



Utilizing Tax Incentives to Cultivate Cultural Industries and Spur Arts-Related Development

A report prepared for the
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INTRODUCTION

The cultural industries have increasingly been recognized as one of the leading economic clusters in the Louisiana economy. The cultural cluster, as defined by the Office of Culture, Recreation and Tourism, includes the following industries: culinary arts, design, entertainment, performing arts, literary arts, and preservation. Together, the nonprofit institutions, individual artists and performers, and commercial businesses in this cluster provided at least 144,000 jobs in Louisiana prior to Hurricanes Katrina and Rita in 2005. As the state seeks to rebuild its cultural economy and to help make culture one of the core engines of the state's recovery, it needs to look creatively at all of the potential economic tools that could be utilized to help bring its creative talent back, to promote the growth and development of cultural production within the state, and to support entrepreneurial development within the cultural economy.

Louisiana has the opportunity to be extremely bold and put together one of the most comprehensive sets of legislative initiatives in the world aimed at supporting individual artists and cultural industries. We are recommending that the state package its current support efforts together into three legislative initiatives:

- 1) *The Status of the Artist Act*: Modeled after similar legislation proposed by UNESCO, enacted in Canada, and currently being expanded in Canadian provinces, this legislation could include special tax exemptions for individual artists, musicians, writers, and performers. In addition, it could include provisions aimed at protecting Louisiana "originators" of cultural products.
- 2) *Cultural Industries R&D and Promotion Act*: This legislation would expand the current tax credits available to the film, digital media, and sound recording industries to all industries defined as being part of the cultural economy. The Act would also ensure that the state R&D credits be applied to the cultural industries and the types of research and development activities that are undertaken in these industries.
- 3) *Community Cultural Development Act*: This legislation would target artist housing, historical preservation, and sales tax-related exemptions to specified cultural development districts within the state.

This memo examines how tax incentives are being utilized to promote the development of the cultural economy in other places and includes examples of various tax incentives at work throughout the country, as well as overseas. Based on a scan of current practice,

tax incentives are categorized and examined in three major categories: artist-based incentives, place-based incentives, and industry-based incentives. The recommendations build upon the learning from this analysis.

The Louisiana Context

Tax incentives are an increasingly popular tool to promote the growth of creative industries and arts-related revitalization in communities across the U.S., as well as overseas. The state of Louisiana was at the forefront of these efforts. Since passing the Louisiana Motion Picture Incentive Program in 2002, the state has added the following tax-related incentives aimed at building the cultural economy:

- **Motion Picture Tax Credits:** Act 456 in 2005 strengthened and expanded the existing film industry tax credits by increasing the percentage of the allowable credit to individual taxpayers for investments in state certified productions, and for infrastructure projects to 25 percent for investments over \$300,000. An additional 10 percent is allowed for payroll for Louisiana residents.
- **Sound Recording Investor Tax Credit:** Tax credits are offered to individuals and corporations investing in state certified musical recording production and infrastructure projects. The amount of the credit is 10 percent of the investment for projects between \$15,000 and \$150,000, 15 percent for projects between \$150,000 and \$1 million, and 20 percent for projects over \$1 million.
- **Digital Interactive Media Producer Tax Credit:** State certified production activities involved in the production of electronic media, most notably video games, can receive tax credits of 20 percent of the base investment in the first two years, 15 percent in the third and fourth years, and 10 percent in the fifth and sixth years. Tax credits could be carried forward for up to 10 years or sold to another taxpayer.
- **Exemption of Consigned Arts from Ad Valorem Taxes:** Louisiana is the only state that imposes an inventory tax on artists who sell artwork on consignment through a dealer or gallery. The law requires inventory taxes be paid on any “material result of a creative endeavor,” including sculpture, photographs, glassworks, furniture—virtually anything handmade of value. In 2005, the Louisiana Legislature passed a proposed constitutional amendment that would exempt from ad valorem property tax all artwork listed as consignment art by an art dealer. This was one of the ballot questions in the November election. Constitutional amendment #5 passed with 54 percent support on November 7, 2006.
- **Historic Tax Credits:** Recent legislation extended the state’s ability to give historic tax credits in downtown development districts increasing the allowable credit for revenue producing property from \$250,000 to \$5 million.

In addition to these incentives specifically aimed at cultural industries, there are other tax-related incentives in Louisiana that have the potential of helping the cultural industries. These include:

- **The Research and Development Tax Credit:** Currently, Louisiana offers companies or individuals who have either taken a federal R&D tax credit, or received a federal

SBIR grant, to be able to earn a credit against state income or corporation franchise tax liabilities. The credit may be carried forward for up to 10 years and, in some cases, sold. Companies must be certified by the Department of Economic Development in one of the clusters described in Louisiana Vision 2020, the 2003 update. In terms of the cultural industries, entertainment is listed.

- Angel Investor Tax Credit: Act 400 in 2005 provides angel investors with a 50 percent tax credit for investments in Louisiana Entrepreneurial Businesses. These credits are capped at \$5 million a year. Excluded activities include retail sales, real estate, professional services, gaming, financial services, and natural resource extraction.

In addition to these tax incentives that are either directly related to the cultural industries or could be utilized for the cultural industries, Louisiana has a wider range of more general economic development incentives including the Quality Jobs Program, which provides a 5 percent or 6 percent annual cash rebate for total payrolls for companies locating in Louisiana. This tax incentive is limited to biotechnology, micro-manufacturing, software, internet and telecommunications, environmental technology, food technology, and advanced materials. The state also has a generous property tax exemption program for manufacturing establishments entering or expanding in Louisiana.

A CULTURAL ECONOMY TAX POLICY FRAMEWORK

A scan of tax incentives to cultivate creative industries and spur arts-related development around the world reveals a variety of approaches and strategies. States use tax incentives to encourage particular kinds of behavior and activity including: recruitment of artists to specific communities to spur revitalization; the rehabilitation of industrial and historic buildings for artist live/work space; and the growth of creative industries that employ a large number of artists, musicians, filmmakers, and designers. Arts-related tax incentives can be grouped into three general categories:

Artist-based Tax Incentives

- Artists are eligible for income tax exemption from sale of their work regardless of place of residence within a state or country, i.e., universal benefit.
- Artists do not have to pay taxes on royalty income.

