Section 181

How this Revised Provision Can Lower Production Budgets and Keep Film and Television Production in the United States.

In 2004, Congress enacted Section 181 of the Internal Revenue Code to create a federal tax incentive designed to combat runaway film and television production. In 2008, Section 181 was significantly expanded to cover larger productions.

This brochure is to help directors, producers and production executives understand how Section 181 can help reduce their film and television production costs when shooting projects in the United States.

DIRECTORS GUILD OF AMERICA DGA

Independent Film & Television Alliance®

Domestic Film Production Incentive Program

Revised Section 181 of the Internal Revenue Code

PRIMARY BENEFITS

Qualifying Film Expenses Immediately Deductible. Producers or active financial participants in qualifying film and television productions may elect to immediately deduct the cost of qualifying film expenditures in the year the expenditure occurs.

- Qualified film and television productions include any film or video tape production of a motion picture or television show whose costs would otherwise be required to be capitalized but for Section 181. Only the first 44 episodes, including the pilot production, of a television series are eligible under the law.

- In the case of a film co-produced by multiple investors, the deduction for qualifying expenditures must be allocated among the owners of the film in a manner that reasonably reflects each owner's proportionate investment and economic interest in the film.

- Qualified films do not include sexually explicit productions as defined in section 2257 of title 18 of the U.S. Code.

Qualifying Expenses Include the First $15 Million of Expenditures. The proposal applies to the first $15 million in production costs for qualifying film or television productions. This is a major expansion from the previous law which only applied to productions with production costs under $15 million.

- A higher expenditure cap of $20 million applies to productions the aggregate costs of which are "significantly incurred" in: a) areas eligible for designation as a low-income community under the New Markets Tax Credit program,[1] or b) areas eligible for designation by the Delta Regional Authority as a distressed county or isolated area of distress.

- As defined by the New Markets Tax Credit program, qualifying low-income communities include any census tract if (a) the poverty rate for such tracts is at least 20%; or (b) (1) in the case of census tracts not located within a metropolitan area, the median family income for the tract does not exceed 80% of statewide median family income, or (2) in the case of a tract located within a metropolitan area, the median family income for the tract does not exceed 80% of the greater of statewide median family income or the metropolitan area median family income. Information on qualifying communities can be found at: **http://www.cdfifund.gov/what_we_do/programs_id.asp?programID=5**

- A list of areas eligible under the Delta Regional Authority statute as distressed counties or isolated areas of distress can be found at: **http://www.dra.gov/about/maps.aspx**

- The IRS temporary regulations (T.D. 9312) outline two alternative tests to determine if costs are "significantly incurred" in qualifying low-income areas. The first test is based upon production costs and establishes a 20% threshold for the test. It compares production costs incurred in first-unit principal photography that takes place in a designated area to all productions costs incurred in first-unit principal photography. This does not include preproduction, editing and post-production costs. The second test is based upon the number of days of principal photography. If at least 50% of the total days of principal photography take place in the designated area, the production will be deemed to satisfy the significantly occurred test.

Definition of Qualifying Production. To qualify, at least 75% of the total compensation expended on the production must be for services performed in the United States.

- Qualifying compensation includes payments for services performed in the United States by actors, directors, producers, and other relevant production personnel. Compensation does not include participations and residuals.[2]

Tax Benefit Duration. This revised domestic film production incentive program – covering the first $15 million of costs of all productions -- will be in effect for qualifying productions commencing after December 31, 2008 and before January 1, 2012.

THIS HANDOUT IS FOR INFORMATIONAL PURPOSES ONLY AND SHOULD NOT BE VIEWED AS TAX ADVICE WITH RESPECT TO YOUR PRODUCTION ACTIVITIES. FOR SUCH ADVICE, YOU SHOULD CONSULT WITH YOUR TAX ADVISOR.

[1] As defined in section 45A of the Internal Revenue Code.

[2] As defined in section 167(g)(7(B) of the Internal Revenue Code

FREQUENTLY ASKED QUESTIONS

Q: What are the key changes to Section 181 that were enacted in 2008?

A: Section 181, was first enacted by Congress in 2004 to apply only to films with total production costs under $15 million. In 2004, it was significantly modified so that the first $15 million ($20 million in the case of productions in certain low-income and eligible areas of the country) of all qualifying film and television shows may be immediately written-off for tax purposes. This now makes the incentive available for film and television productions of all sizes, small or large.

Q: When do productions need to commence to qualify for the new incentive?

