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COMMONWEALTH OF PENNSYLVANIA
DEPARTMENT OF REVENUE



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January 25, 1999

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John E. Nanorta, Jr.
Regulatory Analyst
Independent Regulatory
Review Commission
Fourteenth Floor
Harristown 2
333 Market Street
Harrisburg, PA 17101

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Dear Mr. Nanorta:

Enclosed please find the Department of Revenue's draft final form regulation relating to commercial motion pictures.

We would appreciate it if you could convey your comments to this office by February 22, 1999. Comments received by this date will be considered in the drafting of the final form regulation.

Thank you for your anticipated input and assistance in promulgating this regulation.

Sincerely,

A handwritten signature in cursive script that reads "Douglas A. Berguson".

Douglas A. Berguson
Senior Assistant Counsel

Enclosure

DAB:AMD:tlch

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By: _____
(DEPUTY ATTORNEY GENERAL)

DATE OF APPROVAL

Check if applicable
Copy not approved. Objections attached.

Copy below is hereby certified to be true and correct copy of a document issued, prescribed or promulgated by:

PA Department of Revenue

(Agency)

Document/Fiscal Note

Date of Adoption:

By: _____
Robert A. Judge, Sr.
Secretary of Revenue

Title: _____
(Executive Officer, Chairman or Secretary)

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Copy below is hereby approved as to form and legality. Executive or Independent Agencies.

By: _____

Date of Approval

(Deputy General Counsel)
(Chief Counsel, Independent Agency)
(Strike inapplicable title)

Check if applicable. No Attorney
General approval or objection within 30 days after submission

NOTICE OF FINAL RULEMAKING

DEPARTMENT OF REVENUE

61 Pa. Code §§ 32.38 and 60.22

Sales and Use Tax

Commercial Motion Pictures

PREAMBLE

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The Department of Revenue (Department), under authority contained in section 270 of the Tax Reform Code of 1971 (TRC) (72 P.S. § 7270), by this order amends 61 Pa. Code, Chapter 32. Exemptions, by adding section 32.38, (relating to commercial motion pictures) and amends Chapter 60. Sales and Use Tax Pronouncements - Statements of Policy, by deleting section 60.22 (relating to commercial motion pictures) as set forth in Annex A.

Purpose of Regulation

The Department is setting forth its interpretation of section 2 of Act 7-1997, section 204(54) (72 P.S. § 7204(54)) regarding the sales and use tax exemption for the sale at retail to or use by a producer of commercial motion pictures of any tangible personal property directly used in the production of a feature-length commercial motion picture distributed to a national audience.

Explanation of Regulatory Requirements

Subsection (a) sets forth the definition of various terms for use in § 32.38. Subsection (b) details the scope of the exemption. To effect legislative intent, the Department has added language at § 32.38(b)(1)(ii). If this subparagraph were not added, the purchase of the tangible personal property would be exempt but the repair or alteration would be subject to tax. For example, the purchase of film would be exempt but the development charges would be subject to tax which clearly is not the legislative intent. Subsection (c) describes the treatment of property and services purchased for resale. Subsection (d) provides that charges to install, repair, maintain or service equipment, parts, tools and supplies directly used in the production of a commercial motion picture are exempt from tax. Subsection (e) explains that utilities used directly and exclusively in the production of a commercial motion picture are exempt from tax. Examples of taxable and exempt electricity usage are provided. An explanation regarding the use of exemption certificates is set forth in subsection (f).

With the adoption of § 32.38, the pronouncement set forth at § 60.22 is no longer necessary and is therefore being deleted.

72 P.S. § 7204(54) requires that the purchaser furnish to the vendor a certificate substantially in the form as the Department of Community and Economic Development may prescribe by regulation. In compliance with this provision, the Department of

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Community and Economic Development proposed a rulemaking relating to the exemption certificate form at 28 Pa.B. 1530 (March 28, 1998). 12 Pa. Code § 33.1 (relating to form required) provides that producers of motion pictures, who are qualified to take advantage of section 204(54) of the TRC, shall use a Pennsylvania Exemption Certificate (Form REV-1220).

Affected Parties

Producers of motion pictures who qualify to take advantage of section 204(54) of the TRC (72 P.S. § 7204(54)) may be affected by the regulation.

Comment and Response Summary

Notice of proposed rulemaking was published at 28 Pa.B. 1320 (March 14, 1998). This proposal is being adopted with changes as set forth in Annex A.

