

COLORADO OFFICE OF THE STATE AUDITOR



GOVERNOR'S OFFICE OF ECONOMIC DEVELOPMENT
AND INTERNATIONAL TRADE

OFFICE OF FILM, TELEVISION, AND MEDIA



MAY 2017

PERFORMANCE AUDIT

THE MISSION OF THE OFFICE OF THE STATE AUDITOR
IS TO IMPROVE GOVERNMENT
FOR THE PEOPLE OF COLORADO

LEGISLATIVE AUDIT COMMITTEE

Representative Tracy Kraft-Tharp – Chair	Senator Tim Neville – Vice-Chair
Senator Kerry Donovan	Representative Lori Saine
Senator Cheri Jahn	Senator Jim Smallwood
Representative Dan Nordberg	Representative Faith Winter

OFFICE OF THE STATE AUDITOR

Dianne E. Ray	State Auditor
Monica Bowers	Deputy State Auditor
Andrew Knauer	Audit Manager
Kate Shiroff	Team Leader
Philip Siegel	Staff Auditors
Shannon Wawrzyniak	
Meghan Westmoreland	

AN ELECTRONIC VERSION OF THIS REPORT IS AVAILABLE AT
WWW.COLORADO.GOV/AUDITOR

A BOUND REPORT MAY BE OBTAINED BY CALLING THE
OFFICE OF THE STATE AUDITOR
303.869.2800

PLEASE REFER TO REPORT NUMBER 1670P WHEN REQUESTING THIS REPORT



OFFICE OF THE STATE AUDITOR



May 18, 2017

DIANNE E. RAY, CPA
—
STATE AUDITOR

Members of the Legislative Audit Committee:

This report contains the results of a performance audit of the Office of Film, Television, and Media, within the Office of Economic Development and International Trade. The audit was conducted pursuant to Section 24-48.5-115(4), C.R.S., which requires the State Auditor to conduct a performance audit of the Office of Film, TV, and Media no later than July, 1, 2017, and Section 2-7-204(5), C.R.S., which requires the State Auditor to annually conduct performance audits of one or more specific programs or services in at least two departments for purposes of the SMART Government Act. The report presents our findings, conclusions, and recommendations, and the responses of the Office of Economic Development and International Trade.

OFFICE OF THE STATE AUDITOR
1525 SHERMAN STREET
7TH FLOOR
DENVER, COLORADO
80203

303.869.2800



CONTENTS



Report Highlights	1
CHAPTER 1	
OVERVIEW OF THE OFFICE OF FILM, TV, AND MEDIA	3
Film Office Revenues and Expenditures	5
Audit Purpose, Scope, and Methodology	6
CHAPTER 2	
ADMINISTRATION AND CONTROLS OF FILM INCENTIVE FUNDS	9
Incentive Payments	10
RECOMMENDATION 1	22
RECOMMENDATION 2	24
Controls Over State Funds	25
RECOMMENDATION 3	34
Application Processing	36
RECOMMENDATION 4	41
In-State and Out-of-State Incentives	43
RECOMMENDATION 5	50
Effectiveness of Film Office Activities on Industry Development	52
RECOMMENDATION 6	61
APPENDIX	A-1



REPORT HIGHLIGHTS



OFFICE OF FILM, TELEVISION, AND MEDIA
PERFORMANCE AUDIT, MAY 2017

OFFICE OF ECONOMIC DEVELOPMENT
AND INTERNATIONAL TRADE

CONCERN

The Office of Film, Television, and Media (Film Office) lacks controls to ensure that it only pays incentives to production companies that qualify, to strategically target its incentive funds to provide the most benefit to the State, and to comply with statute in managing contracts and paying incentives. Further, the Film Office lacks information to assess the overall benefit it provides to the State.

KEY FINDINGS

- The Film Office paid about \$1.9 million in incentives for the nine projects in our sample even though none of them met all requirements. This included \$129,000 for projects that did not qualify for incentives and another \$1.8 million for projects for which the Film Office lacked documentation to substantiate they qualified. The Film Office also paid incentives totaling \$102,900 using the lower in-state spending threshold for two projects that do not appear to qualify under the in-state requirements. Paying incentives for projects without ensuring they qualify reduces the funds available for qualifying projects and diminishes the long-term economic benefit to the State.
- The Film Office paid about \$1.9 million in incentives for productions without having contracts in place before the projects began. The majority of this (\$1.3 million) was for projects for which no contract or purchase order was ever executed. Statute prohibits state agencies from disbursing funds unless the disbursement is supported by an approved purchase order or a contract.
- Film Office staff decide whether to approve an incentive based on undocumented conversations with interested companies and do not use uniform criteria to evaluate the extent to which a project supports the Film Office's strategic goals. The goals include offering funds to projects that provide the most economic development and to maximize job creation.
- The Film Office lacks complete and accurate information to assess and report on the effectiveness of its operations. Specifically, the Film Office does not collect data on full-time equivalent jobs created through the incentive program or the amount of income tax revenue the state collects due to these jobs.

BACKGROUND

- The Film Office was created in Fiscal Year 2012 to expand and revitalize the film industry in Colorado.
- One of the Film Office's major functions is to administer the State's film incentive program to encourage production in the State. The Film Office is also tasked with marketing Colorado as a destination for making films, television shows, commercials, and video games.
- A Colorado production project may receive an incentive if at least 50 percent of its employees are Colorado residents and it meets the following thresholds:
 - ▶ \$100,000 spent in the state if the company is an in-state company.
 - ▶ \$250,000 (for commercials, video games, and television shows) or \$1 million (for films) spent in the state if the company is an out-of-state company.
- The Film Office paid a total of \$10.6 million in incentives in Fiscal Years 2013 through 2016, for 31 productions, including 6 commercials, 4 documentaries, 7 feature films, 13 television shows, and 1 video game.

KEY RECOMMENDATIONS

- Implement controls to only pay incentives for projects the Film Office verifies as meeting the qualifications and that have contracts or purchase orders properly executed.
- Implement a documented application procedure, expand policies and procedures to include uniform criteria, and require documentation related to all potential incentive projects and approval decisions be maintained.
- Expand data collection and evaluation of the benefits of the incentive program and use complete and accurate data.



CHAPTER 1

OVERVIEW OF THE OFFICE OF FILM, TELEVISION, AND MEDIA

Colorado has had a program to promote film production in the state almost continuously for nearly 50 years. On July 1, 1969, the Colorado Motion Picture and Television Commission (Commission) became the first legislated film commission in the nation, established to promote Colorado as a location for filming. The Commission was defunded and eliminated in Fiscal Year 2003. In Fiscal Year 2006, the General Assembly changed statute to

annually appropriate \$500,000 from the State's Limited Gaming Fund to the Economic Development Commission (EDC) to give performance-based incentives of up to 10 percent of a production's budget to encourage film production in the state. At that time, the EDC was given the authority to spend 2.5 percent of the funds on administration of the film incentive program.

In Fiscal Year 2012, the General Assembly further modified statute to create the Office of Film, Television, and Media (Film Office), within the Governor's Office of Economic Development and International Trade (OEDIT) [Section 24-48.5-114, C.R.S.]. According to Section 24-48.5-115, C.R.S., the key responsibilities of the Film Office are described below.

CASH INCENTIVE PROGRAM. Statute states that a production company that meets minimum workforce and spending requirements outlined in statute may claim a financial incentive through the Film Office. Section 24-48.5-116(1)(a), C.R.S., states that the incentive amount shall be 20 percent of the production company's qualified local expenditures. A qualified local expenditure is defined as a payment made by a production company to a business in Colorado in connection with production activities in Colorado [Section 24-48.5-114(7), C.R.S.]. The specified spending minimums vary depending on whether the production company is an in-state or out-of-state business.

