

# FilmHawaii

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## Tax Incentives

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As if our spectacular locations, welcoming climate, and relative proximity to the U.S. mainland weren't enticing enough, the state of Hawaii offers three different tax incentives that may be applied to film and television productions:

### **15-20% Motion Picture, Digital Media, & Film Production Income Tax Credit**

This is a refundable tax credit based on a production company's Hawaii expenditures while producing a qualified film, television, commercial, or digital media project. The credit equals 15% of qualified production costs incurred on Oahu, and 20% on the neighbor islands (Big Island, Kauai, Lanai, Maui, Molokai).

### **100% High Technology Business Investment Tax Credit**

This credit was established by Act 221 in 2001 and amended by Act 215 in 2004, hence it is commonly referred to as "Act 221" or "Act 215." It is an income tax credit applicable to Hawaii taxpayers that invest in qualified companies producing "performing arts products," including film, television, video, audio, and animation products. The credit is equal to 100% of the investment amount, payable over five years.

### **Royalties Tax Exemption**

Royalties derived from performing arts products are excluded from a Hawaii taxpayer's income and not subject to state income tax.

For further information, contact the Hawaii Film Office at 808-586-2570 (<http://www.hawaiifilmoffice.com>) or the Hawaii Department of Taxation's Rules Office at 808-587-1577 (<http://www.state.hi.us/tax/index.htm>).

## **15-20% Motion Picture, Digital Media, and Film Production Income Tax Credit**

The *Motion Picture, Digital Media, and Film Production Income Tax Credit* is a refundable income tax credit based on a production company's Hawaii expenditures while producing a qualified film, television, commercial, or digital media project.

### **What is the tax credit?**

- The credit is calculated as a percentage of "qualified production costs" incurred in Hawaii
- The credit shall be claimed against the Hawaii taxpayer's net income tax liability for the taxable year in which the credit is properly claimed
- If the credit exceeds net income tax liability, the excess of credits over liability shall be refunded
- The credit was established by Act 88 in 2006 and is effective July 1, 2006 through December 31, 2015
- The credit is administered by the Hawaii Film Office and the Hawaii Department of Taxation

### **How much is the tax credit?**

- 15% of total "qualified production costs" incurred while filming on Oahu
- 20% of total "qualified production costs" incurred while filming on a neighbor island (Big Island, Kauai, Lanai, Maui, Molokai)
- There is an \$8 million cap per "qualified production"

### **Who is eligible for the tax credit?**

- A company that produces a "qualified production" that spends a minimum of \$200,000 in "qualified production costs" in Hawaii, and belongs to one of the following categories:
  - Feature film (narrative, documentary, experimental, student)
  - Short film (narrative, documentary, experimental, student)
  - Television movie
  - Commercial (an advertising message filmed within 6 consecutive weeks in Hawaii for dissemination via television broadcast or theatrical distribution)
  - Music video
  - Interactive game
  - Television series pilot
  - Single season (up to 22 episodes) of a television series regularly filmed in the State (if the number of episodes per single season exceeds 22, additional episodes for the same season shall constitute a separate "qualified production")
  - Television special
  - Single television episode that is not part of a TV series regularly filmed or based in the State
  - National magazine show
  - National talk show

### **Which "qualified production costs" are used in calculating the credit amount?**

- "Qualified production costs" must meet all of the following requirements:
  - Costs that are incurred in Hawaii
  - Costs that are subject to Hawaii's general excise tax or income tax (See TIR 2006-02: <http://www.hawaii.gov/tax/tir/tir06-02.pdf>)
  - Costs that have not been financed by investments for which an investment tax credit under Hawaii Revised Statutes §235-110.9 ("Act 221 credits") was or will be claimed
  - Costs that belong to the following general categories (not an exhaustive list):
    - (1) Costs incurred during preproduction, such as location scouting and related services;
    - (2) Costs of set construction and operations, purchases or rentals of wardrobe, props, accessories, food, office supplies, transportation, equipment, and related services;
    - (3) Wages or salaries of cast, crew, and musicians;
    - (4) Costs of photography, sound synchronization, lighting, and related services;
    - (5) Costs of editing, visual effects, music, other post-production, and related services;
    - (6) Rentals and fees for use of local facilities and locations;
    - (7) Rentals of vehicles and lodging for cast and crew;
    - (8) Airfare for flights to or from Hawaii, and interisland flights;
    - (9) Insurance and bonding; or
    - (10) Shipping of equipment and supplies to or from Hawaii, and interisland shipments.