The Department received two comments from the public during the public comment period. The Department also received comments from the Independent Regulatory Review Commission (IRRC). No comments were received from the House Finance Committee or the Senate Finance Committee.

The amendments to the proposed rulemaking in response to comments are as follows:

(1) IRRC's first comment relates to the inconsistent use of the terms "exemption" and "exclusion" in § 32.38. The problem relating to the use of these two terms originates with the statutory provision. The title of section 204 of the TRC is exclusions from tax; however, within paragraph (54) the term "exempt" is used. In its comments, IRRC concluded that because paragraph (54) references the term exempt, that references to "exclusion" in the regulation should be amended to "exemption." The Department also received a public comment with regard to the use of the two terms in the proposal. Contrary to IRRC, the public comment suggests that the Department use the term "exclusion" throughout the regulation instead of "exemption." The Department agrees with IRRC and the public comment that for consistency, the regulation should use only one term. The Department agrees with the revision suggested by IRRC, and has amended § 32.38(b)(2) and (b)(3) as well as the title of subsection (b) to reference the term exemption.

(2) IRRC's second area of concern relates to subsection (b) which details the scope of the exemption. IRRC suggests that the subsection does not describe the extent of the scope of the regulation and that the text should be amended and reorganized. In

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response to the concerns raised by IRRC, the Department has amended § 32.38(b) by removing proposed paragraph (2) from § 32.38(b) and creating a definition for the term "production of a commercial motion picture." With the deletion of paragraph (2), the remaining paragraphs were renumbered accordingly. In addition, the name of subsection (b) has been changed from scope to scope of the exemption. Section 32.38(b)(1) has been amended to more clearly set forth the general scope of the regulation. Finally, in accordance with IRRC's suggestion, the Department has added the phrase "of a commercial motion picture" to § 32.38(b)(2) (proposed § 32.38(b)(3)).

(3) Because section 204(54) of the TRC specifically provides that the purchaser shall furnish to the vendor a certificate substantially in the form as the Department of Community and Economic Development (DCED) may prescribe by regulation, IRRC and a public comment both suggested that the Department make specific reference to the DCED regulation that prescribes the form. The Department agrees with the comment and has amended § 32.38(f)(1) accordingly.

For clarity, the Department edited and reorganized the provisions of subsection (f) relating to exemption certificates.

The Department has also amended a style change to the term "national" which was made by the Pennsylvania Bulletin when it published the proposed rulemaking. The Bulletin changed the term from all lower case letters, to an initial capital "National." The Department has amended all references to the term to all lower case letters for two reasons. First, the enabling statute uses all lower case letters. Second, by using an initial capital, the term would be restricting the phrase "National audience" to just the United States and it is the Department's opinion that the term should apply to audiences both within and outside the United States.

Comments that did not result in amendments to the regulation are as follows:

(1) Subsection (e) under § 32.38 relates to utilities used in production. The subsection provides examples of taxable and exempt electricity usage. IRRC suggests that the Department group examples of usage exempt from tax in one subsection and usage subject to tax in a second subsection. Since there are only three examples involved, the Department does not believe separate subsections are necessary.

(2) As one of its comments to § 32.38(b), IRRC suggested that the subsection be entitled "application" instead of "scope." Scope is a customary word utilized in many of the Department's

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regulations, whereas application is not used. The Department does not see the merit in introducing a new term in this regulation; however, as mentioned above, the title of the subsection has been expanded to state "scope of the exemption."

Fiscal Impact

The Department has determined that the amendments will have no significant impact on the Commonwealth. The Department has determined that the expenditure for the exclusion provided by Act 7-1997 is estimated to be \$0.8 million for fiscal year 1997-98.

Paperwork

The amendments will require no additional paperwork for the public or the Commonwealth.

Effectiveness/Sunset Date

The amendments will become effective upon final publication in the Pennsylvania Bulletin. The regulation is scheduled for review within five years of final publication. No sunset date has been assigned.

Contact Person

The contact person for an explanation of the amendments is Anita M. Doucette, Office of Chief Counsel, PA Department of Revenue, Dept. 281061, Harrisburg, Pennsylvania 17128-1061.

Regulatory Review

Under section 5(a) of the Regulatory Review Act (71 P.S. § 745.5(a)), on March 2, 1998, the Department submitted a copy of the notice of proposed rulemaking, published at 28 Pa.B. 1320, to IRRC and the Chairpersons of the House Committee on Finance and the Senate Committee on Finance for review and comment. In compliance with section 5(c) of the Regulatory Review Act (71 P.S. § 745.5(c)), the Department also provided IRRC and the Committees with copies of all comments received, as well as other documentation.

