“Runaway production” is not new. The exodus of production from the Hollywood studio lot has been afoot for decades, and usually occurs for two distinct, but not totally separate, reasons: (1) “artistic flight”;¹ and (2) “economic flight.”² Because the former is primarily fueled by creative decisions it is not the focus of this paper.

To combat economic flight abroad, Congress passed, and President Bush signed, a bill with the goal of keeping production and filming in the U.S.³ However, some states, taking a page out of

¹ Artistic flight is a result of a director’s creative vision which requires filming away from the studio lot to give the film an “authentic” feel. While any decision has some economic aspects—and the venues often capitalize on the opportunity by lowering costs to make the decision easier—artistic flight is fueled primarily by artistic vision. Prime examples of this kind of flight are location shoots in New York City or Paris, which offer an atmosphere that is often impossible to replicate on a studio lot.

² Economic flight is only incidentally artistic (requiring only that one location resemble another closely enough to justify the artistic compromise). An example of successful flight in past decades included Vancouver and Toronto, Canada, where tax incentives and cheap labor attracted big (and small) movie producers to shoot “on location” (which could stand for the Midwest or New York City). In fact, between 1996 and 2006, more than 1,500 film and television productions were “outsourced” to Canada (not including the “scores” of made for TV movies produced there). See Kelly Nestruck, Set in the US, Filmed in Canada, Fed Up in Hollywood, GUARDIAN.CO.UK (Nov. 1, 2007 10:50 GMT), http://www.guardian.co.uk/film/filmblog/2007/nov/01/kellynestruckthursampic; Edward Jay Epstein, Northern Expenditure: Why are so many movies still being shot in Canada?, SLATE (Feb. 13, 2006), http://www.slate.com/id/2136064.

³ See American Jobs Creation Act of 2004, Pub. L. No. 108-357, § 181, 118 Stat. 1418, 1445 (codified as amended in 26 U.S.C. § 181 (2006)). Two of the industry’s largest unions, the Directors Guild of America (“DGA”) and the Screen Actors’ Guild (“SAG”), argued (and the Commerce Department agreed) that runaway production cost the United States $10.3 billion in lost revenue in 1999 alone. To offset this and jump start domestic production, the Act, which had a December 31, 2009 sunset provision, included provisions that allowed for (1) an immediate tax write-off of production expenditures for domestic film and TV production under $15 million (or $20 million for production located in certain “low income” communities), and (2) a 9% deduction from net income for qualifying domestic film production.
Canada’s playbook, introduced their own, often generous, tax incentives to attract production. The result for California, and to a lesser extent New York (with its own established film and television industries), was a war on two fronts: international flight on the one, and intranational flight—financed by both federal and state tax dollars—on the other. These new entrants, however, were not immune from the same effects, with late comers introducing even more generous incentives.

Over the years the number of state programs exploded, with at least forty-two states now participating in some capacity.\(^4\) Two interrelated policy considerations result from this rapid growth: (1) over-saturation of the marketplace,\(^5\) and (2) a “race to the bottom” with the generosity of the incentives.\(^6\) In the process the states may forego valuable opportunity costs that could produce a greater return on their investment.

State incentives come in various forms—such as tax forbearances, free use of locations, an inexpensive labor force and even loan guarantees. Governments seek to recover these investments in different ways. Under the most basic economic model, a state benefits if the rebates and credits it provides are less than the taxes it otherwise collects from the production.\(^7\) However, governments also count the creation of production-related jobs, tourism, the infusion of revenue to low-income areas and the building of valuable infrastructure as indirect benefits (which may even justify losses under


\(^5\) Over-saturation of the marketplace occurs when each state’s return on investment declines as more states adopt aggressive subsidies.

\(^6\) A “race to the bottom” occurs when states compete with each other, gradually ramping up incentives to attract production, and in the process decreasing their own return on investment.

the basic model).\textsuperscript{8} Louisiana’s film tax credit law exemplifies these considerations.\textsuperscript{9}

It is undeniable that big studio productions can infuse large sums of money into a local economy. Two examples are Louisiana and New Mexico, both aggressive early adopters, which established their programs two years before the national response in 2004:

- In 2008, New Orleans, Louisiana was home to twenty productions, with budgets totaling $275 million. The City estimates that at least half of that amount (almost $138 million) was spent locally and therefore benefitted local businesses and production workers. In fact, according to the Office of Entertainment Industry Development (“OEID”),\textsuperscript{10} it is

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\footnotesize{\textsuperscript{8} Id. See also Dan Glickman, Stand Up for Creative Jobs, HUFFINGTON POST (Mar. 19, 2009), http://www.huffingtonpost.com/dan-glickman/stand-up-for-creative-jobs_b_177137.html (“Tax incentives, built responsibly, can serve a critical role in economic stimulus. To do so, they must achieve three objectives: create jobs, increase commerce and generate a positive return on taxpayer’s investment.”).}