FACILITATION EFFORTS. The Film Office markets Colorado as a destination for producing feature films, television shows and commercials, and video games. The Film Office facilitates such production by helping companies scout Colorado locations for films and apply for needed permits, and by helping state and local government agencies in negotiations with production companies.

SUPPORT AND EDUCATIONAL EFFORTS. The Film Office carries out other activities that include partnering with film festivals, art organizations, and local businesses to provide educational seminars, panels, networking events, and film contests for those interested in film and media creation. The Film Office also offers grants for film production

at Colorado colleges, universities, and high schools, and subsidies for professional reviews of screenplays for Colorado residents.

Statute also authorizes the Film Office to offer loan guarantees to help production companies with limited capital secure loans for production in Colorado [Section 24-48.5-115(3)(a), C.R.S.]. To date, the Film Office has not entered into any loan guarantee agreements. The Film Office reports that it believes that the incentive program is a more efficient and effective mechanism to encourage production in Colorado and that there has been limited interest in the loan guarantee program. As a result, the Film Office does not currently accept applications for the loan guarantee program.

For the purposes of the Film Office, Section 24-48.5-114(1)(a), C.R.S., defines “film” as “any visual or audiovisual work, including, without limitation, a video game, television show, or a television commercial...” Therefore, in this audit report, references to film production, or the film industry, encompasses film, television, and video game productions and industries.

FILM OFFICE REVENUE AND EXPENDITURES

The Film Office receives \$500,000 annually in limited gaming funds pursuant to Section 12-47.1-701(2)(a)(VI), C.R.S., and had received an average of \$2.95 million annually in General Funds between Fiscal Years 2013 and 2017, pursuant to Section 24-48.5-116(5)(a)(II), C.R.S. As of May 2017, the General Assembly decreased the Film Office’s General Fund appropriation to \$750,000 for Fiscal Year 2018.

According to Section 24-48.5-116(5)(c), C.R.S., all funds the Film Office does not expend by the end of each fiscal year are available for expenditure in the next fiscal year without further appropriation. EXHIBIT 1.1 outlines the Film Office’s revenues and expenditures for Fiscal Years 2013 through 2016.



FILM OFFICE REVENUES AND EXPENDITURES

	FISCAL YEAR 2013	FISCAL YEAR 2014	FISCAL YEAR 2015	FISCAL YEAR 2016
REVENUES				
General Fund	\$3,000,000	\$800,000	\$5,000,000	\$3,000,000
Limited Gaming Funds	\$500,000	\$500,000	\$500,000	\$500,000
TOTAL REVENUES	\$3,500,000	\$1,300,000	\$5,500,000	\$3,500,000
EXPENDITURES				
Operations ¹	\$414,100	\$349,100	\$453,300	\$622,700 ²
Incentive Program	\$67,500	\$1,959,900	\$1,933,400	\$6,661,400
TOTAL EXPENDITURES³	\$481,600	\$2,309,000	\$2,386,700	\$7,284,100

SOURCE: Office of the State Auditor analysis of Film Office financial information.

¹ “Operations” includes expenses for all of the activities that the Film Office engages in (including salaries, rent, supplies, etc.) except for the payment of incentives.

² The Film Office reports that its operations costs have increased over the 4-year period because it expanded activities such as offering educational seminars, sponsoring film festivals, and awarding grants to Colorado colleges for student production activities as well as increases in the Office of Economic Development and International Trade’s general operating expenses.

³ The Film Office used funds rolled over from previous years to cover instances when expenditures were higher than revenues.

The Film Office has been appropriated 4.5 full-time equivalent employees (FTE) each year since Fiscal Year 2013. The Film Office employed 3.0 FTE in Fiscal Years 2013 through 2015 and then increased to 4.0 FTE in Fiscal Year 2016.

AUDIT PURPOSE, SCOPE, AND METHODOLOGY

We conducted this audit in accordance with Section 24-48.5-115(4), C.R.S., which requires the State Auditor to conduct an audit of the Film Office, the performance-based incentive program, and the loan guarantee program no later than July 1, 2017. The audit was also conducted in accordance with Section 2-7-204(5), C.R.S., the State Measurement for Accountable, Responsive, and Transparent Government (SMART) Act. Audit work was performed from August 2016 through March 2017. We appreciate the assistance provided by the management and staff of the Office of Film, Television, and Media, the Office of Economic Development and International Trade, the

Governor's Office, and the Economic Development Commission during this audit.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The key objectives of the audit were to:

- Assess the Film Office's activities to ensure compliance with statutory requirements and evaluate the Film Office's accomplishment of its statutorily intended purpose of developing the film industry in the state.
- Evaluate whether the incentive program is operated in accordance with statute and Film Office policies, and evaluate what impact the incentive has on the film industry in the state.

To accomplish our audit objectives, we performed the following audit work:

- Reviewed relevant state statutes and Film Office policies.
- Interviewed staff at the Film Office and the Office of Economic Development and International Trade; eight Certified Public Accountants who provided reviews of productions' financial documents; nine of the 10 commissioners from the Economic Development Commission; and a sample of incentive recipients.
- Gathered and analyzed documentation and data on the incentive applications, application reviews, Film Office expenditures, and incentive payment records.
- Analyzed the Film Office's appropriations and expenditures in Fiscal

Years 2013 through 2016 and encumbrances between July 1, 2012, and December 31, 2016.

- Gathered and reviewed data on changes in the incentive program's trends in the number of jobs created, cost per job, and productions incentivized per year in Fiscal Years 2013 through 2016.

We relied on sampling to support our audit work and selected the following sample:

- A non-statistical sample of nine projects that received incentives between Fiscal Years 2013 and 2016.

The results of our testing of this sample was not intended to be projected to the entire population. This sample was selected to provide sufficient coverage to test controls of those areas that were significant to the objectives of the audit.

We planned our audit work to assess the effectiveness of those internal controls that were significant to our audit objectives. Our conclusions on the effectiveness of those controls, as well as specific details about the audit work supporting our findings, conclusions, and recommendations, are described in CHAPTER 2 of this report.

CHAPTER 2

ADMINISTRATION AND CONTROLS OF FILM INCENTIVE FUNDS

One of the Office of Film, Television, and Media's (Film Office) major functions is to administer the State's film incentive program, which is a cash reimbursement for specific expenditures to encourage production companies to conduct production activities in Colorado [Section 24-48.5-115(2)(g), C.R.S.]. From Fiscal Years 2013 through 2016, the Film Office paid \$10.6 million in incentives for 31 productions including commercials, documentaries, feature films, television shows, and video games.

EXHIBIT 2.1 outlines the numbers and types of incentives the Film Office paid in Fiscal Years 2013 through 2016.



FILM INCENTIVE STATISTICS FISCAL YEARS 2013 THROUGH 2016

FISCAL YEAR	PRODUCTION TYPE	NUMBER OF PRODUCTIONS	INCENTIVES PAID	QUALIFIED LOCAL EXPENDITURES REPORTED	NUMBER OF IN-STATE JOBS REPORTED
2013	Commercial	1	\$67,500	\$374,200	95
2014	Commercial	1	\$66,900	\$334,500	52
	Feature Film	3	\$1,158,900	\$15,272,700	316
	Television	4	\$734,100	\$8,099,300	185
	TOTAL	8	\$1,959,900	\$23,706,500	553
2015	Commercial	2	\$121,300	\$621,900	82
	Documentary	1	\$94,300	\$472,500	22
	Feature Film	2	\$598,600	\$3,038,000	107
	Television	4	\$1,119,200	\$6,611,100	213
	TOTAL	9	\$1,933,400	\$10,743,500	424
2016	Commercial	2	\$77,800	\$389,100	86
	Documentary	3	\$165,700	\$985,200	17
	Feature Film	2	\$5,050,000	\$27,912,000	236
	Television	5	\$603,900	\$4,796,900	170
	Video Game	1	\$764,000	\$3,849,200	27
	TOTAL	13	\$6,661,400	\$37,932,400	536

SOURCE: Office of the State Auditor analysis of Film Office performance-based incentive data.