## 15-20% PRODUCTION TAX CREDIT (continued)

### Are there additional requirements for claiming the tax credit?

- During production, a "qualified production" must:
  - Demonstrate reasonable efforts to hire local talent and crew. Such efforts must be reported on the "Hawaii Production Report" described below.
  - Provide evidence of financial or in-kind contributions or educational or workforce development efforts, in partnership with related local industry labor organizations, educational institutions, or both, toward the furtherance of the local film and television and digital media industries. Such contributions must be reported on the "Hawaii Production Report."
- Provide a screen credit or the like to the State of Hawaii, if applicable.
- Provide a DVD copy of the production and an electronic press kit (if one exists) to the Hawaii Film Office.

### Who is NOT eligible for the tax credit?

- Productions that spend less than \$200,000 in Hawaii
- Productions that belong to the following categories (not an exhaustive list):
  - Daily news
  - Public affairs programs
  - Non-national magazine or talk shows
  - Televised sporting events or activities
  - Productions that solicit funds
  - Productions produced primarily for industrial, corporate, institutional, or other private purposes
  - Advertising with internet-only distribution
  - Pornography

### How is the credit claimed?

- At least one week prior to the first Hawaii shoot date, a "qualified production" must register with the Hawaii Film Office by submitting a "Production Registration Form" to get pre-certified for the credit. The Film Office will issue a pre-certification acknowledgment to the applicant.
- No later than 90 days following the end of each taxable year in which "qualified production costs" were expended, a "qualified production" must submit a "Hawaii Production Report," detailed Hawaii expenditure report, and final crew list to the Hawaii Film Office. If, based on the information provided, the applicant qualifies for the credit, the Film Office will file a credit certification letter with the Department of Taxation, and provide a copy to the applicant. Note that the Dept. of Taxation is the ultimate arbiter of tax credit disbursements, and credit eligibility is ultimately subject to the Dept.'s review and, in some cases, audit.
- The applicant must then submit the following forms to the Department of Taxation on or before the prescribed deadline for the filing of your Hawaii income taxes: (1) Hawaii State Income Tax Return, (2) Form N-340, Motion Picture, Digital Media, and Film Production Income Tax Credit, (3) Schedule CR, Schedule of Tax Credits, and (4) Copy of credit certification letter. If the applicant has multiple qualified productions in any taxable year, it must aggregate on a single return the qualified production costs for which it is claiming the credits. (Caution: All claims, including any amended claims, must be filed on or before the end of the 12th month following the close of the taxable year for which the tax credit may be claimed.) Tax forms can be found at: [http://www.state.hi.us/tax/a1\\_forms.htm](http://www.state.hi.us/tax/a1_forms.htm).

### When and how will I receive my credit?

- The credit shall be claimed against the net income tax liability for the taxable year. "Net income tax liability" means net income tax liability reduced by all other credits allowed under Hawaii income tax law.
- If the credit exceeds your income tax liability, the excess of credits over liability shall be refunded to you, provided that no refunds or payment on account of the credits shall be made for amounts less than \$1.
- Approximately 6-8 weeks after the Hawaii Dept. of Taxation receives your tax forms, any refund will be sent to you in the form of a check or directly deposited into your bank account.

### Statutory and Tax References:

- Statute: HRS §235-17 (Established by Act 88 in 2006 via Senate Bill 2570, Conference Draft 1): [http://capitol.hawaii.gov/sessioncurrent/bills/sb2570\\_cd1\\_.htm](http://capitol.hawaii.gov/sessioncurrent/bills/sb2570_cd1_.htm)
- Tax Information Release (TIR) 2006-02: <http://www.hawaii.gov/tax/tir/tir06-02.pdf>
- General: Department of Taxation: <http://www.state.hi.us/tax/>

## **100% High Technology Business Investment Tax Credit**

Commonly known as "Act 221" or "Act 215", the *High Technology Business Investment Tax Credit* was originally established by Act 221 in 2001 and amended by Act 215 in 2004 as a means to encourage investment in high technology businesses and performing arts products, including film and television productions. The credit is an income tax credit equal to 100% of a Hawaii taxpayer's investment in a qualified business that produces performing arts products, distributed over a five-year period.

