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**From programming** shot in studios in Burbank to cutting-edge special effects and animation conjured up by digital artists in the San Francisco Bay area, film and television production is a significant part of the California economy – as well as a bedrock element of the state’s identity and image. But past dominance is no guarantee of future prosperity.

Make no mistake: motion picture and television production in California remains strong. Hollywood is still the clear leader in terms of economic output and innovation, and California’s entertainment-industry employment levels far exceed those of the rest of North America. In 2008, 160 movies and 320 television programs were filmed in the state. The two employment categories that make up the entertainment industry (motion picture and video recording – which also encompasses post-production – and independent artists, writers and performers) together generated \$25 billion in output and sustained 167,000 jobs. California’s robust infrastructure and critical mass of talent, supported by a variety of strong allied industries, have contributed to maintaining its supremacy.

But the state’s mantle is slipping. The high costs of living and doing business have prompted producers to look elsewhere. Producers are finding it more cost-effective to

film in other locations, despite the fact that most of the industry talent lives in California. Smaller films made for limited release are rarely filmed in California, and even large-budget films have achieved significant savings by going out of state – or out of the country.

Forty-one other states and the District of Columbia are currently vying for a piece of the \$57 billion United States film-production industry by offering tax incentives. New York, North Carolina, Louisiana and New Mexico have all made significant inroads in attracting this commerce, and Georgia is coming on strong. Although other locations, including Michigan, have been aggressive in providing tax breaks and other incentives to film locally, the four states mentioned above have now built a true critical mass of production and post-production activity that can sustain ongoing work, rather than just landing one-shot projects. New York, in particular, has the built-in appeal of being a hub of the entertainment industry and a major cultural capital, with a strong concentration of television, radio and theater talent.

Competition, moreover, does not come just from inside the United States. Many other

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countries have long had successful local film industries. But thanks to Hollywood's vast marketing reach and superior filmmaking technology, most film-based revenue has historically been captured by the United States. However, the size of the pie that's up for grabs has prompted several countries to intensify their effort to lure American productions to augment their indigenous film industries.

Countries vying for a piece of the American-based industry include Canada, Australia, New Zealand, Britain, Germany and India. A

combination of financial incentives and the existence of the quality infrastructure that had already been established for their own national movie and television industries have made them increasingly successful in landing American productions.

Canada, where film production is a leading industry, is the most striking example. Film contributed nearly \$8 billion (U.S.) to Canada's economy in 2008. Vancouver, Montreal and Toronto are now considered top locations for filming, approaching the caliber

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of Los Angeles and New York.

Although Canada had been home to the occasional film and television production in the 1970s and 1980s, the industry really took off in the late 1990s. Canada's concerted push also coincided with a period of favorable exchange rates against the American dollar, which made Canada a relatively cheap place to do business in general. But the key to Canada's ongoing success has been a potent combination of financial incentives, lower labor costs, skilled English-speaking workers and short flying time to the United States.

Employment in California's movie and video industry (encompassing production, post-production and independent artists) reached its peak in 1997. The state's share of North American employment in the industry has since declined from 40 percent (1997) to 37.4 percent (2008). Our research concludes that if California had managed to retain the 40 percent share it once enjoyed, some 10,600 jobs, paying an average wage of about \$92,000, would have been preserved.

California has acknowledged the drain, and in July 2009, introduced a tax credit for projects filmed in state with budgets of \$75

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After 2002, Canada found itself faced with increased competition from a number of localities in the United States that adopted their own financial incentives and launched aggressive marketing campaigns. Its provinces responded both by introducing a second layer of incentives on top of those offered by the federal government, and by bolstering their local infrastructure. Vancouver's capabilities are now so sophisticated that the city has become the main center for television filming in North America outside of Los Angeles and New York.

As noted, California still leads the nation in production, turning out 160 films in 2008. It's worth considering, though, that the number of movies either wholly or partially filmed in California has fallen sharply: 272 were made in the state in 2000.

million or less. The credit is designed to offset lower costs (and government subsidies) offered elsewhere.

While this is a positive first step, it makes little sense to exclude big-budget films (which have the most impact on jobs and incomes) from the incentive program. This became apparent recently as filming got under way for the latest installment of the *Transformers* film franchise: While Los Angeles captured much of the production, it lost six weeks of shooting to Michigan and Illinois, with producers citing the subsidies offered there. Due to its \$200 million budget, this film did not qualify for tax credits in California.