A list of incentivized projects between July 1, 2012 and March 31, 2017 is included in Appendix A.

INCENTIVE PAYMENTS

To receive an incentive, a production company must apply to the Film Office by requesting incentive funds for a specified production project and receive conditional approval from the Film Office and the Economic Development Commission (EDC). Once the production

company has completed the project, it must submit documentation of its qualified local expenditures to a Colorado Certified Public Accountant (CPA) and get a report from the CPA that its expenditures equal or exceed the minimum amounts necessary to receive the incentive, [Section 24-48.5-116(2)(c), C.R.S.]. After the CPA reports on the production company's qualified local expenditures and the production company certifies that it meets the eligibility requirements, statute, [Section 24-48.5-116(c)(I)], states that "the [Film] Office shall issue the incentive to the production company."

WHAT AUDIT WORK WAS PERFORMED, WHAT WAS THE PURPOSE, AND HOW WERE THE RESULTS MEASURED?

We reviewed a non-statistical sample of nine of the 31 productions that received an incentive in Fiscal Years 2013 through 2016. We selected the sample to review a variety of production types (e.g., feature film, commercial, and video game) and productions carried out by in-state as well as out-of-state production companies. We also selected the sample to include some productions in which the qualified expenditures or workforce amounts reported were close to the minimum requirements and therefore an error would be more likely to affect the production's incentive amount. These nine productions received a total of about \$1.9 million out of the \$10.6 million that the Film Office paid in incentives over the period we reviewed. We also contacted all 10 of the CPA firms that production companies hired to review production expenditures between Fiscal Years 2013 and 2016, and eight agreed to talk with us regarding how they carry out their reviews.

The purpose of our work was to evaluate whether the Film Office has adequate internal controls for managing the incentive program. Internal controls are processes designed to provide reasonable assurance that agencies will: (1) achieve their objectives; (2) operate effectively and efficiently; (3) safeguard public funds (including minimizing fraud, waste, and abuse); and (4) ensure compliance with applicable laws and regulations. State Controller policy, effective February 2016, adopted

the Standards of Internal Control in the Federal Government (also known as the Green Book) as the state standard for internal controls. Internal controls help ensure compliance with statutory requirements and policies and procedures. Therefore, our audit work evaluated the Film Office's controls for ensuring compliance with the requirements described below.

COLORADO WORKFORCE. Under statute, a production company is eligible to claim an incentive only if the workforce for the production's in-state activities is made up of at least 50 percent Colorado residents [Section 24-48.5-116(1), C.R.S.]. According to the Film Office, the workforce would include cast, crew, and any other individuals or vendors that appear on the production company's set roster, a list of cast and crew that are on the set during the day. Additionally, Film Office policies require production companies to submit documentation to the Film Office of the residency status of the workforce, which includes a declaration of residency form as well as proof of residency, such as a Colorado driver's license, for all in-state employees.

QUALIFIED LOCAL EXPENDITURES. Under Section 24-48.5-116(1), C.R.S., a production company's in-state expenditures must be a minimum of:

- \$100,000 for a Colorado production company.
- \$250,000 for an out-of-state production company creating a commercial, TV show, or video game in Colorado.
- \$1,000,000 for an out-of-state production company creating a film in Colorado.

Production companies can claim payments of up to \$1 million per employee or contractor in wages or salaries for individuals who participate in production activities as qualified local expenditures if they withhold and pay all Colorado income taxes [Section 24-48.5-114(7)(i), C.R.S.].

Statute requires a production company to apply to the Film Office prior to beginning production activities in the state [Section 24-48.5-116(2)(a), C.R.S.] and Film Office policies state that the production company must apply before filming begins. Additionally, Fiscal Rules require state agencies to have a signed purchase order or contract before work can begin [1 C.C.R., 101-1, Rule 2-2 (2.16)].

Film Office policy states that it will review the following before making incentive payments:

- A proof of performance document (required by Section 24-48.5-116(2)(c)(I), C.R.S.) that certifies in writing that the amount of its actual qualified local expenditures equaled or exceeded the minimum amounts (as listed above).
- A final budget and ledger detailing all of the production's qualified local expenditures, a total payroll report showing that state income taxes were withheld for payroll expenses, and a vendor list including addresses.
- A CPA review of the accuracy of the production's financial documents. Statute requires the production company to hire a Colorado licensed CPA to conduct this review [Section 24-48.5-116(2)(c)(I), C.R.S.].

WHAT PROBLEMS DID THE AUDIT WORK IDENTIFY?

The Film Office has not implemented internal controls to ensure that it only pays incentives to production companies that meet the Colorado workforce and local expenditure minimums. We found that the Film Office paid the production companies for all nine of the projects we reviewed a total of about \$1.9 million in incentives even though none of them met all applicable qualification and documentation requirements, as described below.

THE FILM OFFICE PAID \$129,900 IN INCENTIVES FOR PROJECTS THAT DID NOT QUALIFY. Specifically:

- The Film Office paid a \$65,400 incentive in Fiscal Year 2015 for one project for which no CPA report was submitted. This project was one of two separate projects with the same production company that began in the spring of 2013. The EDC had approved the projects separately—a \$368,800 incentive for an estimated \$4.7 million project and \$65,400 incentive for a smaller, \$800,500 project. The Film Office prepared a single contract that included the combined incentive amounts (\$452,200) for both projects, although the contract did not specify the project(s) to be completed and was never signed by the State.

When the production company completed its work on the larger project, it submitted a CPA report for that project and the Film Office paid the full combined incentive of \$452,200. The Film Office reported that it paid the combined amount because the production company exceeded its estimated Colorado spending on the larger project by more than it had estimated spending on the smaller project. The Film Office concluded that the combined incentive amount was warranted because the larger project alone had generated more economic benefit in the state than expected for both projects. However, according to the CPA report for the larger project, the company created only 47 jobs on the larger project for which the Film Office paid the combined incentive of \$452,200, but had estimated that it would create 61 jobs on the two approved projects. Therefore, the Colorado income tax withheld for the Colorado jobs was likely less than expected because fewer Coloradans were employed than was expected. Because there was no CPA review, documentation, or proof of performance submitted for the smaller project, the Film Office has no evidence of the actual qualified local expenditures or of the percentage of Colorado workforce for this production.

As discussed in a later section, the Film Office's decision to pay a higher than approved incentive for the larger project was contrary to

its historical practice of only paying the EDC approved incentive even when a project exceeds the estimated spending and workforce figures.

- The Film Office paid an incentive of \$28,000 for one project in Fiscal Year 2014 that did not meet the Colorado workforce minimum of 50 percent. The CPA report indicated that the minimum had been met, but the supporting documentation sent to the Film Office did not support the CPA report.
- The Film Office overpaid one incentive by \$36,500, or about 5 percent of the total \$764,000 approved amount, in Fiscal Year 2016. The overpayment occurred because the production company improperly included about \$212,000 in expenses that were incurred prior to the effective date of the contract. Therefore, the incentive the Film Office paid was more than 20 percent of the production's actual qualified local expenditures. The CPA report for this project did not identify or correct this error.
- We found another project with inaccuracies in the CPA report that the Film Office did not identify but that did not affect the incentive amount. For this project, the production company included about \$31,000 in payroll expenses for individuals who did not have Colorado income tax withheld. Statute only allows payroll to be included as a qualified local expenditure if Colorado income tax was withheld. In addition, the CPA applied the wrong local qualified expenditure threshold in calculating expenses.

