 168(k) are the top priorities for IFTA Members and the independent production community at large.**

⁴ It is also inconsistent with the treatment of other assets subject to Section 168, which are deemed placed in service when first acquired (irrespective of when revenue is generated) or when first in a condition to be used or sold such as manufacturing equipment.

⁵ Moreover, for independents, pinning depreciation deductions on the date of "initial release" is not an "acceleration". In contrast to the major studios, independents earn the majority of their revenue very quickly after they complete and deliver their films and programs to their distributors (buyers). This reflects the use of third-party licensing in which distributors make upfront payments on the date of delivery against the estimated total royalties for the life- time of their exploitation period. Thus, using the income forecast method under Section 167, independents typically generate most depreciation at or near the date of "initial release" in any event.

A Possible Fix for IRC Section 168(k)

As noted, independent producers were intended beneficiaries of Section 181 at its inception and there is ample reason to believe that the Senate proposal (and final language in TCJA Public Law No: 115-97) to integrate Section 181 into 168(k) was expected to extend those same benefits to independents as to major studios equally going forward. But that can only be accomplished by **amending the relevant provisions to achieve that purpose and by doing so in a manner that meets the needs of both large and small producers.**

These objectives can be achieved in either of two alternate ways:

First, by extending Section 181 permanently (by deleting Section 181(g)). Pursuant to Section 181(b)-(c), a taxpayer that elects treatment of production costs under Section 181 also foregoes other depreciation and amortization of those costs, so this “fix” obviates the necessity for further amendments of the Code. **This result can also be achieved by amending Section 168(k) to also incorporate the provisions of Section 181 as an alternative to bonus depreciation, by election of the taxpayer.** This mirrors the treatment of certain other sectors.

OR

Second, by amending Section 168(k)(2)(H) as follows:

(H) Production placed in service

For purpose of subparagraph (A) **(i) a qualified film or television production shall be considered to be placed in service at the time costs of the production are first incurred [delete: of initial release or broadcast];**

Conclusion

IRC Section 181 must be extended and made permanent to preserve the critical benefits of ‘accelerated depreciation’ of qualifying production costs as they are incurred, paving the way for independents to continue to fuel U.S. film and television production and protect the tens of thousands of employees in our sector, along with the economic contribution of independent production in communities throughout the country.⁶ While the intent of the TCJA drafters to re-write Section 168(k) to meet the needs of investors in productive assets, including film and television, was clear, unfortunately the “placed in service” language erects a barrier for independent producers to access that benefit. IRC 168(k) would need to be fixed in order to meaningfully include the independent sector. Both incentives should be available to independent producers so that they may elect what’s best for each qualifying production.

⁶ Independent films are shot all over the country and in many instances have fueled the rise of new industry hubs. Currently, the top 10 states for independent film production are: 1. California, 2. New York, 3. Georgia, 4. Texas, 5/6. Illinois & Louisiana (tie), 7. Ohio, 8/9. Alabama & Massachusetts (tie), and 10/11. Florida & New Mexico (tie)