Place-based Tax Incentives

- Artists are eligible for income tax exemption from sale of their work if they live/work in a designated “arts district.”
- Galleries and theaters are exempt from sales, amusement, and admissions tax if they locate in a designated “arts district.”
- Artists are eligible for income tax exemptions and property tax abatements if they live in and rehabilitate designated industrial and historic buildings, thereby increasing property values and spurring revitalization.

- Developers and property owners are eligible for state historic tax credits if they rehabilitate designated industrial buildings.

Industry-based Tax Incentives

- Designated “creative” industries (e.g., film, television, sound recording, etc.) are eligible for tax credits based on how much production and related spending occurs in a given state or country.
- Research and development activities of cultural industries are included in state R&D tax credits.

The following sections of the memo build out each category, discuss pros and cons, and provide illustrative examples.

INDIVIDUAL ARTIST-BASED TAX INCENTIVES

Types of Incentives

There has been some experimentation with the use of tax incentives to attract creative talent and support individual artists. Most common in the U.S. are tax breaks for artists tied to revitalization and smart growth efforts, i.e., artists become eligible for income tax breaks if they live and work in designated arts and cultural districts. (See place-based approaches below.) In a scan of national and international models we found three examples of universal tax credits for creative occupations.

▶ Irish Artists’ Tax Exemption

The *Irish Artists’ Tax Exemption* provides an exemption from income tax and surtax for earnings (royalties, sales of bodies of works) up to 250,000 pounds each tax year from “original and creative work that has either cultural merit or artistic merit.” For those qualified artists whose income is greater than 250,000 pounds, tax exemption relief is limited to 50 percent of income. Original and creative work is defined as any unique work that is brought into existence for the first time as an independent entity by the use of its creator’s imagination. Interpretive artists are *not* eligible for the tax exemption, e.g., dancers, actors, and performers. In addition, works created for advertising do not qualify. In order to qualify for the tax exemption, the artist must be a resident or ordinarily reside in Ireland. Certain exemptions are granted on a case-by-case basis for residents living abroad.

Eligible Categories for Artist Tax Exemption (Ireland):

- books or other forms of writing (including certain categories of non-fiction);
- plays;
- musical compositions;
- painting or other like pictures;
- sculpture.

Based on Ireland’s success, the Scottish National Party (SNP) is now considering a similar exemption in an effort to galvanize the arts sector and encourage creative people to live and work in Scotland.¹

▶ **Hawaii High Technology Business Investment Tax Credits**

Within Hawaii’s more extensive tax credit legislation aimed at high technical industry—Act 221—there is a provision that excludes royalties derived from patents, copyrights, or trade secrets from an individual’s income. This exclusion extends the authority to so-called “performing arts products.” For the purpose of the Act, performing arts products are defined as:

- 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 for these products.

▶ **Province of Quebec Artist Exemption**

Quebec has had a longstanding provision in its tax code that provides writers, artists, filmmakers, musicians, performers, and anyone who produces copyrighted materials with a tax exemption. The justification for the Quebec exemption was that artists, creators, and producers provided the equivalent of the research and development that the province supports in other industries.² Targeted artists receive a \$15,000 tax exemption for all copyright income up to \$20,000. The exemption for every dollar over \$20,000 is reduced by \$1.50. The total exemption is for up to \$30,000. Both Saskatchewan and Ontario are in the process of considering similar tax exemptions.

▶ **Income Averaging by Artists**

While not a tax credit, there are also tax measures in other countries that seek to “smooth out” the very variable income of artists. For example, in Sweden, artists are able to create special bank accounts and only pay taxes as they withdraw money from these accounts. Other countries including Australia, Germany, the Netherlands, and the UK allow artists to average their income to compensate for the big fluctuations in salary from year to year.

Analysis of Incentives

▶ **Most beneficiaries of the Irish tax exemption are artists who do not earn a lot of income.**

There has been relatively little analysis of these types of incentives for individual artists. The experience in Ireland, where the incentive has been in place for a relatively long time, is probably the most instructive. The tax exemption is widely credited with

¹ Source: SNP plan “tax holiday for artists” policy. See <http://www.sundayherald.com/print56989>.

² See Clare McAndrew, “Artists, taxes and benefits an international review,” December 2002. Arts Council of England, London. <http://www.artscouncil.org.uk/documents/publications/316.doc>.

galvanizing Ireland’s arts sector. Though hard numbers on artist relocation are not available, the group *Visual Artists Ireland* claims the exemption has “resulted in many artists, musicians, and writers locating in Ireland to avail of its benefits.”³

In 2005, the Irish Finance Minister proposed capping or abolishing the artist tax exemption. The tax exemption has been criticized for providing huge benefits to a small number of big acts (e.g., the band U2) and famous writers. The tax exemption was vehemently defended, and ultimately preserved, by arts groups in Ireland including the *Arts Council*, the principal instrument of arts funding and advisor to government on arts matters, and *Visual Artists Ireland*, a professional membership and advocacy organization representing individual artists.

Arts groups demonstrated that a small minority of claimants are high earners and that half of claimants earn 10,000 pounds per year or less from the sale of original artwork. Data from 2001 showed that of the 1,323 artists that filed for the exemption that year, 694 earned 10,000 pounds or less while only 59 earned 200,000 or above.⁴ At the same time, however, of the roughly 80 million pounds that were exempt from income tax in 2001, only 2.7 million were earned by artists earning less than 10,000 per year. Over half of all tax exempt income in 2001 (approximately 46 million pounds) was earned by artists earning between 500,000 and 10,000,000 per year. (See following table for breakdown.)

