

## Entertainment Law

May 29, 2012

### Saskatchewan Announces New Non-Refundable 25% Film/TV and Digital Tax Credit

On May 4, 2012, the Honourable Bill Hutchinson, Saskatchewan's Minister of Tourism, Parks, Culture and Sport announced the introduction of a new non-refundable film, TV and digital tax credit, the Film/TV and Digital Tax Credit (FTDC).<sup>1</sup> The FTDC is intended to replace the former refundable Film Employment Tax Credit (FETC) which the Saskatchewan government eliminated earlier this year. Re: the elimination of the FETC see our Goodmans Update: *The Saskatchewan Film Employment Tax Credit is Eliminated* at: <http://www.goodmans.ca/Section/Publications/Updates>.

#### Background

On March 21, 2012, Saskatchewan Finance Minister Ken Krawetz announced in the Saskatchewan government's 2012-13 budget statement that the province would no longer offer the FETC which had been in place since 1998.<sup>2</sup> The FETC provided a 45% refundable film tax credit on eligible Saskatchewan labour expenditures plus bonuses for rural production and budgets over \$3 million. Popular Canadian television productions such as "Corner Gas" and "Little Mosque

on the Prairie" were filmed in Saskatchewan and accessed the FETC. As of July 1, 2012, applications for the FETC will no longer be accepted.<sup>3</sup>

The elimination of the FETC provoked outrage in both the Saskatchewan and the Canadian film industry. The decision to eliminate the FETC was heavily criticized by both the Saskatchewan Media Production Industry Association (SMPIA) and the Canadian Media Production Association (CMPA). Representatives of the Saskatchewan film industry, including several prominent Canadian actors and directors, spoke out against the cut publicly, using social media such as Facebook to express their discontent. An on-line petition called "Save the Saskatchewan Film Employment Tax Credit" gained over 8,000 signatures.<sup>4</sup> These protests culminated in meetings between representatives of the Saskatchewan film industry and the Saskatchewan government with a view to creating a new and comparable film incentive program which would replace the FETC.<sup>5</sup> In his press release, Minister Hutchinson stated that the new FTDC was based on "proposals by the Saskatchewan film sector", although judging by the negative reaction of the Saskatchewan film industry to the FTDC, as described below, the industry proposals may have been misconstrued.

#### The New FTDC

The FTDC is a non-refundable, non-transferable, tax credit of 25% on all eligible Saskatchewan production expenses, including labour costs. There are potential "bonuses" for items such as use of Saskatchewan labour, that increase the total FTDC incentive to as much as 43%. According to Minister Hutchinson, the

<sup>1</sup> Information, unless otherwise referenced, was found in: Government of Saskatchewan, News Release, "Government Presents Saskatchewan-Focused Creative Industries Plan" (4 May 2012) online: <<http://www.gov.sk.ca/news?newsId=494dc677-0fec-4619-ace6-5ad208ee6b48>>.

<sup>2</sup> Government of Saskatchewan, News Release, "Budget 2012-13: Keeping the Saskatchewan Advantage" (21 March 2012) online: <<http://www.gov.sk.ca/news?newsId=859d887e-d7a4-45da-9f4b-f25ec4ab59cc>>.

<sup>3</sup> Ishmael N Daro, "Fight over film tax credit continues", The Sheaf (5 April 2012) online: <<http://www.thesheaf.com/2012/04/05/fight-over-film-tax-credit-continues-saskatoon-producer-says-film-industry-not-warned-about-cuts-in-budget/>>.

<sup>4</sup> *Ibid.*

<sup>5</sup> Government of Saskatchewan, News Release, "Premier Wall to Meet with Film Industry to Discuss Tax Credit" (26 March 2012) online: <<http://www.gov.sk.ca/news?newsId=1bd6cac7-2f11-4b57-8f59-1f27634554f6>>.

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old FETC was not serving to develop a strong film industry in Saskatchewan and came at a high cost to taxpayers:

*“Unlike the existing program, the new FTDC is a true tax credit as it is fully deductible from taxes paid in Saskatchewan and could be available July 1, 2012. We wanted to make sure that (the new program) is in fact a non-refundable tax credit program. The current program that we have is really more a grant than tax credit. Companies that produce films get the grant whether they actually pay any income taxes here in Saskatchewan or not.”*<sup>6</sup>

The foregoing views expressed by Minister Hutchinson were also echoed by Saskatchewan Premier Brad Wall who subsequently defended the FTDC saying that it would cost the government of Saskatchewan about \$1 million a year – a large reduction from the FETC which costs the government approximately \$8 million annually. Reflecting his view that a refundable tax credit is more in the nature of a “grant”, Premier Wall further stated that only 2% of the money paid via the FETC was “truly a tax credit”, while 98% was essentially a grant to the industry.<sup>7</sup>

## FTDC is Not Refundable

The key difference between the FTDC and the FETC is that the former is a non-refundable tax credit while the latter is a refundable tax credit. In the case of the FETC, the applicant corporation filed its corporate tax return and was “refunded” the applicable FETC minus any taxes which it owed. Because single purpose companies are frequently used to produce film and TV productions, the corporation which claimed the FETC would often have no or minimal Saskatchewan tax liability.

