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The governments of Ontario and Québec recently made significant positive changes to their respective production services film tax credits — changes which will directly benefit non-Canadians who choose to produce film and television productions in these provinces. In an effort to encourage more foreign service production in the province of Québec, the Québec Minister of Finance, Raymond Bachand, announced on June 12, 2009 that the 25 per cent Québec Refundable Tax Credit for Film Production Services ("QRTCPS") would henceforth apply to all qualifying production costs incurred in Québec with respect to a qualified production, as opposed to only qualifying Québec labor costs. Ontario was quick to follow Québec's lead. On June 29, 2009, Dwight Duncan, the Ontario Minister of Finance, announced that the 25 per cent Ontario Production Services Tax Credit ("OPSTC") will apply to all qualifying production costs incurred in Ontario after June 30, 2009 including both qualifying labor and non-labor related costs incurred in the province.

These tax credit enhancements recognize the continuing importance of the film industry to the respective Ontario and Québec economies, and will facilitate Ontario and Québec remaining among the top jurisdictions in North America for film and television production. While the QRTCPS and OPSTC rates remain unchanged at 25 per cent, the "all spend" concept introduced by the provinces marks a significant increase in the amounts of the respective tax credits which are available to non-Canadian producers who film in Ontario or Québec, by broadening the tax base of each respective tax credit to include all of the production costs incurred in the respective province, including expenditures for studio rentals and equipment purchases in addition to labor related expenses. Since labor costs often account for only about 50 per cent of total production spend, these measures will greatly enhance the value of these provincial production services film tax credits to foreign producers who locate their productions in Ontario or Québec.

In conjunction with the QRTCPS announcement, the Québec government also introduced a five per cent increase in the tax credit rate for computer-aided special effects and animation activities, including the shooting of scenes in front of a chromatic screen (*i.e.*, green screen). All-spend production costs directly attributable to these computer animation and vfx expenditures are now eligible for a combined 30 per cent tax credit rate (*i.e.* 25 per cent of the qualifying "all spend" QRTCPS costs plus an additional five per cent bonus). In Québec, foreign producers which outsource visual effects or digital animation work to local Québec animation or special effects houses can claim these expenditures directly under the "all spend" QRTCPS at the enhanced 30 per cent rate. In contrast, the Computer Animation and Special Effects Tax Credit ("OCASE") in Ontario, which is equal to 20 per cent of qualifying computer animation and vfx labor expenditures, is normally claimed by the visual effects or animation studio that performs the eligible work for the foreign producer. That said, a foreign producer producing in Ontario is not precluded from claiming both the 25 per cent OPSTC "all spend" credit and the OCASE credit on any qualifying visual effects expenditures which it incurs directly (*e.g.*, filming in front of a green screen). For further information, here are links to the Ontario *http://www.omdc.on.ca/AssetFactory.aspx?did=6623* and Quebec *http://www.sodec.gouv.qc.ca/english/documents/BULEN_2009-3-a-b.pdf* announcements.

Ontario Ministry of Finance Announces Additional Details Regarding Proposed Enhancements to the OPSTC

On September 10, 2009 the Ontario Ministry of Finance released a bulletin entitled "*Bulletin: Proposed Enhancements to the Ontario Production Services Tax Credit (OPSTC)*". The *Bulletin* provides additional details with respect to the June 29, 2009 announcement of the Ontario government regarding an expansion of the base of the OPSTC to include both labor and non-labor related expenditures. According to the Ministry, it is not intended as a substitute for any relevant legislation or regulations and the proposed enhancements to the OPSTC described in the *Bulletin* will be implemented through amendments to the *Taxation Act, 2007* (Ontario) which, when enacted, will be retroactive for all qualifying production expenditures which are incurred after June 30, 2009.

Proposed Enhancements to the OPSTC

As per the June 29, 2009 announcement of the Ontario government, the proposed enhancements to the OPSTC will expand the eligible expenditures that qualify for the OPSTC. The OPSTC tax credit rate of 25 per cent will apply to the "qualifying production expenditure" incurred after June 30, 2009 by an eligible corporation in respect of an eligible production as defined in the *Bulletin*.

Qualifying Production Expenditure

According to the *Bulletin*, a corporation's "qualifying production expenditure" in respect of an eligible production for OPSTC purposes will be the amount by which the sum of the following amounts incurred by the corporation in respect of the production in the applicable taxation year exceeds any government or non-government "assistance" received in respect of the production:

a) eligible wage expenditure;
b) eligible service contract expenditure; and
c) eligible tangible property expenditure.

Eligible Wage Expenditure

A corporation's eligible wage expenditure for a taxation year in respect of an eligible production will include employee salary and wages that are:

- reasonable in the circumstances;
- directly attributable to the eligible production;
- incurred by the corporation in the taxation year or the previous taxation year;
- related to services rendered in Ontario for the stages of production from the final script to the end of the post-production stage; and
- paid by the corporation in the year or within 60 days after the end of the year to the corporation's employees who were Ontario-based individuals at the time the payments were made (amounts incurred in the previous year that were paid within 60 days after the end of the previous year are excluded).