Irish Tax Exemption 2001: Distribution of Exemption by Income⁵

Range of Income (in pounds)	No. of Claimants	Income Subject to Exemption
5000 or less	446	916,555
5001-10,000	248	1,796,686
10,001-50,000	456	9,867,796
50,001-100,000	75	5,411,767
100,001-200,000	39	5,298,712
200,001-500,000	31	10,092,434
500,001-10,000,000	28	46,631,197
Totals	1,323	80,015,197

In 2001, the tax exemption cost the Irish government approximately 37 million pounds in foregone tax revenue. In 2002, the last year for which data are available, the tax exemption cost approximately 24 million pounds. Arts advocacy organizations note that of all the tax forgone to the state as a result of various tax incentive efforts, the Artist Tax

³ See http://www.visualartists.ie/alr_ate_scheme.html.

⁴ See http://www.visualartists.ie/alr_ate_scheme.html. Visual Artists Ireland provides a breakdown of costs of the tax exemption to the Exchequer beginning in 1994/95. The exemption peaked in 2000/1 at 36.8 million pounds.

⁵ Source: Visual Artists Ireland, op.cit. 2001 is the last year for which data are available. Data for 2002-2005 will come online by the end of 2006.

Exemption accounted for only 0.38 percent of that total in 2001 and only 0.15 percent in 2002.⁶

Arts advocacy organizations recognize that high earning artists benefit from the tax exemption. They argue, however, that the tax exemption retains high profile artists in Ireland who otherwise might leave for New York, Los Angeles, or London where music, film, and book publishing industries are centered. In a position statement on behalf of the artist tax exemption, Visual Artists Ireland argues that wealthy Irish artists benefit the country in myriad ways. The group notes that high income artists typically pay tax on two-thirds of their income. In addition, artists generate significant business activity and employment related to their production companies, recording studios, and management offices. Finally, high income, high profile artists “contribute hugely to the international reputation of Ireland as a society which values and respects creativity.”⁷

In October 2005, the Arts Council issued the following statement in support of the tax exemption:

It is our view, based on our own wide discussions and research on this matter, that if the exemption is abolished, a number of consequences will flow – artists will emigrate in search of lower costs of living and live more closely to cultural hubs...the existence of the scheme is a major factor in holding many artists in Ireland, far from their natural markets and from potentially larger audiences.⁸

► **All of these exemptions apply only to “creators” and originators, and are thus not available to most performing artists and musicians who are “interpreters.”**

The tax exemptions that are included in all of the current individual artist incentives are primarily related to income associated with the creation of original works. The exemption is primarily thus limited to creative activities that involve copyrights. In Ireland, the tax exemption applies to all income earned through the sale of original and creative work recognized as having cultural and artistic merit. Ireland defines a work as “original and creative” if it “encompasses any unique work that is brought into existence for the first time as an independent entity by the exercise of its creator’s imagination.” The exemption is primarily limited to books, plays, a musical composition, or a work of visual art or sculpture.

In Quebec, the exemption was recently extended to performing artists to some degree by including royalties “pertaining to a performance and neighboring rights.” “Neighboring rights” are defined in the music industries as “the performance rights performers have in their performances, the makers of sound recordings have in their recordings, and broadcasters have in the communication signals they broadcast.” By including “neighboring rights,” Quebec has tried to expand the exemption to performers and record producers.

⁶ Source: Visual Artists Ireland – http://www.visualartists.ie/alr_ate_scheme.html

⁷ http://www.visualartists.ie/alr_ate_position.html

⁸ Arts Council newsletter, Vol. 3, Issue 3 – October 2005. See <http://newsletter.artscouncil.ie>

PLACE-BASED TAX INCENTIVES

In some states, artists and arts-related businesses are eligible for tax breaks if they locate in a designated “arts district.” These place-based incentives are typically geared toward revitalization of urban communities and designed to contribute to smart growth goals. As elected officials and economic development practitioners recognize the potential of artists and arts-related businesses to transform disinvested urban neighborhoods, these types of incentives have become more popular.

Place-based incentives also include state historic tax credits for the rehabilitation of historic homes and industrial buildings located in or near designated arts districts. Because arts districts are typically located in urban core neighborhoods, there is often considerable overlap between designated “arts districts” and “historic districts.” In a number of states, state historic tax credits are granted to property owners and developers that undertake renovations of historic buildings for mixed-use purposes including affordable live/work space for artists. Some states also provide tax incentives to individual artists to undertake rehabilitation of industrial mills.

Arts and cultural districts have become a popular economic development strategy in recent years. According to the American Center for the Arts (ACA), more than 100 cities in the United States have planned or implemented such districts, positioning the arts as the center of their urban revitalization strategies. In *Cultural Districts: The Arts as a Strategy for Revitalizing Our Cities*, ACA defines a district as “a well-recognized, labeled, mixed-use area of a city in which a high concentration of cultural facilities serve as the anchor attraction.” Today, designated arts and cultural districts exist or are in formation in a broad array of cities ranging from Tucson, Minneapolis, and Kansas City, to Pittsburg, Baltimore, and Miami.

Tax Incentives in Designated Districts

While arts and cultural districts are increasingly popular, only a few cities and states have put tax incentives at the center of their district strategy. The two states that have taken this approach the farthest are Rhode Island and Maryland.

► Rhode Island’s Tax Free Arts Districts

Rhode Island has been very proactive in arts-related economic development, luring artists and creative businesses from Boston, New York, and beyond through a variety of economic development incentives. A recent cover story on Rhode Island’s aggressive economic development efforts entitled *How the Littlest State is Luring Money, Talent and Jobs from Boston and Beyond* highlighted the state’s focus on creative industries: “While parts of Rhode Island’s economic development plan target technology, biotech, and finance, its sweet spot has turned out to be creative businesses. Artist, designer, musician, filmmaker, writer, entrepreneur, and inventor are all job categories Rhode

Island has identified as important to its economic and community resurrection.” (See *Boston Globe Magazine*, October 29, 2006.)

Starting in 1998, the Rhode Island General Assembly passed legislation to provide tax incentives for artists to live and work in designated “arts districts” in nine Rhode Island communities.⁹ The legislation provides three different kinds of incentives:

- for artists who *live and work* within a specified district, any sale of work created within the district is exempt from state sales tax;
- for artists who *live and work* within a specified district, any income they receive from the sale of work they have created within the district is exempt from state personal income tax;
- for *gallery spaces* located within the boundaries of a specified district, the sale of original, one-of-a-kind works of art are exempt from state sales tax, whether or not they were created within the boundaries of the arts district.