\footnotesize{\textsuperscript{9} The introduction of § 6007, the Motion Picture Investor Tax Credit, provides that:}

\begin{itemize}
  \item The primary objective of this Section is to encourage development in Louisiana of a strong capital and infrastructure base for motion picture film, videotape, digital, and television program productions in order to achieve an independent, self supporting industry. The objective is divided into immediate and long-term objectives as follows:
  \begin{enumerate}
    \item Immediate objectives are to:
      \begin{enumerate}
        \item Attract private investment for the production of motion pictures, videotape productions, and television programs in Louisiana.
        \item Develop a tax and capital infrastructure which encourages private investment. This infrastructure will provide for state participation in the form of tax credits to encourage investment in state-certified productions and infrastructure projects.
        \item Develop a tax infrastructure utilizing tax credits which encourage investments in multiple state-certified production and infrastructure projects.
      \end{enumerate}
    \item Long-term objectives are to:
      \begin{enumerate}
        \item Encourage increased employment opportunities within this sector and increased global competition with other states in fully developing economic development options within the film and video industry.
        \item Encourage new education curricula in order to provide a labor force trained in all aspects of film and digital production.
        \item Encourage development of a Louisiana film, video, television, and digital production and post-production infrastructure with state-of-the-art facilities.
      \end{enumerate}
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\end{itemize}

\footnotesize{\textsuperscript{10} OEID is a department of Louisiana’s Department of Economic Development.}
estimated that total production in Louisiana increased from $20 million in 2002 to nearly $700 million in 2007.\textsuperscript{11}

- New Mexico’s “Film Incentive Program,” boasting a $276 million fund earmarked for film and television investment and production,\textsuperscript{12} was home to twenty-two productions, generating $130 million of revenue for the state.\textsuperscript{13}

While both programs are aggressive,\textsuperscript{14} neither is as generous as Michigan’s, a relative newcomer hoping to build its own film industry by providing public support of up to 42\% of a production’s costs.\textsuperscript{15} According to a study commissioned by Michigan, the program (launched in April 2008) created 1,102 “full time” jobs, thereby generating $53.8 million in new employment income.\textsuperscript{16} However, in the same time period the program cost taxpayers about $48 million in tax forbearance. Assuming the figures are accurate, a back of the envelope analysis indicates that for every $1, the tax incentives generate only $1.2 in revenue.


\textsuperscript{13} See Streib, \textit{supra} note 7.

\textsuperscript{14} Louisiana, which has a 4\% state sales tax, grants a 25\% investor tax credit based upon the total in-state expenditures of a motion picture production. An additional 10\% labor tax credit is given for the hiring of Louisiana residents. The tax credits are fully transferable. Louisiana also offers a 40\% infrastructure tax credit for the building/establishment of state-of-the-art facilities. The tax credits have no cap. See \textit{La. Rev. Stat. Ann.} § 47:6007 (2010); \textit{New Orleans Office of Film and Video}, http://www.filmneworleans.org (last visited Sept. 12, 2010).

New Mexico, which has a 5\% state sales tax, gives a 15\% tax credit on New Mexico based production expenses. It also has no sales tax at point of sale for commercial filming, no charge for filming at state-owned facilities; and even has a workforce training program to assist production. See \textit{N.M. Stat. Ann.} § 7-2F-1 (2010).

\textsuperscript{15} MICH. COMP. LAWS § 208.1455 (2010); see Michael Cieply, \textit{States Underwrite Films, Some in Narrowest Release}, N.Y. Times, Mar. 19, 2009 at C1. Michigan has to rely on the generosity of its program to attract production because a six year lag allowed states like Louisiana and New Mexico to establish infrastructure which Michigan lacks. Additionally, the physical proximity of New Mexico to Hollywood, and Louisiana’s unique topography (the bayou) provide advantages Michigan has to overcome.

\textsuperscript{16} STEVEN R. MILLER AND ABDUL ABDULKARDI, \textit{Mich. State Univ., The Economic Impact of Michigan’s Motion Picture Production Industry and the Michigan Motion Picture Production Credit} (2009), http://www.michiganfilmoffice.org/cm/The-Film-Office/MSU_Economic_Impact_Study_269263_7%5B1%5D.pdf.
The reason why these tax incentives are so attractive to businesses is laid out in Schulyer M. Moore’s article.\(^\text{17}\) Put simply, most films lose money, but nevertheless hundreds of films are produced each year—almost in defiance of the laws of supply and demand.\(^\text{18}\) One important catalyst for the prominence of the tax credits is a shift in the world of film finance. In the past, as much as one hundred percent of a film’s budget was raised through “pre sales” at film markets (more euphemistically known as “festivals”). That amount has shrunk to about 70% today.\(^\text{19}\) The state and federal tax credits provide an important lubricating function to the wheels of production by providing “free money” to bridge the gap,\(^\text{20}\) in essence making the state a financial backer of the film. However, while this dynamic is attractive to producers, it does not always lead to desirable results for the states.