THE FILM OFFICE PAID \$1.8 MILLION IN INCENTIVES WITHOUT HAVING DOCUMENTATION TO SUBSTANTIATE THAT REQUIREMENTS WERE MET. Specifically:

- **MISSING WORKFORCE DOCUMENTS.** The incentive file for one of the projects was missing proof of residency for the individuals listed as Colorado residents, the files for two projects were missing total workforce information (e.g., a full list of individuals employed), and files for five projects lacked *both* the residency documents and the

complete workforce information. As a result, we were unable to verify that the Colorado resident workforce for eight projects was at least 50 percent of the total workforce. The Film Office paid a combined total of \$1.8 million in incentives on these projects. Additionally, for one production, the CPA only calculated individuals for the total workforce who were listed on the payroll reports and not individuals who were paid as vendors. The Film Office reported that individuals paid as vendors should be included in the workforce total as long as they are listed on the production's daily set roster. The Film Office had no information on whether the individuals paid as vendors were Colorado residents. If they were not Colorado residents, but had been properly included in the total workforce calculation, the production would not have met the 50 percent Colorado resident workforce requirement.

- **LACK OF EXPENDITURE DOCUMENTS.** For one of these projects, the Film Office had no documentation at all to support the production company's expenditures. Additionally, none of the incentive files included supporting documentation that fully aligned with the expenditures included in the projects' qualified local expenditures totals. For example, in one file we reviewed, the local qualified expenditure calculations included gas and lodging expenses without vendor names or addresses that showed that they were made in-state and were associated with the production activities.
- **LACK OF PROOF OF PERFORMANCE.** The incentive files for two projects were missing the final proof of performance document which certifies that the production has completed all the necessary requirements of the contract and is required by statute.

WHY DID THESE PROBLEMS OCCUR?

INCOMPLETE GUIDANCE FOR CPA REVIEWS. The Film Office has not clearly defined the type of work a production company must require a CPA to perform to provide adequate assurance that a project has met the qualifications to receive an incentive. The Film Office includes a list of "Expectations for CPA Review & Report of Film Incentive Proof of

Performance” (which we refer to as the CPA expectations list throughout this section) which was included in all the contracts we reviewed. The list specifies that the CPA must verify certain information reported in the production company’s proof of performance, including the following:

- The financial information, including the budget for the entire production, non-qualified local expenditures, qualified local expenditures, and all backup documentation.
- Total Colorado payroll and proof of Colorado income tax withholding.
- Colorado production workforce information and all backup documentation, including the percentage of the production company’s workforce that were Colorado residents.

However, according to the CPA reports we reviewed, the production companies did not all require the CPAs to conduct the same type or level of verification for their projects. While six of the 10 CPAs who reviewed project files conducted an audit under auditing standards, the other four indicated that they had, “review[ed] the financial information related to production activities to verify the accuracy of the expenses incurred.” According to the American Institute of CPAs (AICPA) an audit is the highest level of assurance service that a CPA provides and is intended to corroborate the amounts and disclosures a company makes in its financial statements by obtaining audit evidence in a number of different ways including: inquiry, physical inspection, examination, and analytical procedures. In contrast, a review is substantially narrower in scope than an audit and does not include the examination of source documents such as receipts, testing of accounting records through inspection, or other procedures normally performed in an audit.

In addition to not having defined the type of work the CPAs should be required to conduct, the Film Office has not clarified the key purposes of the CPA review of expenditures. Specifically, the Film Office provides

no direction about whether the review is intended to verify that the qualified local expenditures claimed by the production company were (1) really payments to a person or business in Colorado in connection with production activities in Colorado, as required by statute; or (2) verifiable expenses connected with the production; or (3) both. For example, the CPA expectations list does not address how several common expenses we noted in our file review should be handled. We found reimbursements to production company employees for various items, including gas or lodging, without receipts or other documents that specified a vendor or business address. Without the addresses, it was not possible to determine if the expenses were in Colorado and/or related to the production. The Film Office provides no direction to CPAs on what information must be included in supporting documentation for expenses to confirm that the expense is qualified.

Finally, the CPA expectations list does not clearly outline how workforce numbers should be calculated and substantiated. The errors we found in our file review indicate that the CPAs do not know how they are expected to verify or calculate the workforce numbers and that they do not calculate the workforce numbers consistently. Four of the eight CPAs we interviewed reported that they verified workforce residency with payroll addresses instead of using the declaration of residency forms that the Film Office intends them to use to verify residency. The Film Office has not stipulated that the CPAs use the declaration form to verify residency. In addition, CPAs may have difficulty consistently identifying and reporting the total workforce count because production companies provide a variety of documents denoting employment, such as payroll records, daily set rosters, crew lists, and vendor lists; the Film Office has not stipulated which documentation should serve as the official employment list nor has it communicated to CPAs the circumstances under which vendors should be considered as part of the workforce.

LACK OF SUBSTANTIVE REVIEW FOR ELIGIBILITY. Film Office staff stated that they review each CPA report submitted solely to ensure that the CPA indicated that the production was eligible for the incentive. They reported that they have insufficient staff resources to do any further

review to ensure the incentives they pay are only for qualifying projects. Specifically:

- The Film Office does not review the CPA reports for reasonableness (such as to check that the CPA applied the correct local qualified expenditure criteria) or to identify any obvious errors, such as inconsistent information within the report or miscalculations.
- The Film Office does not verify the accuracy of the CPA reports by comparing them to any of the supporting documents it requires production companies to submit, such as proof of residency or expense documentation. The Film Office paid 46 incentives between July 1, 2012, and March 31, 2017, an average of about one per month. Therefore, if the Film Office reviewed one project every month against supporting documentation, it could ensure the accuracy of the CPA reports for virtually all of its incentive projects. We estimate it took one person no more than 8 hours to comprehensively compare a CPA report to supporting documentation during our audit (for those CPA projects where the Film Office had supporting documentation). Such reviews could likely be streamlined by the use of standard templates to guide and document them. Further, if the Film Office deems such reviews too resource intensive, it could check information in the CPA reports against supporting documents on a sample or risk basis, for greater efficiency. Either way, such reviews would require that the Film Office enforce its requirements for production companies to provide proof of residency documents and expense documents. The Film Office did not routinely enforce compliance with these requirements for the projects we reviewed.

Instituting a review of the reports for reasonableness, basic accuracy, and to verify the information in the reports against supporting documents would provide more assurance that the Film Office only pays accurate incentive amounts for fully qualifying projects.

An option to the Film Office implementing reviews to ensure CPA reports can be relied upon would be for it to seek statutory change such that the Film Office, rather than the production companies, contract

with a third party, such as a CPA firm, for verification that projects meet all incentive requirements. This approach would provide the Film Office with direct authority over the verification so that it could more directly, and potentially more efficiently, ensure that the work is of a scope and type to serve as a reliable basis for paying incentives. If the Film Office were to contract directly with the CPA firms to conduct the reviews, it could deduct the cost of the reviews from the incentive amount to avoid shifting the costs of the reviews from the production companies to the State. This option would still require the Film Office to clearly define the type and amount of work it would expect the third party to carry out.

WHY DO THESE PROBLEMS MATTER?