Artists and gallery owners obtain applications for income tax and sales tax exemption from the Rhode Island State Tax Administrator. Applications and proof of residency in the tax district must be submitted before art can be assessed. Upon receipt of application, the Tax Administrator sends out an evaluator from the Rhode Island State Council on the Arts to assess the artwork to determine whether it qualifies as “one-of-a-kind” or “limited.” Guidelines are outlined in the state legislation.

► **Maryland Smart Growth Arts and Entertainment Districts**

With the passage of Senate Bill 586, Maryland became the first state in the country to develop arts and entertainment district incentives on a statewide basis. According to Maryland Citizens for the Arts, the bill aims to encourage the creation of hubs of cultural activity by offering tax breaks and state aid to artists and arts-related activity that occurs within a designated district. The Bill’s tie to the state’s Smart Growth/Priority funding programs connects the arts with broader state goals of neighborhood revitalization and economic development.

To date, 12 jurisdictions across the state have obtained an arts and entertainment district designation from the State Department of Business and Economic Development. The Maryland bill offers artists and arts organizations (both nonprofit and for profit) in designated districts the following tax incentives:

- income tax subtraction for artistic work sold by “qualifying residing artists”;
- property tax exemptions for developers who renovate or construct space for artists and/or arts-related enterprises for up to 10 years; and
- exemption from the admissions and amusement tax levied by an arts and entertainment enterprise or qualifying residing artist in a district.

⁹ The nine communities are Providence, Pawtucket, Westerly, Woonsocket, Tiverton, Little Compton, Newport, Warwick, and Warren.

The process of obtaining tax credits is different for each tax category.

For *income tax subtraction*, qualifying individual artists claim a subtraction for income derived from the sale, publication, production, or performance of an artistic work within the designated district. A form and instructions are available from the state comptroller. To receive the *admissions and amusement tax exemption*, enterprises must register with the city's director of finance. For *property tax credit*, owners first contact the state Department of Assessments and Taxation (prior to renovations) to determine if renovations will qualify for a credit. Property owners must then file with individual city finance departments within 90 days of the assessment reflecting the eligible assessment.

Artspace

Artspace is a pioneer in the rehabilitation of historic buildings and the use of historic tax credits for affordable artist live/work space. Artspace buys unused or underutilized historic buildings and converts them into fully functioning space for artists and arts-related businesses and organizations. Today, Artspace owns and manages 18 properties across the country. Artspace has renovated multiple historic buildings in Minneapolis including the Northern Warehouse, the Shubert Theater, the Grain Belt Warehouse, and the Grain Belt Bottling House. Recently completed renovations include conversion of the pre-Civil War Jefferson Davis Hospital into low-income artist housing in Houston, and Tashiro Kaplan Lofts in Seattle, a massive project in the Pioneer Square neighborhood that provides 50 rent controlled units of artist housing and 38,000 square feet of commercial space for arts-related activities. According to the *Seattle Weekly*, the development was meant to address the loss of 250 artists' studios in Pioneer Square over the past five years due to rising property taxes and gentrification. (*Seattle Weekly*, "Art Squared," June 30, 2004).

The 10-year property tax credit reduces the increase in the county property tax that happens when the assessment increases after the construction or renovation of a building. The credit is available for space in manufacturing, commercial, or industrial buildings constructed for use by a qualifying resident artist or arts and entertainment enterprise. The credit for the first year is 80 percent of the increase and declines incrementally each year.

Utilizing State Historic Tax Credits to Create Affordable Artist Live/Work Space

Historic structures are often concentrated in designated arts districts, and a handful of cities and states have made an explicit connection between the state historic tax credit and affordable live/work space for artists. Rehabilitation of historic structures, particularly the old mill buildings and warehouses that artists covet for live/work space, is an expensive and complex undertaking. State historic tax credits provide an incentive to property owners and developers that can help make these projects financially feasible. State credits are typically combined with federal historic tax credits to bring down the costs of rehabilitation.

According to the National Trust for Historic Preservation, roughly half the states in the country have adopted laws creating credits against state taxes to provide incentives for

the appropriate rehabilitation of historic buildings.¹⁰ The report notes that some state programs have been extraordinarily productive at stimulating rehabilitation activity while others have had mixed or minimal results. Factors limiting success include placing a cap on the amount of the credit as well as lack transferability, i.e., ability of the owner that earned the credit to sell the credit outright to a third party. The report notes that “good” state programs have clear eligibility and rehabilitation standards, make credits available for owner-occupied residences as well as commercial properties, and provide a credit level that is high enough to constitute a meaningful incentive, typically in the range of 20-30 percent of qualified rehabilitation expenditures.

Louisiana has a state historic tax credit program and provides a 25 percent credit for income producing properties in “downtown development districts” as well as a 25 percent credit for owner-occupied residential and owner-occupied mixed-use qualified properties. The program for owner occupied structures is capped at \$1 million making it one of the smaller state programs in the country.

Following are examples of states that have explicitly tied tax credits to artist live/work space.

- *Rhode Island.* Rhode Island¹¹ offers the most generous state historic building tax credit in the country, equal to 30 percent of total expenditures on rehabilitation of buildings that qualify for the Rhode Island Register of Historic Places. There is no yearly cap and no project cap. The Rhode Island state historic tax credit program has been approved for more than 200 projects and has resulted in 4,500 units of planned or built housing since 2002 much of which is located in designated “arts districts.”
- *Kentucky.* Kentucky offers a 30 percent income tax credit for owner-occupied residential properties. A minimum investment of \$20,000 is required with the total credit not to exceed \$60,000. There is a 20 percent income tax credit for all other properties, requiring a minimum investment of \$20,000. Credit is freely transferable. Program is capped at \$3 million annually. The Kentucky credit has been put to use in the Paducah Artist Relocation Program. Paducah offers tax credits to individual artists willing relocate to Paducah and to buy and rehabilitate historic structures for live/work space. The tax credit has been a centerpiece in the Relocation program that has served to revitalize Paducah, a small town that lies halfway between Nashville and St. Louis. Since 2000, the Relocation program has caused over 70 artists from

¹⁰ See “State Tax Credits for Historic Preservation,” a Public Policy Report published by the National Trust Forum, May/June 2006. The report lists all states that have adopted the credit and describes individual state programs.