Therefore, it would typically receive a substantial “refund” cheque from the Saskatchewan government – a receivable which could easily and effectively be used by the producer as collateral for a loan from a bank or other interim financier (i.e. in common parlance, the FETC was “bankable”).<sup>8</sup>

Under the proposed FTDC, by contrast, the credit can only be applied against the applicant’s Saskatchewan corporate tax liability. Unlike the FETC, any “excess” credit would not be paid by the Saskatchewan government to the applicant taxpayer as a refundable credit. Rather, it would be applied towards the future Saskatchewan tax liability (if any) of the applicant taxpayer for up to 10 years.<sup>9</sup> Therefore, the FTDC is effectively not “bankable” and a lender would not accept the FTDC as collateral for interim production financing since there is no “refund” receivable to bank.

## Criticism of the FTDC

It is this non-refundable aspect of the FTDC, which has led to severe criticism of the new credit by the film industry in Saskatchewan and throughout Canada. For example, according to Norm Bolen, the President and CEO of the CMPA:

*“Over 70 per cent of a Saskatchewan production’s financing comes from outside the province. Non-refundable tax credits do not trigger this inward investment: they cannot be used by the producer as proof that a production will be fully financed through expected revenues.*

*A non-refundable tax credit is not, therefore, workable or attuned to the industry’s business and funding realities. Bigger picture, non-refundable incentives irreparably jeopard-*

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<sup>6</sup> Angela Hall, “Gov’t unveils new film tax credit”, *Leader-Post* (5 May 2012) online: <<http://www.leaderpost.com/entertainment/movie-guide/unveils+film+credit/6570933/story.html>>.

<sup>7</sup> Angela Hall, “Sask. film industry calls for removal of Minister Bill Hutchinson”, *Leader-Post* (10 May 2012) online:<<http://www.leaderpost.com/news/Sask+film+industry+calls+removal+Minister+Bill+Hutchinson/6602255/story.html>>.

<sup>8</sup> Norm Bolen, “Why the film tax credit is essential”, *Leader-Post* (19 May 2012) online: <<http://www.leaderpost.com/news/film+credit+essential/6648148/story.html>>.

<sup>9</sup> Joe Couture, “Lost? Enroll in Film Tax Credits 101”, *The StarPhoenix* (15 May 2012) online: <<http://www.thestarphoenix.com/news/Lost+Enrol+Film+Credits/6621423/story.html>>.

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*dize the viability of the industry by encouraging the exodus of production activity to other provinces or even out of the country. They eliminate thousands of existing and future jobs, and therefore millions in tax revenues. They undermine Saskatchewan's ability to set the necessary foundation upon which to build a more solid economy, and to compete domestically and internationally.”<sup>10</sup>*

Shortly after the FDTC announcement, Ron Goetz, the President of the SMPA, called for the removal of Minister Hutchinson, stating that his actions have placed the entire Saskatchewan film and video industry in jeopardy.<sup>11</sup> Additional criticism has been voiced by NDP Culture critic Danielle Chartier, as well as TV and film stars, including Saskatchewan-born Kim Coates of “Sons of Anarchy” and Wes Bentley of “Hunger Games”.<sup>12</sup>

Supporters of the film industry position gathered at the Saskatchewan legislature in Regina on May 14 to demand that the government reconsider its decision to replace the FETC with the FDTC.<sup>13</sup> This rally followed other attempts to publicize the issue, including a YouTube video produced by the SMPA. The video compares a non-refundable tax credit, such as the FTDC, to “a car without a motor” and states that a film made in Saskatchewan by a small business with a \$7 million budget would require a profit of \$85 million to benefit from the credit.<sup>14</sup> Minister Hutchinson says that the profit

would need to be only \$14.6 million, but Mr. Goetz argues that “the bottom line is neither number is attainable for any company or production in this province or in Canada”.<sup>15</sup>

More recently, John Lewis, international Vice President and director of Canadian affairs for IATSE, in a May 22 letter to Premier Wall, urged the Premier to reintroduce a refundable film tax credit “...for a two-year period to allow for more consultation.” In his letter, he pointed out to Premier Wall that:

*“There are few industries that are as mobile as the film industry. It is an industry capable of packing up and setting up elsewhere in a matter of days... As productions leave the province, Saskatchewan will lose thousands of jobs and millions of dollars in tax revenue.”<sup>16</sup>*

## Evaluating the Position of the Saskatchewan Government

One can certainly appreciate the reasonable desire of the Saskatchewan government to reduce the overall cost to Saskatchewan taxpayers of its film incentive program, given current fiscal pressures. However, the position expressed by both Premier Brad Wall and Minister Hutchinson that a refundable tax credit (such as the former FETC) constitutes a “grant” and is not “truly a tax credit” is inaccurate and out of step with existing Canadian federal and provincial tax policies.

