

Guidelines for the Virginia Motion Picture Production Tax Credit

Introduction

House Bill 861 and Senate Bill 257 (2010 *Acts of Assembly*, Chapters 418 and 599) established the Virginia Motion Picture Production Tax Credit. According to the Acts, qualifying motion picture production companies are eligible to receive a series of refundable individual and corporate income tax credits for taxable years beginning on and after January 1, 2011, in the aggregate amount of \$2.5 million for the 2010-2012 biennium and \$5 million for any biennium thereafter.

These guidelines are issued by the Department of Taxation ("the Department") to provide guidance to taxpayers regarding the Virginia Motion Picture Production Tax Credit. These guidelines are exempt from the provisions of the Administrative Process Act (*Va. Code* § 2.2-4000 *et seq.*) according to the provisions outlined in *Va. Code* § 58.1-439.12.03. These guidelines supersede the Guidelines and Rules for the Virginia Motion Picture Production Tax Credit issued by the Department on December 21, 2010 (Public Document 10-281). As necessary, additional guidelines will be published and posted on the Department's website, www.tax.virginia.gov.

These guidelines represent the Department of Taxation's interpretation of the relevant laws. They do not constitute formal rulemaking and hence do not have the force and effect of law or regulation. In the event that the final determination of any court holds that any provision of these guidelines are contrary to law, taxpayers who follow these guidelines will be treated as relying on erroneous written advice for purposes of waiving penalty and interest under *Va. Code* §§ 58.1-105, 58.1-1835 and 58.1-1845. To the extent there is a question regarding the application of these guidelines, taxpayers are encouraged to write to the Department and seek a written response to their question.

Description of Credits Available

Base-Income Tax Credit: The base credit available is 15 percent of all qualifying expenses (including wages), with a bonus of 5 percent if the production is filmed in an economically distressed area of the Commonwealth, making the total base credit available up to 20 percent of qualifying expenses.

Additional Virginia Resident Credit: The production company is allowed an additional credit of 10 to 20 percent of aggregate payroll for Virginia residents employed in connection with the motion picture production. For companies that spend at least \$250,000 in total production costs in the Commonwealth, but not more than \$1 million, the credit will equal 10 percent of the total Virginia resident aggregate payroll. For companies that spend over \$1 million in total production costs in the Commonwealth, the credit will equal 20 percent of the total aggregate Virginia resident payroll.

Additional Virginia Resident First-Time Industry Employee Credit: In addition to the above outlined credits, companies may claim a credit of 10 percent of their total

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aggregate payroll for Virginia residents who are employed as first time actors or first time members of a production crew in connection with a production in Virginia.

Credits available through the Virginia Motion Picture Production Tax Credit are offered in addition to other Virginia production incentives. For additional information regarding all available funding assistance for Virginia productions, please refer to the Virginia Film Office's ("VFO") website (<http://FilmVirginia.org>).

Definitions

"Actor" means an individual paid by the production company for performing a role in Virginia, including, but not limited to, featured actors, stunt performers, voice-over talent, hosts, judges, announcers and roles or performers that appear on a recurring basis.

"Amounts Spent in the Commonwealth" means, in the case of tangible property, expenses for goods and materials purchased or leased from a qualified vendor that are actually and physically provided, supplied, consumed or used within Virginia and, in the case of services, means expenses for services performed within Virginia.

"Certification Letter" means a document issued by the VFO upon completion of a qualified production reflecting the credit amount to be allocated to the production company.

"Commercial Advertisement" means advertisements recorded on film, videotape or digital medium for multi-market distribution which extends outside the state of Virginia by way of broadcast television networks, cable, satellite, Internet, DVD, home video or motion picture theaters. Branding, marketing, promotion and/or e-advertising campaigns do not qualify. Certain animated productions may qualify.

"Compensation and Wages" means "wages" as defined in § 3401 of the Internal Revenue Code. Payment methods may include, but are not limited to, direct payments or indirect payments such as payments through an agent or agency, or payments through a personal service company or an employee leasing company that pays the individual.