An eligible wage expenditure would also include the fees a qualifying corporation must pay to guilds and unions such as the Alliance of Canadian Cinema, Television and Radio Artists (ACTRA) in respect of the production for Ontario-based individuals.

Eligible Service Contract Expenditure

A corporation's eligible service contract expenditure will include amounts that are paid to qualifying third parties (*i.e.*, independent contractors) that are:

- reasonable in the circumstances;
- directly attributable to the eligible production;
- incurred by the corporation in the year or the previous year;
- related to services rendered in Ontario in the year or the previous year to the corporation for the stages of production from the final script stage to the end of the post-production stage; and
- paid by the corporation in the year or within 60 days after the end of the year (amounts incurred in the previous year that were paid within 60 days after the end of the previous year are excluded) to a person or partnership that carries on a business in Ontario through a permanent establishment and that is:
  - an Ontario-based individual at the time the amount is paid and who is not an employee of the corporation, provided the services are rendered in Ontario in respect of the production by the individual or the individual's employees at a time when they were Ontario-based individuals;
  - another corporation that is a taxable Canadian corporation, provided the services are rendered in Ontario in respect of the production by the corporation's employees at a time when they were Ontario-based individuals; or
  - a partnership, provided the services are rendered in Ontario in respect of the production by an Ontario-based individual who is a member of the partnership or the partnership's employees at a time when they were Ontario-based individuals.

Eligible service contract amounts will include the cost of on-set police services.

Eligible service contract amounts will not include: (i) travel where any portion is outside of Ontario; (ii) meals and entertainment (other than on-set catering); and (iii) living expenses (hotels, etc.).

Eligible Tangible Property Expenditure

A corporation's eligible tangible property expenditure will include all or a portion of an amount incurred by the corporation for the acquisition or rental, in Ontario, of tangible property used in the eligible production provided:

- the property is used in Ontario in a manner that is directly attributable to the eligible production;
- the property is used during the stages of production, from the final script stage to the end of the post-production stage;
- the expenditure is incurred in Ontario in the taxation year or the previous taxation year;
- the expenditure is paid by the corporation in the year or within 60 days after the end of the year (amounts incurred in the previous year that were paid within 60 days after the end of the previous year are excluded);
- the expenditure is reasonable in the circumstances; and
- the expenditure is paid to a person that carries on a business in Ontario through a permanent establishment and that is:
  - an Ontario-based individual at the time the amount is paid and who is not an employee of the corporation; or
  - a taxable Canadian corporation; and
  - the corporation's primary source of active business income is derived from selling or renting tangible property.

Under the proposed enhancements, generally, tangible property would have its ordinary meaning, *i.e.*, physical property that can be touched. Eligible tangible property expenditures *would* include items such as equipment, studio rentals and computer software. Examples of expenditures that would *not* qualify for the OPSTC include financing and banking costs, insurance premiums, the cost of completion bonds and story rights.

For depreciable tangible property that is acquired by the qualifying corporation and meets all of the above proposed criteria, the corporation's eligible tangible property expenditure for the year would include only the portion of the Ontario capital cost allowance (CCA) for the property for the taxation year under the

Income Tax Act (Canada) that relates to the use of the property in Ontario in the year in the course of completing the eligible production.

Excluded Items

Under the current OPSTC rules, a corporation's qualifying production expenditure will not include remuneration determined by reference to profits or revenues, an amount to which section 37 of the federal *Income Tax Act* applies nor, for greater certainty, an amount that is not a production cost (*e.g.*, an amount in respect of advertising, marketing, promotion, market research, etc.) or an amount related in any way to another film or video production.

A corporation's qualifying production expenditure may not include alcoholic beverages.

For further information, a link to the Ontario Ministry of Finance Bulletin is provided below:

http://www.fin.gov.on.ca/english/publications/bulletins/2009_09_10_filmtax.html

The recent enhancements to the Québec and Ontario production services tax credits has created pressure in British Columbia (BC), the third major production center in Canada and the Canadian province with the most US originated production service work, to match the changes. After the Québec and Ontario tax credit enhancements were announced, the BC production community immediately lobbied the BC government to level the playing field by expanding the base of the BC production services tax credit to include non-labor costs in a similar fashion to Québec and Ontario. Unfortunately, BC is currently facing its largest budget deficit in history and therefore, despite these intense lobbying efforts, the budget of the BC government which was introduced on September 1, 2009 did not include any measures to expand the BC production services tax credit to include non-labor costs. Therefore, for the time being, BC is at a competitive disadvantage versus Québec and Ontario in terms of the quantum of its production services tax credit. However, at the time of writing, the BC producers' lobbying efforts are continuing unabated and the BC production community is very optimistic that the BC government will be persuaded to make changes to the BC production services tax credit in the very near future which will make the services credit more competitive with its counterpart tax credits in Québec and Ontario. ■

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