In preparing these final-form regulations, the Department has considered the comments received from IRRC, the Committees and the public.

These final-form regulations were (deemed) approved by the Committees on _____ and were (deemed) approved by IRRC on _____, in accordance with section 5.1(e) of the Regulatory Review Act (71 P.S. § 745a(e)).

Findings

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The Department finds that:

(1) Public notice of intention to amend the regulations has been duly given under sections 201 and 202 of the act of July 31, 1968 (P.L. 769, No. 240) (45 P.S. §§ 1201 and 1202) and the regulations thereunder, 1 Pa. Code §§ 7.1 and 7.2.

(2) The amendments are necessary and appropriate for the administration and enforcement of the authorizing statute.

Order

The Department, acting under the authorizing statute, orders that:

(a) The regulations of the Department, 61 Pa. Code, are amended by adding section 32.38 and deleting section 60.22 to read as set forth in Annex A.

(b) The Secretary of the Department shall submit this order and Annex A to the Office of General Counsel and the Office of Attorney General for approval as to form and legality as required by law.

(c) The Secretary of the Department shall certify this order and Annex A and deposit them with the Legislative Reference Bureau as required by law.

(d) This order shall take effect upon publication in the Pennsylvania Bulletin.

ROBERT A. JUDGE, SR.
SECRETARY OF REVENUE

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ANNEX A

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Title 61. Revenue, Part I. Department of Revenue, Subpart B.
General Fund Revenues, Article II. Sales and Use Tax, Chapter
32. Exemptions.

§ 32.38. Commercial motion pictures.

(a) Definitions. The following words and terms, when used
in this section, have the following meanings, unless the context
clearly indicates otherwise:

Commercial motion picture - A series of related images at
least 40 minutes in length either on film, tape or other similar
medium, where the images shown in succession impart an impression
of motion together with accompanying sound, if any, which is
produced for distribution to a ~~National~~ NATIONAL audience. The
term does not include motion pictures produced for private
noncommercial use, including motion pictures of weddings or
graduations to be used as family mementos, accident
reconstruction videotapes to be used for legal analysis or
student films to be used for class projects.

Distribution to a ~~National~~ NATIONAL audience - Distribution
by means of theatrical release or for exhibition on ~~National~~
NATIONAL television by a television network or through
syndication.

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Producer - A purchaser who is responsible for the production of a commercial motion picture.

PRODUCTION OF A COMMERCIAL MOTION PICTURE - THE PROCESS OF RECORDING THE ACTIONS TAKING PLACE WITHIN A COMMERCIAL MOTION PICTURE AND INCLUDES THE ACTUAL SHOOTING OF THE PICTURE, EITHER ON LOCATION OR AT A MOTION PICTURE STUDIO, AS WELL AS THE EDITING, DUBBING AND MIXING OF A COMMERCIAL MOTION PICTURE.

(b) Scope OF THE EXEMPTION.

(1) The sale at retail to or use by a producer of tangible personal property AND SERVICES THERETO THAT ARE directly used in the production of a commercial motion picture distributed to a ~~National~~ NATIONAL audience is exempt from sales and use tax.

~~(2) The production of a commercial motion picture involves the process of recording the actions taking place within the motion picture and includes the actual shooting of the picture, either on location or at a motion picture studio, as well as the editing, dubbing and mixing of the motion picture.~~

(i) Examples of tangible personal property that may be directly used in the production of a commercial motion picture include film and tape products; set construction equipment and supplies; props, including livestock, motor vehicles, books, paintings and other tangible personal property when photographed as part of a scene; wardrobe; grip and lighting equipment; cameras; camera mounts including tripods; jib arms; steadicams; cranes; dollies; generators; walkie talkies; boats,

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trains, helicopters, airplanes, vans, trucks or other motor vehicles specifically equipped for motion picture production or used solely for production activities, wardrobe and makeup trailers; special effects and stunt equipment; video assists, videotape recorders, cables and connectors; sound recording equipment; and editing, dubbing and mixing equipment.

(ii) Examples of services performed upon tangible personal property that may be directly used in the production of a commercial motion picture include sound or music recording; creation of special effects or animation on film, tape or other audiovisual medium, including animation drawings, inkings, paintings, tracing and celluloid "cels"; preparation of storyboards for either animation or live photography; technological modification, including colorizing; computer graphics, including transfers of computer graphics on computer-generated media; sound dubbing or sound mixing; sound or music or effect transferring; film or tape editing or cutting; developing or processing of negative or positive prints; timing; coding or encoding; creation of opticals, titles, main or end credits; captioning; and medium transfers (for example film to tape, tape to tape).