"Credit Allocation Letter of Intent" means a document issued by the VFO after receipt and approval of a production company's initial application outlining the terms and conditions of the credit, which shall include the maximum amount of credits to be received by a production company based on an estimate of qualifying expenses.

"Digital Interactive Media Production" means any interactive entertainment intended for commercial exploitation, including, but not limited to:

- Video game projects;
- Console games;

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- Computer games;
- Handheld console games;
- Mobile electronic device games; and
- Massively multi-player online video games (MMOG) and virtual worlds that meet the requirement of multi-market distribution via the Internet or any other channel of exhibition.

“Economically Distressed Area” means an area designated as such by the Virginia Economic Development Partnership.

“Employed for the First Time as an Actor or Member of a Production Crew” means receiving compensation and wages for the first time in Virginia as either an actor or as a member of the production crew as verified by the VFO.

“Employed in Connection with the Production of a Film in the Commonwealth” means any individual listed on a production company’s payroll for the production for which the production company is receiving the credit.

“Employee Leasing Company” means a business, which by agreement and for a fee, places employees of a client company on the leasing company's payroll. In turn, the leasing company "leases" these employees back to their original employer, usually for an unlimited period of time.

“Episodic Television Series” means a television program consisting of multiple episodes of a single season. For the purpose of these Guidelines, an entire season of episodes shall be deemed one motion picture production.

“Filmed” means the creation or digital manipulation of a moving image project; the actual production activity for various industry segments:

- For a live action feature film, television program, or commercial project, the production of the project involving the capture of images by a camera;
- For an animated feature film, television program, or commercial, the creation of computer generated digital images or the use of a camera to film with stop motion or time lapse photography;
- For a video game, the use of computers or software to create interactive digital images and visual effects; and
- For a visual effects project, the finishing of a feature film, television program, or commercial with the creation of visual effects including, but not limited to, editing, visual effects, sound effects, music or animation.

“Filmed in the Commonwealth” means a motion picture production that has made best faith efforts to film at least 50 percent of its principal photography days within the Commonwealth.

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“Goods and Services” means physical products and services domiciled and used in Virginia that are directly attributable to the production of a project including, but not limited to, contractors, subcontractors and service providers, and product or equipment purchases, rentals, and leases. For goods with a purchase price of \$25,000 or more, the amount included in qualifying expenses is the purchase price less the fair market value of the good at the time the production is completed.

Example: Elite Motion Pictures purchases a new car for \$50,000 to be used as a prop on the set of their movie for filming. At the completion of production, the car’s value has depreciated to \$40,000. Elite Motion Pictures may only report \$10,000 worth of expenses for the cost of the car to qualify for the credit.

“Member of a Production Crew” means persons employed as production staff or on-set technicians, including, but not limited to, accountants, coordinators, secretaries, camera, casting, construction, costume, electric, editing, grip, location, hair, make-up, props, swing gang, set decorating, sound, special effects, transportation, and visual effects.

“Memorandum of Understanding” means a document issued by the VFO to be signed by both the VFO and the production company as an agreement of the terms and conditions that must be met in order for the production company to receive the tax credits.

“Motion Picture Production” means any recorded audio-visual project using a series of moving images intended for distribution or commercial use including, but not limited to, feature films, episodic television series, commercials, etc. On January 1, 2013, this term will include digital interactive media productions. “Film”, “production”, and “project” mean the same as “motion picture production” for the purpose of these Guidelines.

“Motion Picture Production Company” means any individual, corporation, partnership, electing small business corporation (S corporation), limited liability company, or other form of business association producing a motion picture production. For purposes of determining whether a company qualifies to receive the Virginia Motion Picture Production Tax Credit, an entity that is at least 80 percent owned by a motion picture production company and which is required to file a Virginia income tax return may also be considered a motion picture production company if the memorandum of understanding between the VFO and the production company designates such entity as the company that will receive the credit. “Production company” shall mean the same as “motion picture production company” for the purpose of these Guidelines.