For example, in 2009 the Wisconsin Department of Commerce issued a harsh report on the cost of film tax credits.\(^\text{21}\) Wisconsin

\(^{17}\) Schuyler M. Moore, Financing Drama: The Challenges of Film Financing Can Produce as Much Drama as Takes Place on the Screen, 31-May L.A. Law. 26 (2008).

\(^{18}\) Moore proposed two rationales for this: (1) the “sex-appeal” of being in the business; and (2) the chance for a big payoff (while 600 to 700 movies are produced each year, only 200 movies may obtain a theatrical release; of these two hundred, a handful see a profit; but rare “blockbusters” produce exponential returns, and may offset the loss suffered by dozens of films.) As he points out, this is gambling in its purest form, tax-credits, therefore, would be analogous to playing with the house’s money. Id.

\(^{19}\) This led to layered finance models in which gap loans made up most of the difference, but required completion guarantees and did not cover pre-production expenses, which in turn required bridge lenders, who were willing to make loans to fund preproduction expenses with no completion guarantees in place. Analogizing this to a housing loan, these lenders would come in third in seniority, after both the primary mortgage and the secondary mortgage on the film. Naturally, these kinds of loans carry a hefty premium (sometimes reaching 1% per week). Id. at 28.

\(^{20}\) This “free money” comes in two flavors: assignable and non-assignable tax credits. Assignable tax credits can be readily sold to third parties, and an entire cottage industry has developed around their brokerage. Competition increased the value of assignable tax credits from 70 cents to 82 cents on the dollar. Non-assignable tax credits are not as liquid; they are analogous to the securitization in the mortgage market—the company must obtain a loan secured by the tax incentives for the lender to obtain direct payment of the tax refund. Id.

\(^{21}\) See Wis. Dep’t of Commerce, Cost Benefit Analysis of Wisconsin Film Tax Credit Program (2009), http://www.senate.michigan.gov/gop/senators/cassis/Wisconsin%20Film%20Tax%20Analysis.pdf; see also Tom Still, Lights! Camera! Inaction? State film tax credits stir debate, Wisconsin Technology Network News (Apr. 16, 2009),
Commerce Deputy Secretary Aaron Olver characterized the tax credit as “the least effective” tool in the agency’s arsenal of economic development, saying that a tax credit for manufacturers costs the state a little more than $3 for every hour of labor it creates, while the film tax credit costs twenty times as much ($60, or 3x20) for the same hour of labor.22 In other words, if we had to choose, we could get one full-time job on a film for one year or we could get twenty factory jobs that might last for twenty years.23 Even in successful states like Louisiana, that very scenario may cost the state’s taxpayers more than $20 million.24 The specific question in Michigan with its decimated manufacturing base and an unemployed skilled work force, is whether film tax credits are a responsible investment in the future, or are the opportunity costs foregone in pursuit of those industries too steep?

If a traditional investment in manufacturing jobs would yield a greater return, as Olver suggests, the state foregoes that opportunity by pursuing the far “sexier” field of film production. As mentioned supra, states look at both the hard numbers (the return on investment) and some indirect benefits, such as job creation, infrastructure, and tourism

http://wistechnology.com/articles/5943/. The Department believes that the tax credits cost more than they are worth in economic benefits to the state. The report called the program “really expensive,” because it is not a typical tax credit program—capped at a percentage of taxes paid—but a refundable tax credit program, making it akin to a blank check, if the tax credit exceeds the recipient’s actual tax bill, the state will write a check for the difference.

22 See Wisconsin Film Incentives, FILM WISCONSIN, http://www.filmwisconsin.net/Incentives/WhatTheyAre.asp (last visited Aug. 31, 2010). The Wisconsin program has an investment tax credit of 25% that can be claimed for investing in Wisconsin based productions; a comprehensive sales and use tax exemption for machinery, equipment and services used in production and post-production and 0% tax for all film and television services contracted by out of state production companies; a refundable tax credit of 25% of direct production expenditures for feature films, television movies, episodic and mini-series television, video games and broadcast advertising production; a 15% state income tax credit for film, television and electronic game production businesses who make a capital investment by starting a business in Wisconsin, with further incentives available on a city-by-city basis. It is not nearly as ambitious and costly as the Louisiana and Michigan programs.

23 See Still, supra note 21 (citing the Johnny Depp film “Public Enemies” which was shot in Wisconsin) (“The film generated spending of $18.5 million but all but $5 million of that spending took place outside the state. ‘Even making favorable assumptions about indirect economic impact, “Public Enemies” only returned $1.70 for every $1 invested,’ the Commerce report concluded.”).