A: The incentive, is one of a number of temporary tax provisions in the Internal Revenue Code which must be extended on a periodic basis. The current provision is in effect for qualified productions commencing after December 31, 2008, and before January 1, 2012.

Q: Can the immediate write-offs be taken in more than one year?

A: Yes, if an election is made to use the incentive, the immediate deduction takes place in the year the expenditure is incurred. Therefore, if production expenditures are incurred in more than one year, the immediate tax deduction will be taken in more than one year.

Q: When, where, and how does the "election" to immediately deduct the qualifying expenditures apply?

A: The election is to be made on the tax return for the taxable year in which the production costs are first incurred. The election must be made by the due date (including extensions of time) of such return.

Q: What tax form do I need to fill out to get the incentive?

A: Currently, there is no specific form to fill out. The IRS temporary regulations require that you declare in a separate statement that you are electing to utilize Section 181. The legislative history also states that: "deducting qualifying costs on the appropriate tax return shall constitute a valid election." Therefore, deducting the production costs (that would otherwise be capitalized) on your tax return will qualify as electing to take advantage of this incentive.

Q: Does it apply to all productions (e.g., big budget productions)?

A: Yes, as mentioned above, the immediate write-off provision now applies to the first $15 million (or $20 million in low income or distressed areas) of costs for all productions regardless of the aggregate cost of the project.

Q: What is the real benefit of this incentive?

A: This is a significant Federal tax incentive that allows producers of qualifying productions to take an immediate tax deduction for the full or partial costs of a production in the year the cost is incurred (as opposed to having to spread or amortize those costs over a period of years beginning after the film goes to market).

Q: How do I determine if it is beneficial to my production?

A: Since the new incentive is elective, producers can run numbers with or without the new incentive and determine whether or not to elect to immediately expense the production costs in the first year(s).

Q: Is the incentive transferable?

A: No. However, depending on the investment structure you choose, multiple parties may be able to properly allocate costs that could be immediately expensed.

Q: What happens in the case of a co-production or a film financed by multiple investors?

A: The $15 million ($20 million) threshold refers to the qualifying film. The benefits of the provision must be allocated among the owners of a film in a manner that reasonably reflects each owner's proportionate investment in and economic interest in the film.

Q: In order to qualify for the higher ($20 million) deduction, what does it mean to require that a "significant" amount of the expenditures be incurred in an eligible area?

A: The IRS temporary regulations outlined two alternative tests to determine if the "significantly occurred" requirement is met. One test is based upon production costs and establishes a 20% threshold for the test. It compares production costs incurred in first-unit principal photography that takes place in a designated area to all productions costs incurred in first-unit principal photography. This does not include preproduction, editing and post-production costs. The second test is based upon the number of days of principal photography. If at least 50% of the total days of principal photography take place in the designated area, the production will be deemed to satisfy the significantly occurred test.

Q: How will other practical issues related to this broadened incentive be determined?

A: Like other tax issues, producers should consult with their professional tax advisors on any issues related to this new Federal tax incentive. In light of the new legislation, the Treasury and IRS may revise their temporary regulations, which may come in the form of Notices and Regulations. A number of groups that worked on this important legislative change are expected to continue working with the Treasury Department and the IRS to ensure the incentive fulfills its objective and provides the industry with meaningful tax relief.

Q: Are there other Federal tax incentives that may be valuable to film productions?

A: Yes, all US based productions continue to have other potential incentives including a 9% tax deduction from gross revenues for U.S. film and television production activities (Section 199). Producers should consult with their professional tax advisors for other tax incentives that may be available.

Independent Film & Television Alliance®

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The DGA and IFTA have worked with a coalition of film industry organizations for over ten years to stem the tide of runaway production. The current effort focused on amending Section 181 to make the United States a competitive place for film and television production. Combined with the incentives that many states have enacted, DGA and IFTA believe that the federal incentive will serve as an effective tool to keep more television and film production in the United States.

Runaway Production Alliance Members:

Academy of Television Arts and Sciences
American Federation of Musicians
American Federation of Television and Radio Artists
Association of Independent Commercial Producers
Association of Talent Agents
The Caucus for Television Producers, Writers and Directors
Directors Guild of America
Film Musicians Secondary Markets Fund
Hollywood Post Alliance
International Alliance of Theatrical Stage Employees
Producers Guild of America
Independent Film & Television Alliance
International Brotherhood of Teamsters, Local 399
Recording Musicians Association
Screen Actors Guild
US Film Commission Caucus, Association of Film Commissioners International

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