“Obscene Material” means any material which, considered as a whole, has as its dominant theme or purpose an appeal to the prurient interest in sex, that is, a shameful or morbid interest in nudity, sexual conduct, sexual excitement, excretory functions or products thereof or sadomasochistic abuse, and which goes substantially beyond

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customary limits of candor in description or representation of such matters and which, taken as a whole, does not have serious literary, artistic, political or scientific value.

“Personal Service Company” means a business that is a qualified personal services corporation under § 448(d)(2) of the Internal Revenue Code.

“Political Advertising” means advertising whose central focus is the marketing of ideas, attitudes, and concerns about public issues, including political concepts and political candidates.

“Post Production” means the period of physical production that occurs at the completion of production (principal photography), including, but not limited to, editing, sound editing and mixing, music, visual effects and animation.

“Pre-Production” means the period of physical production that occurs before the start of principal photography, but after the project has received a Credit Allocation Letter of Intent. This includes, but is not limited to, activities such as location scouting, hiring of crew members, and establishment of a dedicated production office.

“Principal Photography” means the phase of production during which the motion picture production is actually being filmed or created.

“Production” means the period encompassing pre-production, principal photography, and post production.

“Qualified Motion Picture Production” means a production that has been certified by the VFO as fully meeting the initial requirements for the credit and had received a Credit Allocation Letter of Intent.

“Qualified Vendor” means any individual, partnership, corporation, limited liability company or other business entity that 1) provides goods and services that it provides in its ordinary course of business to a qualified motion picture during production; 2) maintains a physical place of business in Virginia; and 3) is qualified to do business in Virginia.

“Qualifying Expenses” means the sum of actual amounts spent in the Commonwealth by a production company in connection with the production of a motion picture filmed in the Commonwealth for certain goods and services leased or purchased and certain compensation and wages as approved by the VFO. Examples of qualifying expenses include, but are not limited to:

- Resident and non-resident cast and crew wages (less than or equal to \$1 million per individual);
- Accommodations;
- Costs of set construction and operations;
- Editing and related services;

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- Photography;
- Sound synchronization;
- Lighting;
- Wardrobe; makeup and accessories;
- Film processing;
- Sound mixing;
- Special and visual effects;
- Music;
- Location fees;
- Purchase and rental of facilities and equipment;
- Licensing, registration, and permitting fees;
- Costs associated with the independent certified public accountant's report ; and
- Any other production expense for which taxes are assessed or imposed by the state and is approved by the VFO.

Examples of non-qualifying expenses include:

- Wages or compensation in excess of \$1 million paid to individuals for personal services with respect to a single production (in such cases, only the first \$1 million of salary is considered a qualifying expense.);
- Development costs, marketing and promotion expenses, distribution expenses, or any expenses incurred prior to pre-production or after post production of a feature film, television production or video game; and
- Any expenditures made or incurred outside the Commonwealth of Virginia.

“Reality Television Production” means a television production depicting real events and non-actors through actual footage which presents persons engaged in seemingly unscripted situations; no fictional characters are created.

“The Department” means the Virginia Department of Taxation.

“VFO” means the Virginia Film Office.

“Virginia Resident” means an individual domiciled in Virginia at any time during the taxable year and every other individual who, for an aggregate of more than 183 days of the taxable year, maintained his place of abode within Virginia, whether domiciled in Virginia or not.

Production Eligibility Requirements

These are the minimum requirements a production company must complete to be eligible for the tax credit.

A production company may be eligible for the credit if it:

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- Satisfactorily completes the initial application (found on the VFO website, <http://FilmVirginia.org>);
- Meets all deadlines outlined by the VFO; and
- Completes all of the requirements specified in the memorandum of understanding.

A production company must also meet the following requirements:

- Spends at least \$250,000 in “qualifying expenses;”
- Makes a best faith effort to film at least 50 percent of principal photography in the Commonwealth;
- Agrees to contain a ‘filmed in Virginia’ credit and Virginia logo in the final production;
- Is fully funded with a multi-market distribution contract, without taking into account the value of the tax credits; and
- Verifies that the project will go into pre-production within 90 days of the approval of the application.