The Film Office's lack of controls has resulted in it paying incentives for ineligible production projects and creates a risk that ineligible payments will continue. When the Film Office pays incentives for productions that do not employ a workforce consisting of at least 50 percent Colorado residents, it is not incentivizing the creation of jobs or state income tax revenue to the extent intended by statute. Similarly, paying incentives for productions that did not reach the minimum qualifying expense level means that the Film Office is not incentivizing spending in Colorado to the extent intended by statute. Further, paying ineligible incentives reduces the amount available to offer for productions that meet all the requirements and therefore provide the economic benefits intended by statute.

When the Film Office is inconsistent in how it manages its incentives, it creates both the appearance and the actuality of inequity. Specifically, when the Film Office paid a higher incentive to one production company because it overspent its budget for one of two incentive projects, it departed from its typical practice of only paying the incentive amount approved by the EDC, even on projects that significantly exceeded their planned budgets, and violated its own policy and procedure manual which states, "the amount of incentive cannot exceed the maximum amount initially determined by the Office regardless of actual expenditures." In other cases, the Film Office has incentivized

different projects by the same company but treated each as a separate project that was expected to meet the minimum requirements on its own. Additionally, the Film Office reported that it considers productions to only be eligible for an incentive of up to the amount approved by the EDC and has denied requests for additional incentive funding when a company overspends its original budget.

RECOMMENDATION 1

The Office of Economic Development and International Trade should strengthen its oversight of the CPA review process by:

- A Establishing specific requirements in each project contract for the type of work production companies must require CPAs to conduct to provide adequate assurance that the project is qualified for the incentive payment. This should include defining the type of work, and the type of supporting documentation, (e.g., original receipts showing that the expenses were made in Colorado, and a complete list of production employees and residency documentation for all Colorado employees) that can be used to verify qualified local expenses and workforce figures.
- B Enforcing its policies that require production companies to submit specified documentation before paying the incentive.
- C Implementing reviews of the CPA reports to include reasonableness and general accuracy reviews of all reports and verification of the accuracy of at least some reports against underlying documentation.

RESPONSE

OFFICE OF ECONOMIC DEVELOPMENT AND INTERNATIONAL TRADE

- A AGREE. IMPLEMENTATION DATE: JULY 2017.

The Office of Economic Development and International Trade agrees that stricter definitions of cast, crew, and expenses can be implemented (in addition to what is already in place) in order to provide CPAs with stronger guidance of the type of report required for the program. The incentive contracts will be amended to include: 1) stricter definitions of workforce, 2) requirements about the type

of work production companies must require CPAs to conduct, and
3) the type of supporting documents production companies must provide to CPAs to carry out the specified work.

B AGREE. IMPLEMENTATION DATE: APRIL 2017.

The Office of Economic Development and International Trade began stricter enforcement of policies in April 2017. Since that time, the Office has not paid incentives on projects that were completed without first obtaining all required documentation.

C AGREE. IMPLEMENTATION DATE: APRIL 2017.

As of April 2017, the Office of Economic Development and International Trade strengthened reviews of CPA reports for reasonableness and general accuracy. CPA reports are reviewed against payroll reports and Colorado residency verification as provided by the project.

RECOMMENDATION 2

As an alternative to RECOMMENDATION 1, the Office of Economic Development and International Trade should evaluate the costs and benefits of the Office of Film, Television and Media contracting directly with a third party to verify qualified local expenditures and workforce figures and:

- A Use the results of the review to seek legislative change, as appropriate.
- B Establish specific requirements for the type and amount of work a third party must conduct to provide adequate assurance that the project is qualified for the incentive payment if the Office of Film, Television, and Media begins contracting for verification itself.

RESPONSE

OFFICE OF ECONOMIC DEVELOPMENT AND INTERNATIONAL TRADE

- A NOT APPLICABLE.

In light of the implementation of Recommendation 1, Recommendation 2 is not applicable.

- B NOT APPLICABLE.

See above.

CONTROLS OVER STATE FUNDS

To manage the State's incentive program, the Film Office accepts and reviews incentive applications for production company eligibility and project viability on a continuous basis. Once the Film Office approves an application, it is presented to the Economic Development Commission (EDC) for funding approval, conditional upon whether the production company meets the statutory criteria as discussed in the Film Incentives Finding. If the EDC approves funding for a production, the Film Office contacts the company to let it know and begins the process of executing a contract or purchase order with the company for the project. The Film Office pays the incentive, in accordance with statute [Section 24-48.5-116, C.R.S.], once the production is complete, the production company's CPA has reviewed and reported on the qualified local expenditures, and the production company has certified that the production has met statutory eligibility criteria.

EXHIBIT 2.2 shows the number of productions for which the Film Office executed contracts or purchase orders, including dollar amounts, between July 1, 2012, and December 31, 2016.



**INCENTIVE PROJECTS AND AMOUNTS
JULY 1, 2012 THROUGH
DECEMBER 31, 2016**

	FISCAL YEAR 2013	FISCAL YEAR 2014	FISCAL YEAR 2015	FISCAL YEAR 2016	JULY 1, 2016 THROUGH DECEMBER 31, 2016	TOTAL
Number of Projects with Executed Contracts or Purchase Orders ¹	7	10	20	18	6	61
Contracted Amount	\$1.4M	\$1.2M	\$9.2M ²	\$2.8M	\$2.1M	\$16.7M

SOURCE: Office of the State Auditor analysis of data from the State's financial management system, the Colorado Operations Resource Engine (CORE), and data provided by the Film Office.

¹Since the EDC approves projects throughout the year, the year in which a contract is executed may not be the year that the project was approved.

²This amount is for all of the projects that were contracted in Fiscal Year 2015. However, five of these projects, totaling \$1.6 million were approved in Fiscal Year 2014.

WHAT AUDIT WORK WAS PERFORMED, WHAT WAS THE PURPOSE, AND HOW WERE THE RESULTS MEASURED?

We reviewed all of the EDC approved incentive projects between July 1, 2012 and December 31, 2016. We also reviewed contract and purchase order information for the 61 incentive projects for which the Film Office executed contracts or purchase orders between July 1, 2012, and December 31, 2016. Of these 61 contracted projects, the Film Office has paid incentives for 43, totaling \$11.7 million. We also reviewed all of the EDC monthly meeting minutes for the same period to identify the incentive projects and amount of incentives that were approved by the EDC.

The purpose of the audit work was to evaluate the Film Office's controls for managing the commitment and disbursement of incentive funds for production projects against the following requirements:

- **DISBURSEMENT OF FUNDS.** Statute prohibits state agencies from disbursing funds unless the disbursement is supported by an

approved purchase order or a contract [Section 24-30-202(1), C.R.S]. In addition, Fiscal Rules require state agencies to maintain an adequate system of internal controls to identify and prevent or minimize the disbursement of funds without prior approval through a contract or purchase order [1 C.C.R., 101-1, Rule 2-2 (7.3)].

- **RECORDING THE OBLIGATION OF FUNDS.** Fiscal Rules require the State Controller or delegate to review contracts before approving them. The review process involves verifying that a number of requirements are met, including that funds are encumbered, before executing the contract [1 C.C.R., 101-1, Rule 3-1 (9.3.1.1.4)]. An encumbrance is an amount reserved in the accounting system to reflect a formal obligation of the State [1 C.C.R., 101-1, Rule 2-2 (2.7)].

WHAT PROBLEMS DID THE AUDIT WORK IDENTIFY?

We found that the Film Office does not have an adequate system of internal controls over the commitment and disbursement of incentive funds as illustrated by the problems discussed below.