### **What is the tax credit?**

- This is a business investment tax credit designed to stimulate greater investment in Hawaii's high technology industry, and is applicable to the film and television industry.
- The credit is available to the Hawaii taxpayer for each investment in a "qualified high technology business" (QHTB). [Definition below.]
- The credit is deductible from the Hawaii taxpayer's net income tax liability.
- The credit applies to investments made in taxable years beginning on January 1, 2001 and ending on December 31, 2010.
- The credit is non-refundable.
- The credit is administered by the Hawaii State Department of Taxation.  
([http://www.state.hi.us/tax/a2\\_b2\\_6hi\\_tech.htm](http://www.state.hi.us/tax/a2_b2_6hi_tech.htm))

### **How much is the tax credit?**

- The tax credit is applied in percentages, spread out over five years, totaling 100% at the end of the five-year period.
  - 35% The year in which the investment was made.
  - 25% First year after which the investment was made.
  - 20% Second year after which the investment was made.
  - 10% Third year after which the investment was made.
  - 10% Fourth year after which the investment was made.
- The credit is capped at \$2 million per each investor's qualified investment in a QHTB, per year, and is credited to the investor at varying amounts over five years (Maximum per each investor's qualified investment: Year 1: \$700,000, Year 2: \$500,000, Year 3: \$400,000, Year 4: \$200,000, Year 5: \$200,000).
- If the tax credit exceeds the Hawaii taxpayer's income tax liability for any of the five years that the credit is taken, the excess of the credit over liability may be used as a credit against the taxpayer's income tax liability in subsequent years until exhausted.

### **Who is eligible for the tax credit?**

- Hawaii taxpayers who invest in a QHTB are eligible for the credit.
- To qualify as a QHTB, a company must pass an "activity test" or a "gross income test":
  - Activity Test: More than 50% of its total business activities are "qualified research" [Definition below] and the business conducts more than 75% of its qualified research in Hawaii, or,
  - Gross Income Test: More than 75% of its gross income is derived from qualified research, and this income is received from products sold from, manufactured in, or produced in Hawaii; or from services performed in Hawaii.
- Non-Hawaii taxpayers who invest in QHTBs cannot use the credits directly because they have no Hawaii income tax liability. However, they may still benefit from the credits by allocating them to Hawaii taxpayers. This is typically done via the formation of a partnership or an LLC that sets rules for the allocation of credits between the Hawaii taxpayers and non-Hawaii taxpayers.
- Eligibility for the credit is ultimately determined by the Hawaii State Department of Taxation. A company or its investors may confirm its QHTB status by submitting a request for a "Comfort Ruling" for a fee from the Hawaii State Department of Taxation. To request a "Comfort Ruling," go to [http://www.state.hi.us/tax/a2\\_b2\\_6hi\\_tech.htm](http://www.state.hi.us/tax/a2_b2_6hi_tech.htm). For details on fees required to obtain a "Comfort Ruling," go to Dept. of Taxation Announcement 2005-19: <http://www.state.hi.us/tax/announce/ann05-19.pdf>.
- For examples of how the credit is applied, go to Tax Information Release No. 2003-01: <http://www.state.hi.us/tax/tir/tir2003-01.htm>.