The credit shall only be granted for expenses with respect to eligible motion picture productions. Eligible motion picture productions include, but are not limited to:

- Feature length films;
- Documentaries;
- Long-form specials,
- Television mini-series;
- Episodic television series;
- Commercial advertisements;
- Videos and music videos;
- Interactive television; and
- Effective on January 1, 2013, digital interactive media productions.

Eligible motion picture productions do not include:

- Political advertising and editorial based content;
- Any ongoing television program created primarily as news, weather or financial market reports;
- Any live or pre-recorded production featuring current events, sporting events or an awards show or other gala event;
- A reality television production, including, but not limited to, productions in the respect of a game, questionnaire, auction, or contest;
- Any production that contains obscene material;
- Productions whose sole purpose is fundraising;
- A long-form production that primarily markets a product or service;
- A production used for corporate training or in-house corporate advertising or other similar productions;
- Games of chance websites and other games of chance productions;

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- Marketing and promotional websites or microsites; all forms of social media, social networking, marketing and brand promotion;
- Infomercials, infotainment, or edutainment content;
- Solicitation-based productions; and
- Productions that do not spend at least \$250,000 in qualifying expenses.

Application Process and Procedures

Initial Application

Production companies meeting the basic eligibility requirements outlined above must submit an initial application to the VFO at least 30 days prior to production. The application must include any documentation required by the VFO. Applications can be found online at the VFO website, which is located at <http://FilmVirginia.org>.

Processing of Applications by the VFO

The VFO will review each application to ensure that all necessary documentation is attached. If the application is incomplete, the VFO will contact the production company to request missing information. The application will not be reviewed for credit allocation until the application is complete.

Completed applications will be reviewed by the VFO to determine the estimated amount of qualified expenses, the total cost of production and other information necessary to determine both eligibility and level of credit allocation. The VFO will determine which productions to approve and which to deny credit allocations based on any or all of the following factors:

- The amount of in-state production spending; and
- The qualifying criteria of the motion picture production, which shall include, but not be limited to:
 - Whether the production involves physical production within the Commonwealth of Virginia;
 - The number of residents of Virginia that will be employed in the production and the level of compensation they will be paid;
 - The extent to which the production will contribute to the support and expansion of existing production companies in Virginia;
 - The extent to which the production will impact existing local businesses and the local economy;
 - The extent to which the production will involve existing and new companies located in Virginia;
 - The extent to which the production provides employment at facilities physically located within the Commonwealth of Virginia; and
 - Any other relevant considerations as determined by the VFO.

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Productions will only be considered when funding is available. As funding is limited, it is possible that all of the funds will have been reserved by earlier productions at the time of the production company's submittal of its initial application. In this case, the VFO will inform the production company of the next date when a review of the production may be performed. The VFO will also inform the production company if a new application is required for later review.

The allocation of available credit funding is at the sole discretion of the VFO and its decisions as to the eligibility of a motion picture company and the amount of credit funding initially allocated to it are final.

Motion picture production companies that are rejected by the VFO for a particular production may apply in the future for tax credits regarding other productions.

Credit Notification

The VFO intends to approve or deny completed applications within 10 business days of receipt of application but reserves the right to take up to 30 days to respond.

A decision to potentially grant tax credits to a production company will be confirmed by a Credit Allocation Letter of Intent that will include:

- The maximum amount of the tax credit allotted;
- The date that eligibility for qualified expenses begins; and
- The date that eligibility for qualified expenses ends.

After receipt of the Credit Allocation Letter of Intent, the production company will enter into a memorandum of understanding with the VFO outlining the requirements the production company must meet in order to receive the credits. The memorandum will include at minimum:

- The estimated amount of money to be spent in Virginia;
- The estimated number of Virginia resident hires;
- The timeline for completing production in Virginia; and
- The maximum amount of credits to be allocated to the production company.

By signing the memorandum of understanding, the motion picture production company forfeits any right to contest the amount of tax credits that have been assigned to it and agrees that while the amount of credits granted upon the completion of the motion picture production may be lower than the maximum amount listed on the memorandum of understanding based on the amount of qualifying expenses, it may not be more.

Production companies seeking the tax credit must receive a Credit Allocation Letter of Intent from the VFO before making or incurring any qualified production expenditures in order for those expenditures to be eligible for the credit.