DISBURSING FUNDS WITHOUT EXECUTED PURCHASE ORDERS OR CONTRACTS. We found that the Film Office paid a total of \$1.9 million in incentives for nine projects either without having a contract or purchase order in place, or without having a contract or purchase order in place before the project work began. Specifically we found:

- The Film Office paid about \$1.3 million dollars in incentives on four productions for which no contract or purchase order was ever executed. These payments represent 11 percent of the \$11.7 million the Film Office paid for all 43 projects, for which it paid incentives between July 1, 2012 and December 31, 2016.
- The Film Office executed two contracts after the production company completed production. The CPA reports in both instances indicated that the production period ended about a month before the

contract was executed. The Film Office paid about \$67,000 in incentives for each of these projects.

- The Film Office executed contracts for three projects after the production company began work on the project and thereby began earning the incentive. Specifically, the Film Office executed one contract in March 2013, about 2 months after the production company began work, and later paid the production company a \$307,000 incentive; the Film Office executed another contract in October 2013, almost 4 months after the production company began work, and later paid the production company a \$100,000 incentive; and it executed a third contract in May 2014, about 3 months after the production company began work, and later paid the production company a \$70,000 incentive.

NOT ENCUMBERING FUNDS. We found that the Film Office never encumbered funds in the state’s financial management system, the Colorado Operations Resource Engine (CORE), for three of the 61 contracted incentive projects (5 percent) we reviewed. The unencumbered projects totaled about \$820,000 in approved incentive funds. Further, the Film Office waited to encumber \$1.3 million in approved incentives for 12 other projects for between 31 and 206 days after it had executed the contracts or purchase orders, as illustrated in EXHIBIT 2.3. Projects can vary substantially in length, with commercials typically being completed and paid within about 6 months of executing a contract and TV shows often running more than a year.



INCENTIVE PROJECTS TIMING OF ENCUMBRANCES

NUMBER OF INCENTIVE PROJECTS	NUMBER OF DAYS BETWEEN CONTRACT/PURCHASE ORDER AND ENCUMBRANCE
46	0-30
9	31-60
1	61-90
2	>120
TOTAL	58¹

SOURCE: Office of the State Auditor analysis of data from state accounting systems, Colorado Operations Resource Engine (CORE) and Colorado Financial Reporting System (COFRS).

¹ Three of the contracts were never encumbered.

WHY DID THESE PROBLEMS OCCUR?

The Film Office reported that the reason some contracts were never executed is that the production companies refused to sign the contract because of concerns about some of the terms. For example, one of the standard contract terms stated that if the production company failed to perform, then the State would own the rights to any work product and copyright associated with the production. According to the Film Office, it worked with the Office of the State Controller and changed the terms in June 2014 so that the contract language was no longer an issue. We recognize that the Film Office needed to find a solution to the problematic contract language so that it could be effective in working with production companies to promote production in Colorado. However, the Film Office violated statute and Fiscal Rules when it chose to pay the incentives to production companies that refused to sign the contracts. Fundamentally, the Film Office still lacks basic controls to ensure that it complies with statute and fiscal rule, as described below.

THE FILM OFFICE LACKS CONTROLS TO ENSURE CONTRACTED PROJECTS ARE BEGUN AND COMPLETED IN A TIMELY MANNER. The Film Office reported two specific factors that have caused delays in contract execution:

- The film industry practice of applying for incentives in multiple states may mean that a production company is not willing to sign a contract until it gets multiple offers and decides which is best for it. In some cases, production could begin before this process is completed, particularly because some states offer incentives to projects already underway.
- The Film Office does not want to tie up funds it would otherwise consider available for commitment to another incentive project until it is fairly certain the contracted incentive will actually be earned. A company may not earn a contracted incentive if the project never actually occurs or does not meet all of the requirements; may not earn the entire incentive if the qualified local expenses are lower than projected; or may be delayed in earning the incentive if the beginning or completion of the project is delayed. We confirmed that just under 20 percent of the 48 incentive projects contracted and paid or released from July 1, 2012, through December 31, 2016, (13 of the total 61 contracted projects were still pending as of December 31, 2016, the date of our review) did not earn their contracted incentives. These projects represented \$2.0 million (12 percent) of the total incentive amounts contracted over the period.

To date, the Film Office has not implemented controls to help reduce delays in contracting and encumbering. For example, the Film Office does not require a production company to begin or complete an incentive project within a specified time after executing a contract. The Film Office also does not have procedures to unencumber funds for projects that are delayed for lengthy periods and require companies to reapply in such situations. We found that some other state film offices do impose deadlines. For example, the Texas film office does not allow production companies to apply for an incentive earlier than 60 days before the first day of production and in Washington, production companies must begin principal photography no later than 120 days after they receive approval for the incentive.

Further, the Film Office has not accurately reflected Fiscal Rule requirements related to encumbrances in its policies. The Film Office

policy and procedures manual states that once an incentive project receives approval from the EDC, the Film Office must execute a contract and then encumber the funds, rather than the reverse, as required by Fiscal Rules which state that the State Controller or delegate cannot sign a contract unless the funds are first encumbered [1 C.C.R., 101-1, Rule 3-1 (9.3.1.1.4)]. In practice, the encumbrance and contract execution should occur at essentially the same time.

WHY DO THESE PROBLEMS MATTER?

As a result of the Film Office not executing contracts or purchase orders for approved incentive projects, it received five statutory violation notices from the State Controller's Office on the 31 incentives (16 percent) it paid between July 1, 2012, and December 31, 2016. The Film Office received one of these statutory violations in Fiscal Year 2014, three in Fiscal Year 2015 and one in Fiscal Year 2017. A state agency can receive a statutory violation when it incurs a liability or makes a payment on the State's behalf without the prior approval of a purchase order or a contract, which violates Section 24-30-202(1) or (3), C.R.S. Fiscal Rules allow for the State Controller to ratify and pay an expenditure that received a statutory violation if certain conditions are met, including that the violation is not part of a consistent pattern of statutory violations [1 C.C.R., 101-1, Rule 2-2 (7.4.5)]. If the State Controller determines that the statutory violations are part of a consistent pattern, he or she can refuse to pay the obligation and Fiscal Rules create personal liability for any person who incurs, orders, or votes for an obligation, or makes a payment, which creates a statutory violation [1 C.C.R., Rule 2-2 (7.2)]. Thus, the Film Office places its employees and the EDC members at risk of being personally liable for any approved incentive amount that is not documented in an executed contract.

Not encumbering approved incentive funds at the time that contracts are executed could result in the EDC over-approving funds and the Film Office overspending its funds. The Film Office keeps a production tracking spreadsheet which staff report is used to track funds, inform the EDC about the amount available for approving new incentive

project applications, and help prevent overspending its appropriation. We reviewed the spreadsheet and found that it does not serve as an accurate means of tracking the funds available to prevent approving incentives or spending funds that are not available. Specifically, the spreadsheet does not have a consistently calculated monthly balance of available funds nor does it indicate when the Film Office determined that specific projects would not be produced in the state so that those committed funds could be made available for other projects.

Because of the errors in the Film Office's spreadsheet, we tracked the amounts the EDC approved, the amounts included in executed contracts, and the amounts the Film Office paid in incentives for all projects from July 2012 through December 2016, and found that the Film Office gave inaccurate information about how much money was left in its incentive account in all 24 of the 44 monthly EDC meetings that it presented its budget during this period because of the errors in its spreadsheet. The Office of Economic Development and International Trade staff reported to us that they use CORE to report the account balance information to the EDC. However, since the Film Office has not recorded encumbrances in a timely manner, CORE is also not an accurate source of information about the availability of incentive funds. Therefore, the EDC is making decisions about approving incentive projects using inaccurate information. We determined that 12 of the 61 contracts (20 percent) that the Film Office signed over the period we tracked overcommitted the Film Office budget at the time the contract was signed. If all of these projects had been completed during the period we reviewed, the Film Office would not have had sufficient funds to pay all of the incentives. According to our calculations, the incentive account balance was overcommitted by about \$1.7 million at the end of Fiscal Year 2015.

