



GLENN A. CUNHA
INSPECTOR GENERAL

The Commonwealth of Massachusetts
Office of the Inspector General

JOHN W. McCORMACK
STATE OFFICE BUILDING
ONE ASHBURTON PLACE
ROOM 1311
BOSTON, MA 02108
TEL: (617) 727-9140
FAX: (617) 723-2334

July 27, 2018

The Honorable Joan B. Lovely, Vice Chair
Senate Committee on Ways and Means
State House, Room 413A
Boston, MA 02133

The Honorable Jeffrey Sánchez, Chairman
House Committee on Ways and Means
State House, Room 243
Boston, MA 02133

Dear Vice Chair Lovely and Chairman Sánchez:

As you consider the economic development bills passed by each branch, I would like to address section 60 of House bill 4732, *An Act relative to economic development in the Commonwealth*. House 4732 creates a theater tax credit similar to that currently available for films but with even fewer safeguards. I am opposed to the creation of such a tax credit. However, any tax credit should have stringent safeguards to prevent abuse and to ensure that the Commonwealth benefits fully from the establishment of the credit. The current language does not contain the necessary safeguards.

As currently proposed the theater tax credit is not structured to benefit the Massachusetts economy. While there is a higher tax credit for in-state costs, the bill still allows out-of-state costs, to count towards the credit. House 4732 establishes a tiered tax credit program that grants a 35 percent tax credit for in-state costs, including labor, and a 25 percent tax credit for in-state production and performance expenditures and out-of-state labor costs. Expenditures including but not limited to, set design, special and visual effects, costumes, advertising, public relations and payroll qualify for the tax credit equaling 25 percent. If a company can receive the same 25 percent credit for out-of-state labor costs, there is little incentive to hire a Massachusetts-based company or employee for these types of expenditures. Transportation of cast, crew and equipment is also eligible. Consequently, an applicant could hire an out-of-state contractor to do work in Massachusetts, or could purchase supplies from another state to be delivered to Massachusetts. For example, a theater company could construct the majority of the set outside of Massachusetts and then transport it to a local theater. Both of these expenditures would qualify for the 25 percent tax credit, but they would not benefit the

Massachusetts economy. The writing of a script or pre-production that takes place out of state would also be eligible for the tax credit. Qualified expenditures should only be those that directly benefit Massachusetts businesses or residents.

Further, all salaries, wages, fees and other compensation paid to non-residents should carry a minimum state withholding tax. Any gains associated with the transfer, sale or assignment of the tax credit should be subject to a minimum state withholding tax and should be payable by the applicant who originally received the eligible theater production certificate. No theater production certificate should be issued to an applicant with any outstanding Massachusetts tax obligation.

House 4732 does not have the necessary safeguards to prevent fraud and abuse. Other tax credits, including the film tax credit, cap credits at 25 percent of costs. Even with a \$5-million-dollar limit for theater tax credits, there are no provisions requiring that a certain percentage of production expenditures be made in Massachusetts. A company applying for the film tax credit program is only eligible for the production tax credit if the in-state production expenses exceed 50 percent of the total production expenses or at least 50 percent of the days spent filming are completed in Massachusetts. These two safeguards ensure that companies focus on hiring Massachusetts-based companies and employees. I highly recommend adding similar requirements to a theater tax credit program.

Independent oversight is essential to ensure that those applying for a tax credit are truly eligible and that they present verifiable documentation as part of that application. Currently, House 4732 allows the Department of Revenue (“DOR”) and the Massachusetts Office of Travel and Tourism (“Office of Travel and Tourism”) to review a company’s eligibility based solely on an accountant’s certification, without an independent investigation. An independent public accounting firm licensed in the Commonwealth should audit the production and performance expenditures (“expenditures”), DOR should establish minimum review criteria, and the public accountant should attest to the accuracy of these expenditures. DOR should qualify public accounting firms for this purpose and maintain a list of qualified firms.

Furthermore, an applicant should submit the tax credit application and documentation of its expenditures under the pains and penalties of perjury. The applicant should be required to retain all records relating to the theater tax credit for at least seven years. The Inspector General should have access to these records, and any relevant DOR records, for the purpose of independent verification. All documents, including tax returns, submitted during the two-step eligibility and certification process should be submitted directly to the Inspector General for analysis. Many tax credit programs have few oversight mechanisms and many have not been subject to significant review. Access to these documents allows the Office to uphold its mandate to prevent and detect fraud, waste and abuse. All submissions and findings related to theater tax credits should be public documents. Additionally, the Office of Travel and Tourism, in consultation with DOR, should issue an annual report analyzing the economic impact of the tax credit on the Commonwealth.

Vice Chair Lovely and Chairman Sanchez

July 27, 2018

Page 2 of 3

Additionally, the language as drafted is flawed. For example, section 60 defines “payroll” but then refers to “labor costs” later in the section in terms of what is eligible for the tax credit. It also appears that payroll could be counted twice, once as labor costs and then again as a production and performance expenditure.

As Inspector General and a former prosecutor, I have seen instances in which tax credits and similar programs have been abused. For example, parties using the film tax credit program overstated costs and included purchases, such as personal vehicles, that did not qualify under the program. Had safeguards similar to those discussed above been in place, the abuses would not have occurred and the Massachusetts taxpayers would have been protected.

Again, I am opposed to the creation of a theater tax credit. If this legislation were to pass, it must have strong oversight provisions to prevent fraud and to protect the Commonwealth.

Sincerely,

A handwritten signature in blue ink that reads "Glenn A. Cunha". The signature is fluid and cursive, with the first letters of the first and last names being capitalized and prominent.

Glenn A. Cunha
Inspector General