¹¹ Rhode Island has passed a slew of legislation to encourage historic preservation and renovation. Because there is a great deal of overlap between the state’s tax free arts districts and historic districts, the renovation work is presumed to benefit artists and create artist live/work space. Other related legislation includes the Rhode Island Mill Building and Economic Revitalization Act that provides tax credits equal to 10 percent of substantial rehabilitation of mills. The goal is to attract local businesses and private owners to invest in the rehabilitation of vacant mill buildings worthy of reuse. In addition, the Urban Mill Restoration and Tax Exemption Act applies the same artist tax exemptions (income from sale of artwork) to artists who inhabit mill buildings and endeavor to restore the property regardless of whether it is located in a designated arts district.

cities as far reaching as Tucson, Washington, D.C., and Los Angeles, to relocate to Paducah.¹²

- *Massachusetts.* Income producing properties in Massachusetts are eligible to receive up to 20 percent of the cost of certified rehabilitation. The program is capped at \$10 million. Massachusetts has been a leader in rehabilitating industrial warehouses and mill buildings for artist live/work space and a state agenda is now forming around the issues of economically sustainable artist space. In 2004, with a grant from Leveraging Investments in Creativity, a new Massachusetts team called *ArtsLink* formed to focus explicitly on the advancement of an artist space agenda for the state. ArtsLink works with developers and municipal officials to help them understand space development financing options including the application process and eligibility standards for state historic tax credits. ArtsLink provides three key services: preservation and creation of permanent and affordable artist space; policy work at the state and local levels to encourage artist-friendly policies; and a comprehensive website including available arts space throughout the state. ArtsLink is actively involved in the current rehabilitation of numerous historic structures across the state. It is not clear from the website, however, how many of these efforts have utilized state historic tax credits. See <http://www.artistlink.org>.

Analysis of Place-Based Incentives

► Impact and Cost

Rhode Island and Maryland “art district” strategies are credited with revitalizing downtown areas and distressed urban communities. It is difficult to determine the precise impact of tax incentives on revitalization, however, as there are many other factors at play in these efforts and available data are scant.

Rhode Island has received a great deal of press coverage for its arts-related economic development work and Providence and Pawtucket, in particular, stand out for their thriving arts communities, revitalized downtowns, and renovated mill buildings. Observers of the state suggest that the tax incentives have played an important role in the renaissance.¹³ Some note, however, that development tax credits, including the state historic tax credit and the Urban Mill Restoration Program, are having a considerably larger impact on revitalization than income tax breaks for artists. A recent study conducted by the State Council on the Arts, for example, noted that few artists living in arts districts have taken advantage of the personal income tax credits because their incomes from the sale of art are too low to make the tax break financially valuable.

In Maryland, economic development officials widely credit the tax incentives for revitalizing downtown areas and several districts are in the process of expanding their geographic boundaries to cover larger areas. An article in the *Baltimore Daily Record* noted that there are no statewide statistics available regarding how many individuals or

¹² See Zach Patton, “Paducah refines a way to restore a decaying community,” *Governing Magazine*, August 2006. For an overview of the program see <http://www.paducaharts.com>

¹³ See Sunday Globe Magazine article op. cit.

enterprises have applied for tax credits. Each district is required to submit an annual report.

Station North Arts and Entertainment District in Baltimore has received particular attention for the conversion of numerous industrial buildings into mixed use and artist live/work space.¹⁴ While statewide statistics are not available regarding the number of individual artists or property owners that have taken advantage of the credits, each district is required to submit an annual report to the state. The Station North Arts report for FY 2004, for example, estimates that 385 artists live and work in the district and that 103 artists have located in the district since its designation. The report also notes that only one entertainment venue has applied for and received exemption from the admissions and amusement tax.

► **Victims of Their Own Success: Combating the “SoHo Effect”**

Some suggest that art district tax incentives have been a boon to arts-related businesses and developers but have done little to help individual artists. They point to the so-called “SoHo effect” in which artists, as a result of their pioneering efforts in distressed urban neighborhoods, increase the value and “hip” factor of such neighborhoods but are subsequently displaced and priced out of the neighborhood due to rising property taxes, rents, and high demand for downtown living among white collar professionals.

- *Providence.* The SoHo effect describes the current situation in Providence where few artists can afford to live in the downtown tax-free zone. In 2005, the city of Providence created a second tax-free arts district (the West End Arts District) to create more affordable options for artists. The Partnership for Creative Industrial Space drafted and lobbied the passage of the bill through the Rhode Island General Assembly with support from the arts community. In announcing the bill that recognizes the new district boundaries, Providence Mayor Cicilline acknowledged that rising property values in the downtown district had made living there unaffordable for many artists. The Mayor pledged his continued commitment to retaining artists and making Providence a haven for artistic talent.
- *Kansas City.* In Kansas City, tax abatements have been under study for more than a year by the Kansas City Council due to rising property values. Artists have argued for several years that they are being forced out of the Crossroads neighborhood they pioneered over 15 years ago, due to rising property taxes. The abatements are designed to retain artists and arts-related businesses that promote economic revitalization of the district. Abatements would apply to improvements made by owners of buildings that house art-related businesses. The Kansas City Business Journal notes that artists started buying and refurbishing old warehouses 20 years ago before the area became fashionable. As property values skyrocketed and commercial development took root, many residents and arts-related business owners claimed they could no longer afford to stay in the district.

¹⁴ Major rehabilitation efforts in the Station North District of Baltimore include Penn Lofts, Railway Express, Area 405 and the Cork Factory.

