Law 101 – The Brave New World of Production Incentives

By Mark Litwak

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I recently wrote an in-depth article for *Los Angeles Lawyer* magazine about production incentives (**www.marklitwak.com/downloads/LALawyer.pdf**) titled "Runaway Home." The article explains the trend toward generous production incentives offered by other nations and even other US states to lure producers away. This tendency was confirmed by several studies, including a report from the US Department of Commerce which estimated that in 2001, foreign tax incentives cost the US economy more than $10 billion per year.

Despite the unfortunate impact on the domestic economy, filmmakers need to be aware of the existence of production incentives, as well as the pros and cons of taking advantage of them.

Many countries consider their production incentives to be a reasonable and equitable device to level the playing field and enable their producers to compete against Hollywood. While some incentives are designed to attract production dollars from abroad into the local economy, other programs are meant just to protect local filmmakers and their native industry.

In 2002, US films attracted 70% of all moviegoers in the European Union. There were 665 million European admissions to US films in 2002, compared to 182.3 million admissions to European films in their own market. Ticket sales for European films outside their domestic market amounted to only 73.8 million. At the same time, foreign language cinema captures a mere .05% of the US box office.

The domination of American films is not purely an economic and trade issue. Foreign governments consider movies part of their culture, not just another export product. Motion pictures promote a country's language, customs, and attractions to audiences worldwide. Consequently, many governments encourage their citizens to create films, especially those with local content.

As a result of this competitive disadvantage and desire to promote their culture, many countries directly subsidize local film producers. Some have negotiated co-production treaties to encourage their producers to collaborate with producers of other nations and pool their resources. It bears noting that none of these treaties is with the United States. While these co-production agreements have undoubtedly helped some national cinemas survive, they have had unintended consequences as well. Because treaties require that technical and artistic participation be allocated among nationals from different countries, this can distort the creative process. An Italian actor, for instance, might be cast because of his nationality rather than because he is the best person for a part. European movies that become a mishmash of incongruous elements are sometimes referred to as "Euro-pudding." Many of these films have been criticized for their lack of artistic merit as well as their dismal box office performance.

Subsidy incentives come in a variety of forms. Location-based rebates are given to producers based on the amount they spend in a community. Canada, Luxembourg, Iceland and Australia, among others, offer such subsidies. While the rebate may not be disbursed until after production has been completed, sometimes funds will be advanced to the producer with the anticipated benefit as collateral. Other such incentives consist of free or reduced prices for locations, facilities, police, or permits.

Some incentive programs seek to support filmmaking by encouraging investors. The German film funds, the Netherlands' CV system of limited liability partnerships, French SOFICAs, and UK sales leasebacks are examples of this kind of incentive.

Loans on attractive terms may be used to draw productions. The UK and Italy have such programs (as does the state of New Mexico.) At the regional level, Germany also offers such support. The European Investment Bank, a European Union backed institution, offers loan guarantees.

France, Spain, and the Nordic countries have schemes in which a small slice of box office revenue is siphoned off to encourage future production. The EU's MEDIA Plus program uses box office revenue to assist distributors and exhibitors.

Many European countries provide subsidies and grants to films on cultural grounds. The Nordic countries provide significant support to encourage native filmmakers. The MEDIA Plus program provides script development and training funds.

In addition to evaluating the appeal of incentives enshrined in law, producers usually consider other benefits that can arise from moving a production. In Eastern Europe, South Africa, and China the wage scale is so low that crews, extras, and actors can be hired for a fraction of their rate in the United States. Likewise, food, lodging and construction can be a bargain. If a producer can purchase services for 20% of their customary price, then the producer receives the equivalent of an 80% subsidy without the burden of completing complicated paperwork and incurring legal and accounting fees.

Another factor to consider is the currency exchange rate. Canada and South Africa are attractive locations in part because the American dollar is strong compared to the local currency.

By international treaty, some countries encourage their nationals to collaborate with others by allowing them to aggregate incentives. These agreements allow its producers to pool financial, creative and technical resources with producers from other nations. The treaties lower the requirements that normally must be met in order for each producer to access incentives in their native land, and may reduce administrative burdens.

While the United States is not a party to any international co-production treaties, our filmmakers can contract on their own with foreign nationals. Even if no incentives are available, a local co-production partner may have the savvy and relationships needed to secure the best deals and ensure compliance with local regulations. Moreover, an American movie that includes a local director or star may enhance the commercial appeal of the film in that country, increasing the license fee obtainable.

Despite these financial attractions, distant locations may also present drawbacks and complications. Savings may be offset by increased travel and lodging expenses. Moreover, if a camera or critical piece of equipment fails in a remote location it can take days to fly in a replacement. If a crewmember becomes disabled, there may be a limited pool of skilled workers to draw upon for a substitute.

[*Mark Litwak is a veteran entertainment attorney and Producer's Rep based in Beverly Hills, California. He is the author of six books including:* Reel Power: The Struggle for Influence and Success in the New Hollywood, Dealmaking in the Film and Television Industry, Contracts for the Film and Television Industry, *and the recently published* Risky Business: Financing and Distributing Independent Film. *He is the author of the CD-ROM program Movie Magic Contracts, and the creator of the Entertainment Law Resources website at* ***www.marklitwak.com****. He can be reached at* ***law@marklitwak.com.***]