24 Id.
to decide if the cost is worth it.\textsuperscript{25} Some of these assumptions, however, may not be well grounded in fact. To wit:

- While a producer is concerned with the long term goal of turning a profit, the state is interested in the job creation—and business related expenses by the production—in the average 18-month period of the production. To sustain employment, a state needs a steady flow of new productions in the pipeline, however, a factor often outside its control. While the generosity of the tax credit is a part of the studio’s decision, it is but one part of the calculus.\textsuperscript{26}

- Arguably the most important secondary benefits—long term infrastructure building and the post-production jobs in it—have an important caveat closely related to the above point. The numbers of jobs are finite, and while more than 600 films are produced each year, only the handful of big-ticket productions, undertaken by major studios, would produce the desirable effects in a state. Simply put, there are not enough of those to go around for each of the forty-two states currently in the business of financing film to sustain long term production job growth.\textsuperscript{27}

- Even more precarious is the tourism justification. Even if a film is spectacularly successful, tourism to the state is not guaranteed, because a producer concerned with the bottom line may choose a location based in part on the economic incentives

\textsuperscript{25} These benefits are the “economic multipliers” effects on which legislatures rely to support the passage of the tax credits. See Miller, supra note 16; see also Ernst & Young, Economic and Fiscal Impact of the New Mexico Film Production Tax Credit; Prepared for the New Mexico State Film Office and State Investment Council (2009), http://www.nmfilm.com/locals/downloads/nmfilmCreditImpactAnalysis.pdf.

\textsuperscript{26} Incidentally, some states have legislation, such as Louisiana, that profess a long term goal of providing “new education curricula in order to provide a labor force trained in all aspects of film and digital production,” therefore committing further resources to the enterprise. See La. Rev. Stat. Ann. § 47:6023(A)(2)(b) (2010). But if these trainees act in their own best interests, the best result the majority of states can actually hope for is that trainees will find jobs in the field, most likely in already established film markets such as California and New York—thereby transferring all of the benefits accrued to another state.

\textsuperscript{27} This appears axiomatic, but it does not stop states from passing subsidies in hopes of attracting these productions, and further assuming that they can reproduce that result year after year to justify the infrastructure and job growth assumptions made in passing the tax credits.
the state offers, thereby setting a story in a totally different state, with no tourism benefit flowing to the incentivizing state.  

An important implication of the scarcity of these projects is that interstate competition is producing a “race to the bottom,” which only has intensified as more and more states became aggressive in pursuing film projects. While pioneers in the field—first New York, and more recently New Mexico and Louisiana—only needed to compete with a handful of states, recent arrivals, such as Michigan and Georgia, have to create a place for themselves at the table by competing on the generosity of their tax incentives. Because Georgia and Michigan cannot yet compete with incentives like a trained workforce or sound stages, they are left with attracting film production using bigger tax incentives. This is, of course, detrimental to all states involved. Just as Michigan is left with the unenviable position of returning almost nothing on its investment for the next 3–5 years, Louisiana—and, to a lesser extent, New Mexico, thanks to its geographical proximity to Hollywood—are in danger of losing productions and having their trained workforce, and infrastructure, unengaged in the business they worked to build.

Because the interests of the producers and the states are diametrically opposed—the former vying for bigger incentives and the latter for greater returns on their investment—aggressive competition among the states favors the producers to the detriment of the states. If competition persists (or increases) it may even become a challenge to hold on to the gains already made, let alone successfully build entirely new industries. States must recognize that such competition is

28 Consider two examples: First is the film Annapolis, originally set to film “on location” in Maryland, but was lured at the last moment to Pennsylvania by a $10M incentive. Clearly, Pennsylvania would get no tourism boost from this successful movie if one was inspired by the movie to visit the naval academy. The second example is Runaway Jury, set in Mississippi, but filmed in Louisiana for similar reasons. It would stand to reason that Louisiana did not benefit from a tourism boost based on a movie set in Mississippi. Tax Me If You Can, Wall St. J., Mar. 14, 2009 at A8.

29 See State Film Incentives, supra note 7; see also Economic Research Associates, Project Report: Louisiana Motion Picture, Sound Recording, and Digital Media Industries (2009), http://louisianaentertainment.gov/film/files/IERA%20report/pdf.pdf. For example, while Louisiana had an exemplary year in 2007, with an estimated $763M in economic benefits—up from $576 in 2006, and $421M in 2005—its 25% production credit is not nearly as generous as some of its newest competitors in Georgia and Michigan, with 30% and 42% credits respectively.
economically detrimental to them, and that while big productions can infuse large sums of money into a local economy, better uses for state funds, which may produce greater returns on their investment, may exist.