The tax abatement plan, studied and recommended by the Planned Industrial Expansion Authority, would provide financial assistance to qualified applicants by freezing property taxes at designated rates for a period of years on properties occupied for arts and cultural uses within the Crossroads district. Those uses could include studio spaces for independent artists, writers, and performers; art dealers, motion picture, and video industries; sound recording; fine arts schools; performing arts companies; and historical sites. All arts and cultural uses would be reviewed by an advisory committee appointed by the Mayor. In developing the tax abatement plan, Kansas City officials drew on Baltimore's Station North Arts and Entertainment District as a model.

INDUSTRY-BASED TAX INCENTIVES

Recognizing the large economic impact of creative industries, many states now offer tax incentives to encourage film and television producers to undertake production in their states. Typically, the incentives take the form of tax credits ranging from 10 to 25 percent of total production costs. Some states have taken tax credits a step further offering credits to investors who invest in film and media infrastructure (e.g., film and sound recording studios) in an effort to root and grow creative industries rather than simply attracting "one-time" productions. To date, 27 states have passed legislation creating tax incentives for film and related industries. Canadian provinces including Quebec, Ontario, and British Columbia offer a range of film and media-related tax incentive programs as well.

Film and television production tax credits usually fall into the following categories: production expenses tax credit, payroll tax credit, and investment tax credit. According to an October 2006 policy brief by the New England Center for Public Policy at the Federal Reserve Bank of Boston, tax credits "generally relieve taxpayers of the obligation to pay all or part of a tax liability. Typically, state film tax credits are applied toward the individual or corporate liability of qualified producers, investors, or – in states where the credits are transferable – the purchaser of earned, unused credits."

Louisiana has been a national leader in the development of tax incentives for creative industries. Since 2002, the state has passed numerous pieces of legislation that grant tax credits to the film, music, and digital media industries. These include the recently amended Motion Pictures Incentives Act (Act 456), the Recording Investment Incentives Act (Act 485), and the Digital Media Incentives Act (346). Collectively, this legislation creates a tax infrastructure that stimulates investment, industry infrastructure development, and job creation in Louisiana's cultural industry sectors. Louisiana's tax credit initiatives, particularly the motion picture incentive package, have garnered national media attention and helped catapult the state to a major position nationally in terms of money spent on movie production.

Given that Louisiana is a leader in the use of tax incentives to stimulate the growth of creative industries, it can adapt and expand upon what other states and regions have done. There are two specific ways that it can do this:

- further expand existing credits to other cultural industries and develop new policies that ensure the effective use of these tax incentives; and/or
- amend existing state economic development related tax incentives to include the cultural industries

Expand Tax Credits to a Broader Set of Cultural Industries

While most state tax incentives related to the film industry are relatively limited, a number of states like Louisiana have broadened their definition of film to include digital media, including computer games. These states include:

- in 2006, Hawaii extended its tax credits for film to include digital media;
- in 2006, the Connecticut General Assembly established tax credits for the production of digital media and motion pictures in Connecticut;
- the New Mexico Film Production Tax Credit includes video games and national or regional advertising content in film and digital formats; and
- Maine's Attraction Film Incentive Wage Tax rebate plan includes a commercial, photographic project, interactive computer or video game.

The most expansive use of industry tax credits is in Ontario where the Ontario Media Development Corporation (OMDC) oversees a range of tax credits in six cultural industries:

- Book publishing
- Music
- Interactive digital media
- Film
- Magazine publishing
- Television

The Ontario Media Development Corporation is an agency of the Ontario Ministry of Culture. It was created in December 2000 under the Development Corporations Act to re-brand the Ontario Film Development Corporation entity under a new name and with a new mandate to expand it to other cultural industries and to stimulate employment and investment.

The government's focus is to build the capacity and competitiveness of Ontario's cultural media industries individually and across sectors. A chief executive officer oversees OMDC's activities in conjunction with the agency's board of directors to achieve the agency's mandate. OMDC services and programs are delivered through three divisions:

Business Affairs and Research, Industry Development, and Tax Credits and Financing. The Business Affairs and Research division coordinates strategic and business planning, agency operations, and industry research and data collection; the Industry Development division provides opportunities for cultural entrepreneurs to create and market new products, develop existing markets, access new markets and grow their business.

The Tax Credits and Financing division of OMDC administers, processes, and assesses eligibility for the Ontario government’s comprehensive book publishing, film, television, digital media, and sound recording tax credit programs. In conjunction with the Ministry of Finance, this division evaluates tax credit applications according to government legislation and regulations. Information referral services are provided for applicants and potential applicants as are tax credit information sessions. The division also promotes the program to national and international producers.

The OMDC co-administers the following tax credits with the Ministry of Finance based on eligible Ontario expenditures:

- *Ontario Book Publishing Tax Credit:* 30 percent of eligible Ontario pre-press, printing, marketing, and book publishing expenditures, up to a maximum tax credit of \$30,000 per book, is allowed by Canadian corporations located in Ontario.

Value and Distribution of Ontario Media Tax Credits: 1998 - 2005		
	VALUE OF TAX CREDIT	% OF TOTAL
Sound Recording	\$ 3,440,000	1%
Film and Television	\$ 317,385,000	62%
Book Publishing	\$ 8,672,000	2%
Production Services	\$ 155,761,000	30%
Animation and Special Effects	\$ 19,685,000	4%
Digital Media	\$ 5,823,000	1%
TOTAL	\$ 510,766,000	100%

Source: 2004 Annual Report of Provincial Auditor and 2005 Annual Report of Ontario Media Development Corporation

- *Ontario Computer Animation and Special Effects Tax Credit:*

Twenty percent of eligible Ontario labor expenditures for digital animation or digital visual effects by Canadian or foreign-owned corporations located in Ontario.

- *Ontario Film and Television Tax Credit:* Twenty percent of eligible Ontario labor expenditures by Canadian-owned production corporations located in Ontario.
- *Ontario Interactive Digital Media Tax Credit:* In 2006, the Ontario Interactive Digital Media Tax Credit was further enhanced, with the size test removed and fee-for-service work by video game developers included.
- *Ontario Production Services Tax Credit:* Eleven percent of eligible Ontario labor expenditures by Canadian-owned or foreign-owned production corporations located in Ontario.
- *Ontario Sound Recording Tax Credit:* Twenty percent of eligible Ontario production, marketing, and distribution expenditures by Canadian-owned corporations that have

been located in Ontario for at least 12 months or were sole proprietorships or partnerships prior to incorporation.