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<sup>10</sup> Bolen, *supra* note 8.

<sup>11</sup> Angela Hall, “Sask. film industry calls for removal of Minister Bill Hutchinson”, *Leader-Post* (10 May 2012) online: <<http://www.leaderpost.com/news/Sask+film+industry+calls+removal+Minister+Bill+Hutchinson/6602255/story.html>>.

<sup>12</sup> Joe Couture, “Film lobby takes protest to legislature”, *The StarPhoenix* (14 May 2012) online: <<http://www.thestarphoenix.com/news/Film+lobby+takes+protest+legislature/6620422/story.html>>. Leader-Post; Etan Vlessing, “Film Industry Pans Canada’s Newest Film Tax Credit”, *The Hollywood Reporter* (7 May 2012) online: <<http://www.hollywoodreporter.com/news/canada-newest-film-tax-credit-panned-critics-wes-bentley-hunger-games-320870>>.

<sup>13</sup> Couture, *supra* note 12.

<sup>14</sup> “The ‘New’ Saskatchewan Film/TV Digital Tax Credit & Why it Doesn’t Work” (video), online: YouTube <<http://www.youtube.com/watch?v=W4XldJypjc>>.

<sup>15</sup> Joe Couture, “NDP, film industry critical of gov’t plan”, *The StarPhoenix* (8 May 2012) online: <<http://www.thestarphoenix.com/news/film+industry+critical+plan/6582995/story.html>>.

<sup>16</sup> The quotes from the May 22 letter of John Lewis are taken from the article: Etan Vlessing, “IATSE Tells Saskatchewan to Reintroduce Refundable Tax Credit, Or Else”, *The Hollywood Reporter* (24 May 2012) online: <<http://www.hollywoodreporter.com/news/iatse-tells-saskatchewan-reintroduce-refundable-329212>>.

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The federal Canadian government, most Canadian provinces and over 35 U.S. states have a refundable tax credit program for the film industry.<sup>17</sup> Many other Canadian industries are subsidized through refundable tax credits. And average Canadians receive tax refund cheques from the Canadian government on a routine basis after they file their tax returns each year.

The fact is that tax credits can be refundable, transferable, non-refundable and/or non-transferable. In the U.S., for example, several U.S. states have introduced transferable film tax credits (eg. Louisiana, Georgia, Connecticut, Illinois, Arizona, New Jersey).<sup>18</sup> Using Premier Wall's terminology, a transferable tax credit is "truly a tax credit" in that it can only be utilized by a local taxpayer to offset its local tax liability (for example, a company carrying on business in Saskatchewan with taxable income). However, it can be transferred (i.e. sold and assigned) by the taxpayer which initially applies for the credit, whether with or without the assistance of an intermediary such as a broker, to a local taxpayer in the jurisdiction. It is a shame that the Saskatchewan government did not consider this option when it introduced the FTDC. Of course, a refundable credit such as the FETC, is arguably more straight forward and effective than a transferable one, but if the FTDC had been made transferable at least producers would have had an opportunity to monetize the credit.

It remains to be seen whether the Saskatchewan government will, once again, reconsider its position vis-a-vis its film incentive. In the meantime, there is a significant risk that Saskatchewan film producers will move their business out of the province and cause potential damage to the film industry in Saskatchewan.<sup>19</sup> In addition, for-

eign based producers such as the Hollywood studios will likely not view Saskatchewan as a desirable production location given that the FTDC only benefits local Saskatchewan taxpayers. Yet another concern is the potential precedent-setting nature of this proposal (i.e. Saskatchewan will be the only jurisdiction in Canada with a non-refundable and non-transferable film tax credit), and the impact it could have on the industry in Canada if other provinces were ever to follow suit.

It would be a shame if the Saskatchewan film industry were to suffer as a result of the FTDC. Hopefully, before any negative impact on production in the province occurs, the Saskatchewan government will review the proposed FTDC and consider making it either refundable or, at least, transferable, to the benefit of its domestic film industry.

If you would like further information or have any questions about this matter, please do not hesitate to contact any member of our Entertainment Law Group:

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<sup>17</sup> "Minister inept with film issue", *The StarPhoenix* (12 May 2012) online: <<http://www.thestarphoenix.com/opinion/Minister+inept+with+film+issue/6610320/story.html>>.

<sup>18</sup> William Luther, *Movie Production Incentives: Blockbuster Support for Lackluster Policy* (Washington, DC: Tax Foundation, 2010) online: <<http://taxfoundation.org/files/sr173.pdf>>.

<sup>19</sup> Couture, *supra* note 15.