## 100% INVESTMENT TAX CREDIT (continued)

### How is the credit claimed?

- Any taxpayer or partnership (for income tax purposes) claiming this credit must:
  - (1) Before March 31<sup>st</sup> of each year, submit a properly completed *Form N-318A, Certified Statement of Investment in a QHTB and Claim of the High Technology Business Investment Tax Credit*, and/or *Form N-319A, Certified Statement of Research and Development Costs Incurred by a QHTB and Claim of the Tax Credit for Research Activities* to the Hawaii Tax Department. The forms can be found at [http://www.state.hi.us/tax/a2\\_b2\\_6hi\\_tech.htm](http://www.state.hi.us/tax/a2_b2_6hi_tech.htm).
  - (2) Attach the Department-issued certificates (sent only to taxpayers qualified for the credit *after* Form N-318A or N-319A are filed) to the tax return as a prerequisite to claim the credits. Investors and QHTBs will have until the Fall of that same year to file these certificates with their tax returns.
- Visit the high-tech tax incentives section of the Department of Taxation's Web site ([http://www.state.hi.us/tax/a2\\_b2\\_6hi\\_tech.htm](http://www.state.hi.us/tax/a2_b2_6hi_tech.htm)) for specific filing deadlines and to determine what additional forms may be required.
- In order for the credits to continue to be available during the four years following the initial investment, the QHTB must continue to qualify as a QHTB, the QHTB or interest in the QHTB must not have been sold by the investor, and the investor must not have withdrawn his investment wholly or partially from the QHTB. If these conditions are not met, the credit can no longer be claimed in subsequent years, and 10% of the credit already claimed in the two preceding taxable years will be recaptured from the investor.

### What are the fees associated with claiming the tax credit?

- There is a \$1,000 fee to request a "Comfort Ruling," and fees ranging from \$150-\$1000 to certify investment and research credits for credit claims over \$25,000. Other exemptions may apply. See the Tax Department site for more information: [http://www.state.hi.us/tax/a2\\_b2\\_6hi\\_tech.htm](http://www.state.hi.us/tax/a2_b2_6hi_tech.htm).
- For a full list of fees, go to Dept. of Tax Announcement No. 2005-19: <http://www.state.hi.us/tax/announce/ann05-19.pdf>.

### Definitions:

- **Qualified High Technology Business (QHTB):**
  - A business employing or owning capital or property, or maintaining an office in Hawaii, provided that:
    - More than 50% of its total business activities are "qualified research" [Definition below] and that the business conducts more than 75% of its qualified research in Hawaii, or,
    - More than 75% of its gross income is derived from qualified research, and that this income is received from products sold from, manufactured in, or produced in Hawaii; or from services performed in Hawaii.
  - In certain cases, a company's transactions must have "economic substance" (i.e., significantly change a taxpayer's economic position and have a substantial non-tax purpose) to qualify as QHTB.

## Royalties Tax Exemption

Amounts received by an individual or "qualified high technology business" as royalties, copyright, and trade secrets, are excluded from gross income, adjusted gross income and taxable income on the taxpayer's Hawaii state income tax filing. With respect to "performing arts products," this exclusion extends to:

- The authors of performing arts products, or parts thereof, with or without regard to the application of the work for hire doctrine under United States copyright law.
- The assignors, licensors, and licensees of any copyright rights in performing arts products, or any parts thereof.

### Definitions:

- **Qualified High Technology Business (QHTB):**
  - A business employing or owning capital or property or maintaining an office in Hawaii, provided that:
    - More than 50% of the total business activities are "qualified research" and that the business conducts more than 75% of its qualified research in Hawaii, or,
    - More than 75% of its gross income is derived from qualified research and that this income is received from products sold from, manufactured in, or produced in Hawaii, and services performed in Hawaii.
  - In certain cases, a company's transactions must have "economic substance" (i.e., significantly change a taxpayer's economic position and have a substantial non-tax purpose) to qualify as QHTB.
- **Qualified Research:**
  - Development and design of computer software for ultimate commercial sale, lease, license or to be otherwise marketed, for economic consideration. With respect to the software's development and design, the business shall have substantial control and retain substantial rights to the resulting intellectual property.
  - Biotechnology
  - Performing arts products [Definition below]
  - Sensor and optic technologies
  - Ocean sciences
  - Astronomy
  - Non-fossil fuel energy-related technology
- **Performing Arts Products:**
  - Audio files, video files, audio-video files, computer animation, and other entertainment products perceived by or through the operation of a computer; and
  - Commercial television and film products for sale or license, and reuse or residual fee payments from these products.

### References:

- General: Department of Taxation: <http://www.state.hi.us/tax/>
- Statute: Hawaii Revised Statutes (HRS) Section 235-7.3: [http://www.capitol.hawaii.gov/hrscurrent/Vol04\\_Ch0201-0257/HRS0235/HRS\\_0235-0007\\_0003.htm](http://www.capitol.hawaii.gov/hrscurrent/Vol04_Ch0201-0257/HRS0235/HRS_0235-0007_0003.htm)