An onerous permit process, increased restrictions and city-imposed moratoriums on location filming driven by residents' complaints, along with a lack of highly functional

industrial space, are further eroding California's appeal to filmmakers. Faced with rising costs, increased competition, lower profits, and, in the case of some publicly traded companies, increased pressure from shareholders, executives of studios in the United States have had to find innovative ways to cut costs. A growing number of states and foreign countries are courting these producers with competitive tax breaks, even establishing offices in Los Angeles to market themselves.

The places most successful in attracting filmmakers offer incentives with less restrictive qualification criteria. And they have been able to adopt innovative policies to ensure the availability of high-quality infrastructure and labor, cut the red tape in getting permits, provide adequate security and address local concerns about noise, traffic and other issues.

Data from FilmL.A., a nonprofit organization that coordinates permits for on-location shooting, shows a strong increase in production days in Los Angeles for the first two quarters of 2010, which the group largely attributes to the new state incentives. While this is an early positive sign, the battle isn't won yet. We conclude that to expand film and television production, California will also need to take the following steps:

**Track film production data more effectively** to determine how many days of production are spent within the state versus other locations, along with the utilization rates of studio soundstages and similar facilities.

**Create a balanced two-tier film incentive program**, with one set of benefits to engage big-budget studio films that are not covered under the current incentive program and another to attract smaller independent productions, including those intended for cable TV.

**Expand the current tax credit for television production** to encompass network and premium cable shows.

**Make the tax incentive programs permanent**, signaling a long-term commitment to retaining the industry.

**Consider a new digital media tax credit** to attract and retain developers of digital animation, visual effects and video games.

**Encourage long-term investments in infrastructure** by implementing tax credits for building or upgrading studio and post-production space.

**Improve the ability of local film commissions to coordinate with local authorities** in expediting the film-permit process.

**Create proactive marketing and outreach strategies** to communicate new incentives and programs.

**Establish cooperative relationships with civic and industry leaders** beyond the state's borders to attract foreign-funded productions.

One route to implementing several of these recommendations would be to provide the California Film Commission (which is part of the state's Business, Transportation & Housing Agency) with more staff and marketing resources. The commission could then take on the task of comprehensive data collection, establishing the capacity to monitor the health and development of a crucial industry, and to gauge the effectiveness of public policy. Industry data is currently inconsistent and often incomplete – a problem that needs to be corrected, given the importance of film to the state's economy.

In addition to measures carried out at the state level, some promising initial steps have recently been taken by the City of Los Angeles. It does not have its own tax-credit program, but the City Council did recently pass film-friendly initiatives to “keep Hollywood home.” The program extended the free use of city-owned buildings, added more access for film producers to city-owned parking spaces, delegated the Department of Water and Power

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to install energy nodes around the city to accommodate filming equipment and reduce energy-related costs to filmmakers, and mandated the creation of a film coordinator within the Recreation and Parks Department.

But Los Angeles could go further by giving the film industry an all-purpose ombudsman in city government. With one person installed in City Hall to serve as a liaison to FilmL.A., the city would be better able to cut through the bureaucracy to obtain filming permits from various city and county agencies.

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Given the state's gaping budget deficit, there is no denying that California can barely afford to provide tax breaks. But in this case,

it can't afford not to. The state can't squander opportunities to retain and add significant numbers of high-paying jobs. And the long-term payoff to be realized in shoring up a major industry far outweighs the short-term cost in revenues.

That said, the state should not attempt to match incentives from other locations that provide large upfront cash advances and unsustainably large film credits. However, by providing somewhat more generous and more effectively targeted credits that lower the cost of production to a reasonably competitive level, California will position itself to win over producers based on its strengths in human capital and facilities, as well as its reputation for excellence. **M**



## And the guy on the spine is...

**Simon Johnson**, a macroeconomist who now teaches at MIT's Sloan School of Business. Formerly the low-profile (but very competent) chief economist at the IMF, Johnson morphed from Clark Kent to the Superman of center-left economics – a public intellectual in the same league as Paul Krugman – when he returned to academia in 2008. He is probably most famous for his 2009 article in *The Atlantic Monthly*. There, he explained how well-connected investment bankers had taken control of U.S. economic policy in a “quiet coup” that culminated in the Great Recession.

Today, it's hard to surf the Web without bumping into his well-reasoned arguments in defense of tougher regulation of the financial services industry, and in opposition to deficit hawks willing to risk the economic recovery in order to put Washington's fiscal house in order. For a proper dose of Johnsonomics, check out his blog, *BaselineScenario.com* (written with James Kwak), his contributions to the *Economix* blog at *The New York Times*, or his book, *Thirteen Bankers: The Wall Street Takeover and the Next Financial Meltdown* (also with Kwak).