The Film Office's practice of not using the encumbrance process to accurately track the commitment of funds could harm the State's reputation and discourage production companies from considering Colorado for their projects. For example, once the EDC has approved a production company for an incentive, the company may view the commitment as firm, even before a contract is signed or work begins. If

the Film Office ever has to delay or deny an approved incentive payment because it has overcommitted funds, production companies may be reluctant to seek the incentive to film in Colorado and instead look at other states as preferred locations.

RECOMMENDATION 3

The Office of Economic Development and International Trade should improve its controls over film incentive funds and its compliance with requirements for encumbrances and contract execution by:

- A Implementing controls, such as internal deadlines, that require incentive funds to be encumbered and a contract executed within a limited and specified time after EDC approval.
- B Establishing controls to help ensure approved projects are completed in a timely manner. This may include stipulating timelines for applying for incentives, beginning and completing work on approved projects, unencumbering unneeded funds, and requiring reapplication for projects that are delayed beyond a specified deadline.
- C Revising the policy and procedure manual to accurately reflect Fiscal Rule requirements to encumber funds at the time contracts are executed.

RESPONSE

OFFICE OF ECONOMIC DEVELOPMENT AND INTERNATIONAL TRADE

- A AGREE. IMPLEMENTATION DATE: JULY 2017.

The Office of Economic Development and International Trade implemented a new procedure after the April and May EDC Meetings that encumbers approved funds immediately using a General Accounting Encumbrance. The Office will enforce timeliness of contract execution by: 1) sending contracts for approval before the EDC meeting and 2) creating an internal checklist that requires deadlines for contract execution.

B AGREE. IMPLEMENTATION DATE: JULY 2017.

In addition to the existing communication between production companies and the Film Office, the Office of Economic Development and International Trade will create a reasonable timeline for project execution based on the type and scale of potential projects. The Office will adhere to the set timelines and require follow up at specific milestones, which will be documented. Projects that get off track or need to be extended will require approval from the Office in writing.

C AGREE. IMPLEMENTATION DATE: JULY 2017.

The Office of Economic Development and International Trade will revise its policy and procedure manual to accurately reflect Fiscal Rule requirements to encumber funds at the time contracts are executed.

APPLICATION PROCESSING

For production companies to be eligible for an incentive, statute requires them to apply to the Film Office before beginning production activities in the state. The Film Office makes an initial determination about whether the project is eligible and the Economic Development Commission (EDC) votes to conditionally approve or to deny each project [Section 24-48.5-116(2), C.R.S.]. Conditional approval means that the Film Office will pay the incentive after production is complete, if the company certifies and the company's CPA report agrees that the production meets the statutory requirements.

The Film Office starts the process of evaluating projects for a film incentive by asking interested production companies to contact the Film Office to provide basic information about the project. According to Film Office staff they consider questions listed in the Film Office's policy and procedure manual, such as, "What are the major factors in selecting a location, convenience, or scenery?" and "What is your budget and what is your current financing status?" during their initial conversation with interested companies. The Film Office considers these questions guidance for their staff. Based on the conversation, staff evaluate whether the company has the capacity to successfully complete the project in terms of having adequate funding, experienced staff, and a logistical plan. If staff decide that the proposed project is not viable, or if the Film Office lacks sufficient funds to offer an incentive, staff recommend that the production company go no further and the process ends. Thus, the Film Office decides based on this conversation whether the potential project should be funded.

If staff conclude that a proposed project is viable and the Film Office has available funds, staff ask the company to submit a three-page form that contains information such as the production company's name and address; how many jobs it estimates it will create during the production;

and how much money it expects to spend on the production, both in-state and out-of-state. This document serves as the application and is presented at the EDC's monthly meeting where the EDC votes on the project. Based on the minutes of the EDC meetings from July 2012 through December 2016, the EDC approved all but one project that the Film Office presented, which it tabled. In the period July 1, 2012 through December 31, 2016, the Film Office received a total of 76 applications of which 72 were approved by the EDC. Of these 72, 61 resulted in signed contracts with a production company and the Film Office ultimately paid 43 of them an incentive. Not all projects approved by the EDC ultimately receive an incentive payment either because the production company never signs a contract with the Film Office or did not complete production.

WHAT AUDIT WORK WAS PERFORMED, WHAT WAS THE PURPOSE, AND HOW WERE THE RESULTS MEASURED?

We reviewed 31 of the 43 incentive applications for projects for which the Film Office paid an incentive from July 1, 2012 through December 31, 2016. These 31 applications represent all of the applications for projects that the Film Office paid an incentive in Fiscal Years 2013 through 2016. We also reviewed the Film Office's documentation for the three applications it denied in Fiscal Years 2013 through 2016. We used the following criteria to evaluate the Film Office's incentive application processes:

- **FILM OFFICE GOALS.** The Film Office has two goals to strategically use its funds to the benefit of the State. The first is to “strategically incentivize projects that will bring the most economic development to the State and prioritize projects that plan to spend money outside of metro Denver.” The second is to “utilize incentive funds strategically in order to maximize the number of jobs created and the number of qualified prospects served through our limited yearly funding.” Qualified prospects are incentive projects that are likely to meet the qualifications to receive an incentive.

- **TRANSPARENCY AND ACCOUNTABILITY.** The State Measurement for Accountable, Responsive, and Transparent (SMART) Government Act emphasizes accountability and transparency in state government programs, stating, “It is important that state government be accountable and transparent in such a way that the general public can understand the value received for the tax dollars spent by the state” [Section 2-7-201(1)(a), C.R.S.]. To achieve the intended accountability and transparency, we would expect a state program like the film incentive program, that is determining whether an entity is eligible for funding, to have and communicate uniform eligibility criteria, apply the criteria in a fair and consistent manner to determine eligibility, document the decision making process, and communicate eligibility decisions to interested entities in writing.

WHAT PROBLEMS DID THE AUDIT IDENTIFY AND WHY DID THEY OCCUR?

We found that the Film Office’s current process for accepting and processing applications does not promote achievement of its goals to strategically incentivize productions that bring the most economic development to the State, prioritize projects that plan to spend money outside of metro Denver, or maximize the number of jobs created and projects it incentivizes each year. The process also is not transparent to potential applicants, policy makers, or the public, as described below.

NO UNIFORM EVALUATION CRITERIA. The Film Office has no criteria for staff to use in interpreting the information obtained through the conversations with interested companies, even though these conversations serve as the sole process for the Film Office to determine whether a potential project should be offered an incentive. For example, the Film Office told us they ask interested companies about the experience of the production staff and the planning for the project, but the Film Office has not developed objective measures, such as the amount and type of experience production staff should have or the amount of planning that should have been completed, for staff to use in deciding whether a project should be offered an incentive. Staff reported

that their backgrounds in and knowledge of the film industry allow them to accurately gauge an interested company's capacity and make a denial decision without either specified criteria or any further evaluation of the project. They indicated that they use this informal process so that production companies do not incur the time and cost of completing the three-page application until they know that the project will be recommended for an incentive.