~~(3)~~ (2) The ~~exclusion~~ EXEMPTION from sales and use tax provided for property and services directly used in production OF A COMMERCIAL MOTION PICTURE does not apply to either:

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(i) The purchase of property used for administrative purposes. Administrative purposes includes activities such as sales promotions, general office work, ordering and receiving materials, making travel arrangements, the preparation of shooting schedules, and the preparation of work and payroll records.

(ii) The purchase of catering services, as well as secretarial services, disinfecting or pest control services, building maintenance or cleaning services, help supply services, lawn care services, self-storage services and employment agency services, as terms are defined under section 201 of the TRC (72 P.S. § 7201). However, charges for employment agency services provided by theatrical employment agencies and motion picture casting bureaus are not subject to sales or use tax (72 P.S. § 7201(bb)).

~~(4)~~ (3) Where a single unit of tangible personal property is used in two different activities, one of which is a direct use and the other of which is not, the property will not be ~~excluded~~ EXEMPTED from tax unless the producer makes use of the property more than 50% of the time directly in the production phase of a commercial motion picture.

(c) Property and services purchased for resale.

(1) A producer may make certain purchases for resale. Materials and services on these materials that will become a component of the product sold may be purchased exempt from tax,

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if a properly completed exemption certificate is issued to the supplier.

(2) For example, the original negative is the medium (film, tape, and the like) first used in the camera when photographing live action, special effects, animation, computer generated images, and the like. The developing of the film is a service that is purchased for resale because the producer is selling the film on which the service is being performed.

(d) Installation, repair, maintenance and service of tangible personal property. Charges to install, repair, maintain or service equipment, parts, tools and supplies directly used in the production of a commercial motion picture are exempt from sales and use taxes. Examples of these services include:

(1) Installing illumination lighting and sound equipment.

(2) Installing special effects riggings.

(3) Connecting wiring from electrical sources to production equipment.

(e) Utilities used in production. Utilities used directly and exclusively in the production of a commercial motion picture are exempt from tax. Examples of taxable and exempt electricity usage:

(1) Electricity used for set lighting is exempt.

(2) Electricity used in a mobile trailer maintained for actors is taxable.

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(3) Electricity used to light and heat a temporary or permanent office is taxable.

(f) Exemption certificates.

(1) A producer shall furnish a properly completed exemption certificate AS REQUIRED UNDER 12 PA. CODE § 33.1 (RELATING TO FORM REQUIRED) to its vendors ~~to~~ WHEN CLAIMING AN EXEMPTION UPON THE PURCHASE OF THE FOLLOWING:

(i) ~~Exclude the producer's purchases of tangible~~ TANGIBLE personal property that becomes a physical component part of the commercial motion picture and is actually transferred to the customer ~~(for example, resale).~~

(ii) ~~Exclude the producer's purchases of~~ qualifying production PRODUCTION machinery, equipment, parts, tools or supplies for use directly in the production of a motion picture. ~~This certificate shall also be furnished to those who install, repair, maintain or service the exempt machinery, equipment, parts, tools or supplies. To claim this exclusion, the producer shall state on the certificate in the space marked "Other" the following: "Property or services shall be directly used in the production of a commercial motion picture under section 204(54) of the TRC (72 P.S. § 7204(54))."~~

(III) REPAIRS AND MAINTENANCE SERVICES PURCHASED BY A PRODUCER WHICH ARE PERFORMED UPON PRODUCTION MACHINERY, EQUIPMENT, PARTS, TOOLS OR SUPPLIES FOR USE DIRECTLY IN THE PRODUCTION OF A MOTION PICTURE.

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(2) ~~A properly completed exemption certificate shall be furnished and accepted in good faith no later than 60 days after delivery of the property or service or the sale will be considered a taxable sale.~~ THE EXEMPTION CERTIFICATE SHALL BE ANNOTATED IN THE SPACE MARKED "OTHER" AS FOLLOWS: "PROPERTY OR SERVICES WILL BE RESOLD OR SHALL BE DIRECTLY USED IN THE PRODUCTION OF A COMMERCIAL MOTION PICTURE UNDER SECTION 204(54) OF THE TRC (72 P.S. § 7204(54))."

Chapter 60. Sales and Use Tax Pronouncements - Statements of Policy.

§ 60.22. Reserved.

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