An analysis of an auditor's report from the Office of the Provincial Auditor of Ontario and the OMDP's 2005 Annual Report finds that a vast majority of the tax credits are being used for film- and television-related productions. Animation and special effects, while small, has been a growing component of the tax credits, with about one-third of the total amount occurring in 2004/2005. Sound recording, digital media, and book publishing remain a small amount of total tax credits.

While small in dollar amounts of tax credits, a relatively large proportion of the number of certificates issued went to corporations involved in book publishing and sound recording. In the 2004/2005 period, 23 percent of the certificates issued were for sound recording companies and 20 percent for book publishing. This data provide evidence that the credits are being used by relatively small companies for smaller size production activities, not just for very large motion picture projects.

Include Cultural Industries in State R& D Tax Credits

A large number of states, as well as the federal government, have developed tax incentives aimed at promoting the high technology industry and research and development activity. A review of state R&D tax credits by the Fiscal Research Center at Georgia State University reports that about 30 states offer a R&D Tax credit to spur the creation of high technology jobs in their states. Many of these tax credits are piggybacking the state credit on the amount reported to qualify for the federal R&D tax credit. States with high levels of state credits include Rhode Island, which offers 22.5 percent on the first \$110,000 and 16.9 percent for expenditures over \$110,000, and Massachusetts, which provides a 10 percent credit on basic research and a 15 percent credit on research conducted through a state university. The definition of research and development in most states is primarily limited to technology-related activity. The one exception is Hawaii, which has defined R&D to capture some segments of the cultural economy.

▶ Hawaii's 100% High Technology Business Investment Tax Credit

In addition to its credits for the film industry and the income tax exclusion for royalties, Hawaii has a tax credit for investors (including individuals, partnerships, companies, or corporations) in "performing arts" companies. Act 221 ("100% High Technology Business Investment Tax Credit") passed in 2001 and amended in 2004, awards nonrefundable income tax credits capped at \$2 million per each investor's qualified investment in a Qualified High Tech Business (QHTB). To qualify as an QHTB, companies must pass an activity test: 50 percent of total business activities must be "qualified research," and business must conduct more than 75 percent of its research in Hawaii *or* 75 percent of gross income must be derived from qualified research from products sold from or manufactured in Hawaii.

While many states grant R&D tax credits for technology companies, Hawaii is unique for including “performing arts products” in its definition of qualified research.¹⁵ According to Film Hawaii, qualified performing arts products include the following:

- 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.

In relation to the performing arts, the goal of the high tech tax credit is to encourage investment in performing arts companies that are planning to remain in Hawaii for at least five years. Because Hawaii has both a film tax credit for production, as well as the investment tax credit, a single film can “double dip” to claim both tax credits.

The tax credit in Hawaii has been somewhat controversial. A draft report was presented in October 2006 that examined the economic implications of the tax credit. According to the recently released data, the state issued \$184 million in tax credits between 2001 and 2004. Taxpayers have claimed \$74.9 million of that amount. However, there was minimal information available on the specific types of companies and number of companies that have utilized the credit. The lack of data on the economic impacts of the tax credit has led to some criticism by opponents who fear that the credit is being abused.

RECOMMENDATIONS

Create a Comprehensive Legislative Package for the Cultural Industries

As Louisiana contemplates the introduction of legislation, it is important to be clear about development goals in order to craft corresponding tax incentives. The primary goals of a proposed legislation package for the cultural industries would be:

- attract creative talent back to the state by enabling them to more readily earn a living from their art and/or obtain affordable live/work space;
- provide additional financial and legal support to existing Louisiana residents who produce the state’s cultural products;
- make Louisiana a magnet for creative talent and creative businesses;
- revitalize distressed communities utilizing artists and arts-related activities as an economic development catalyst;
- create new businesses and new jobs through investments in the growth and development of commercial businesses in the cultural economy; and
- make Louisiana a national center of the film, music, digital media, and literary and visual arts industries.

¹⁵ Other “qualified research” under the Hawaii legislation includes: computer software, biotechnology, sensor and optic technologies, ocean sciences, astronomy and non-fossil fuel energy-related technology.

These goals are not mutually exclusive and often are pursued in tandem. Some states, notably Rhode Island, have pursued many of these goals aggressively to make arts-related development a centerpiece of state economic development strategy. Throughout the world, countries are beginning to develop a full package of incentives aimed at strengthening their creative industries. With a new, comprehensive set of incentives, Louisiana can make its mark as the leader in the U.S., and be comparable to other nations in terms of its commitment to building its cultural industries and treating cultural industries on par with other economic development targets.

Elements of the Legislative Package

The legislative agenda for building the Louisiana Cultural economy should have three components:

1. THE STATUS OF THE ARTIST ACT

- Create tax exemption for royalties and copyright income for original creative products.
- Create a “Status of the Artist” Task Force to consider a full range of economic and legal rights to ensure the protections of the creators of Louisiana’s cultural products

2. CULTURAL INDUSTRIES R&D AND PROMOTION ACT

- Expand the tax credit legislation to all cultural industries—create a new credit for literary arts, visual arts, culinary arts, performing arts, and historic preservation.
- Make the state’s R&D tax credit applicable to all cultural industries.

3. CULTURAL COMMUNITY DEVELOPMENT ACT

- Increase the cap on state residential historic tax credits by increasing it to an annual amount of \$10 million from its current \$1 million.
- Allow local communities to designate cultural product districts with property and sales tax incentives.
- Provide developers with tax credits for the creation of artist housing.

► Status of the Artist Act

As Louisiana contemplates an artist tax exemption, there are several factors to consider. First and foremost is the question of who the tax exemption is designed to help. There are three primary groups to consider:

- Providing financial assistance to low- and moderate-income artists who currently reside in Louisiana?