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Requirements During Production

The applicant must at all times keep proper books of record and accounts in accordance with generally accepted accounting principles consistently applied, with the books, records, or papers related to the accredited production in the custody or control of the taxpayer open for reasonable inspection and audits by the Department, including, without limitation, the making of copies of the books, records, or papers, and the inspection or appraisal of any of the assets of the applicant or the accredited production. This must include all vendor receipts for which the production is applying for tax credits.

If physical production goes over one calendar year, the production company must file a report with the VFO that verifies the progress of the production. The report shall include a detailed account of amounts spent in the Commonwealth at the current stage of production and provide proof that it is moving forward.

After Production

Upon completion of a qualified production, the applicant must submit to the VFO proof of the amount spent in the Commonwealth and any additional documentation required by the VFO in combination with the Department. Any pass-through entity that wishes to claim the credit at the entity level rather than allocating the credit to its individual owners must notify the VFO in writing at the time the final application is submitted.

Applications shall be submitted with a form approved by the VFO and signed by a licensed independent certified public accountant. The CPA must certify that (i) he has reviewed the expenses claimed by the applicant, (ii) such expenses meet the definition of Qualifying Expenses, and (ii) they were incurred in Virginia by the applicant in connection with the production of a motion picture filmed in Virginia.

Upon approval, the VFO shall issue a Certification Letter to the applicant indicating the amount of the tax credit that the taxpayer may claim on its Virginia income tax return. The Certification Letter will include the name of the production, a description of the production, and a detailed account of the qualifying expenses with respect to which the credit is being claimed.

Claiming the Credit

Under the requirements of *Va. Code* § 58.1-499 C, the taxpayer, upon receipt from the VFO of copies of the Certification Letter, must file the applicable Virginia state income tax return and attach any required documentation in order to receive the refundable Virginia Motion Picture Production Credit. The credit is refundable and shall be used against the taxpayer's Virginia individual or corporate income tax liability for the taxable year in which physical production was completed.

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Whenever a taxpayer is eligible to claim more than one Virginia income tax credit, the taxpayer shall exhaust all other applicable credits before utilizing the refundable Motion Picture Production Credit to ensure that the taxpayer receives the maximum benefit of his credits. The Motion Picture Production Credit has no carryforward provision, and, as such, must be used against Virginia income tax liability for the taxable year in which physical production was completed. If the amount of the available credit exceeds the taxpayer's tax liability, the taxpayer will receive a refund from the Department of the net excess of the refundable credit over such remaining tax liability. See Public Document 95-240 (9/22/95) for further information regarding the ordering of tax credits.

Any taxpayer allowed this tax credit must maintain and make available for inspection any information or records that the Department requests.

Pass-Through Entities

The amount of any credit attributable to a pass-through entity, such as a partnership, electing small business corporation (S corporation), or limited liability company, will generally be allocated to the individual partners, shareholders, or members, respectively, in proportion to their ownership or interest in such business entities. If a pass-through entity wishes to claim this credit at the entity level without allocating the amount of credit to the individual owners, the pass-through entity must notify the VFO in writing at the time it submits its final application and, upon approval, must follow any instructions for claiming the credit as provided in the certification letter.

Details for the Department's Annual Report

The Department, in consultation with the VFO, must publish a report by November 1 of each year for the 12 month period ending the preceding December 31. This report will include the following information:

- Location of sites used in a production for which a credit was claimed;
- Qualifying expenses for which a credit was claimed, classified by whether the expenses were for goods, services, or compensation paid by the production company;
- Number of people employed in the Commonwealth in connection with the production for which the credits were claimed; and
- The total cost to the Commonwealth's general fund of the credits claimed.

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Additional Information

These Guidelines and rules are available on-line in the Tax Policy Library section of the Department's website, located at www.policylibrary.tax.virginia.gov. For additional information, please contact either the Department of Taxation at (804) 367-8037 (www.tax.virginia.gov) or the Virginia Film Office at (804) 545-5530 (<http://FilmVirginia.org>).

Approved:


Craig M. Burns
Tax Commissioner