- Creating an incentive for artists who left Louisiana post-Katrina to return to the state?
- Creating an incentive to artists who have never lived in Louisiana to move to the state to pursue their artistic endeavors?

Determining the primary beneficiary of the tax exemption is key and should determine the overall design of the program. For example, if the primary goal of the tax exemption is to provide financial assistance to existing artists and/or an incentive to former artist-residents to return to the state, the exemption can likely be set lower than if the goal is to attract new artists or high income, high profile artists with no previous connection to Louisiana.

As noted above, the Ireland tax exemption provides 100 percent income tax exemption on sales of original artwork up to 250,000 pounds and 50 percent above and beyond that threshold. This structure enables high income artists to receive significant tax breaks even if they are a minority of claimants. This aspect of the Irish tax program has been subject to a great deal of criticism and contributed to the Minister of Finance to proposing to abolish the exemption in 2005

Depending on program goals, Louisiana may want to cap the tax exemption at a lower level than the Irish program to safeguard against criticism. Since the vast majority of artists earn far less than \$50,000 per year on the sale of original artwork, Louisiana could create an exemption targeted to this category of artists. This would signify the state’s commitment to this population without creating “tax windfalls” for wealthy individuals. Louisiana might create a graduated schedule in which low- and moderate-income artists receive a greater tax exemption than middle- and high-income artists. The type of program outlined below provides support to lower-income artists while still recognizing the important contributions of higher earning artists to the state’s creative economy. Such a schedule is likely to be less controversial than a program that provides a higher tax exemption to wealthy artists.

Range of Income from Original Artwork	Percent Income Tax Exemption
Less than \$50,000	100% exemption
\$ 50,000-100,000	50% exemption
\$100,000-500,000	25% exemption
\$500,000+	10% exemption

Another important consideration for Louisiana is to clearly define what type of art and what type of artists are eligible for the exemption. Ireland’s program is limited to books, plays, musical composition, painting, and sculpture. Interpretive artists including dancers, actors, and performers are not eligible for the exemption. Under Ireland’s definition, experimental filmmakers, computer animation specialists, graphic designers, and individuals working in culinary arts would not qualify for the tax exemption. How closely should Louisiana’s definition of eligible artwork and artists follow its cultural

economy focus? Musicians, for example, are critical to Louisiana's arts community. Which aspects of a musician's income would be eligible for tax exemption under a tax exemption plan? Income for recording contracts of original compositions would qualify under the Irish program. But income paid to bands to play live music in nightclubs would not qualify for the exemption under the Irish plan.

A next step for Louisiana is to clearly define both the artistic products and the individuals that would be eligible for the tax exemption. These definitions should relate to and reflect overall program goals, i.e., intended beneficiaries, and should logically relate to other aspects of the state's overall art-incentive package, e.g., place-based and industry-based tax incentives.

In addition to the tax exemption on royalty income, legislation could be proposed to create a task force to review a more comprehensive set of incentives and protections of artists in Louisiana. This Task Force should review existing work in this area by UNESCO, the Canadian federal government, and recent task forces that have looked at these issues in Ontario, Quebec, and Saskatchewan.

▶ **Cultural Industries R&D and Promotion Act**

Louisiana already has one of the most generous and broad based set of incentives for investment in the cultural industries. In this area, the primary focus would be to amend the current R&D tax credit to include in its definition all of the cultural industries and to expand the current industry tax credits to include the literary arts, visual arts, culinary arts, performing arts, and historic preservation. The Ontario Media Development Corporation provides the best model for both the design and the management of these incentives.

In addition, due to the changing nature of the incentive environment at the state level, legislation could be passed calling for an annual review that compares the state's incentive package to other states and provinces.

▶ **Cultural Community Development Act**

Louisiana could clearly be doing more to provide incentives for the development of cultural districts within the state. Currently, the state caps the historic tax credit at a relatively low level. With the substantial need of housing for creative talent, and the need to restore and rebuild following Katrina and Rita, the need to provide further incentives to promote rebuilding should be a high priority.

Louisiana can develop a set of incentives similar to Rhode Island and Maryland that provide for both income tax and sales and entertainment tax exemptions in designated arts, cultural, and entertainment districts. The incentives could include

- For artists, musicians, actors, dancers, and other creative talent who live and work within a specified district, any sale of work created or performed within the district is exempt from state sales tax.

- For artists, musicians, actors, dancers, and other creative talent who live and work within a specified district, any income they receive from the sale of work they have created or performed within the district is exempt from state personal income tax;
- For *gallery spaces and performance venues* located within the boundaries of a specified district, the sale of original, one-of-a-kind works of art or performances are exempt from states sales tax, whether or not they were created within the boundaries of the arts district.
- Property tax exemptions for developers who renovate or construct space for artists and/or arts-related enterprises for up to 10 years in designated districts

Managing the Cultural Incentive Programs

It is critical that the state of Louisiana develop a very strong management and accountability plan as part of these legislative initiatives. This will require developing very clear definitions of eligibility and an oversight structure to ensure that these definitions are being followed.

In addition, all of the legislation should include very strong language about the collection of data on outcomes and require annual reviews. In Ontario, there has been very detailed analysis of how its existing incentives are being used and by whom. On the other hand, Hawaii has experienced considerable controversy because there are very little data available about the companies that have benefited from its tax credits. In Louisiana, to ensure accountability, legislation should require the following information for all tax exemptions and tax credits related to the cultural economy:

1. the number of individuals and corporation participating in the program;
2. the income of the individuals benefiting from the program;
3. the income and size of the corporations benefiting from the program;
4. benefits by the different segments of the cultural industry; and
5. the total cost of the program to the state of Louisiana.

The data should be made public on an annual basis.

Marketing and Outreach

One of the major potential economic development benefits of this legislative package would be helping to further brand Louisiana as an international leader in supporting the development of the cultural economy. It is critical that the state ensure that information about eligibility for these incentives be widely known both within Louisiana as well as globally. A broad based and comprehensive marketing campaign should be developed in conjunction with these incentives.