NO DOCUMENTATION OF THE EVALUATION OR DECISION PROCESS. We found the Film Office maintained virtually no documentation of how it reached decisions to fund proposed incentive projects. Specifically:

- The Film Office does not keep records of all of its conversations with companies interested in an incentive, such as notes about the major factors the company said were important in selecting a location or the company's budget and financing status (questions staff said they routinely ask). The Film Office does have some records of production company interest that includes contact information, but it does not track project information during those phone calls and does not always log contact information for every interested production company that calls.
- Film Office staff had no records indicating how and why they decided a company should submit a written application or not.
- The Film Office had no records indicating that staff conducted any further evaluation of potential projects once completed application forms were submitted. In Fiscal Years 2013 through 2016, the Film Office received 76 applications and recommended all but three to the EDC (96 percent). The Film Office reported that this high approval rate is due to its informal assessment and decision process.
- The Film Office had a letter for only one of the three written applications it denied, which stated that the reason for denial was that the production company applied after it had completed much of its production, so it did not meet the statutory requirement to apply before beginning production in the state. The Film Office did not have any documentation showing why the other two written

applications were denied or that it had communicated the reasons to the applicants.

WHY DO THESE PROBLEMS MATTER?

It is important for the Film Office to have a consistent, documented process for evaluating incentive applications for two reasons. First, the lack of guidance and criteria on what makes a good incentive project means the process is not designed or operating to allow the Film Office to strategically maximize its incentive funds by awarding them to projects with the highest expected economic impact, which is one of its strategic goals. Second, without a documented evaluation and decision process, the Film Office's decisions are not transparent and do not demonstrate accountability for making decisions that are fair, consistent, and effective in accomplishing the Film Office's purpose. In fact, the current application procedure appears to promote the approval of projects based solely on staff's perception of the company's capacity and ability to meet the minimum spending requirements, not on criteria that reflect the goals of using funds strategically to provide the most economic development or maximize job creation.

Further, the current informal process is not consistently documented and does not allow the Film Office to track how many production companies have shown interest in the incentive over any period and the proportion that were denied. Thus, the Film Office does not have data to evaluate the extent of unmet interest in film production in Colorado so that it can accurately represent its resource needs to policy makers. The Film Office staff stated that they do sometimes log information about interested projects into a database, but that they have not been consistent about doing so for every project and that the individual records are incomplete with only the name of the project and contact information for the production company, but no information about the project budget. Further, Film Office staff told us that the State has lost production projects to surrounding states based on not having enough incentive money, but because its documentation of the application and evaluation process is so minimal, it could not provide us with any supported data to illustrate the loss.

RECOMMENDATION 4

The Office of Economic Development and International Trade should improve the incentive application process by:

- A Implementing a documented application procedure that ensures that the Office of Film, Television, and Media collects comprehensive and consistent information on all prospective incentive projects.
- B Expanding the Office of Film, Television, and Media's policy and procedure manual to include uniform criteria to be used in evaluating proposed projects and making recommendations to the Economic Development Commission. The criteria should include factors that reflect the production company's capacity for the project, the expected economic benefit, and how the project furthers the Office of Film, Television, and Media's strategic goals.
- C Implementing written policies and procedures to maintain documentation related to all potential incentive projects that includes the reasons why each project was denied or recommended for approval.
- D Implementing a documented method of informing interested production companies of the reasons why the Office of Film, Television, and Media has denied a proposed project.

RESPONSE

OFFICE OF ECONOMIC DEVELOPMENT AND INTERNATIONAL TRADE

- A AGREE. IMPLEMENTATION DATE: JULY 2017.

The Office of Economic Development and International Trade will

create an application checklist and maintain a log of all applications and prospective projects to ensure all the required information is collected consistently in accordance with the checklist.

B AGREE. IMPLEMENTATION DATE: JULY 2017.

For evaluating incentive projects, the Office of Economic Development and International Trade will modify existing policies to develop and use uniform criteria for all applicants. The Office will also create a rating scale for the criteria that allows factors such as project viability, past experience from production companies, and overall economic development of the project, to be used as measures for recommending or denying projects to the EDC.

C AGREE. IMPLEMENTATION DATE: JULY 2017.

The Office of Economic Development and International Trade will implement written policies and procedures to maintain documentation related to all potential incentive projects that includes the reasons why each project was denied or recommended for approval.

D AGREE. IMPLEMENTATION DATE: JULY 2017.

The Office of Economic Development and International Trade agrees to implement a standardized method of informing interested production companies of the reasons why the Office has denied a proposed project.

IN-STATE AND OUT-OF-STATE INCENTIVES

Colorado's film incentive program is available to both in-state and out-of-state production companies. EXHIBIT 2.4 shows incentives the Film Office paid to in-state and out-of-state production companies in Fiscal Years 2013 through 2016.



FILM INCENTIVES PAID TO IN- AND OUT-OF-STATE COMPANIES FISCAL YEARS 2013 THROUGH 2016

FISCAL YEAR	2013	2014	2015	2016	TOTAL
In-State Production Companies	0	4	6	10	20
In-State Incentive Amounts	\$0	\$490,700	\$863,400	\$840,500	\$2,194,600
Out-of-State Production Companies	1	4	3	3	11
Out-of-State Incentive Amounts	\$67,500	\$1,469,200	\$1,070,000	\$5,820,900	\$8,427,600
Total Number of Productions	1	8	9	13	31
Total Incentive Amounts	\$67,500	\$1,959,900	\$1,933,400	\$6,661,400	\$10,622,200

SOURCE: Office of the State Auditor analysis of Film Office incentive data.

The differences between the in-state and out-of-state incentive requirements are shown in EXHIBIT 2.5. Specifically, the workforce requirements are the same for both, but the amount of qualified local expenditures required for in-state production companies is lower for all types of productions.



STATUTORY REQUIREMENTS IN-STATE AND OUT-OF-STATE INCENTIVES

	IN-STATE PRODUCTION COMPANY	OUT-OF-STATE PRODUCTION COMPANY
Colorado Resident Percentage of Workforce	50%	50%
Total Qualified Local Expenditures for TV Shows, Commercials, and Video Games	\$100,000	\$250,000
Total Qualified Local Expenditures for Films	\$100,000	\$1,000,000

SOURCE: Office of the State Auditor analysis of Section 24-48.5-116 (1), C.R.S.

WHAT AUDIT WORK WAS PERFORMED, WHAT WAS THE PURPOSE, AND HOW WERE THE RESULTS MEASURED?

We reviewed all 31 of the Film Office’s paid incentive productions in Fiscal Years 2013 through 2016 to evaluate whether the production companies that were approved for an in-state incentive met the following requirements to qualify for the in-state incentive:

- **DEFINITION OF A PRODUCTION COMPANY.** Statute defines a production company as a person, including a corporation or other business entity, *that engages in production activities* [emphasis added] for the purpose of producing all or any portion of a film in Colorado [Section 24-48.5-114(6), C.R.S.].
- **DEFINITION OF IN-STATE.** According to statute, an in-state production company “has been a resident of the state or registered with the Secretary of State for at least 12 consecutive months; except that, if the production company creates a business entity for the sole purpose of conducting production activities in the state, then such business entity need not be registered with the Secretary of State for 12 consecutive months, but the owner of the business entity must be a resident of the state for at least 12 consecutive months” [Section 24-48.5-114(4), C.R.S.].

WHAT PROBLEMS DID THE AUDIT WORK IDENTIFY?

We found problems with the qualifications of two of the 20 production companies that were approved for in-state incentives over the period we reviewed, as described below.

ONE COLORADO COMPANY DID NOT APPEAR TO BE A PRODUCTION COMPANY. For one feature film production, we found that an out-of-state production company applied for an incentive and also listed an in-state production company on the application. Although the in-state company met the statutory requirement of having been registered with the Secretary of State for at least 12 consecutive months, there are indicators that it was not a production company. Specifically:

- None of the Secretary of State filings for the company listed the principal address as a Colorado address and the company's registered owner was not a Colorado resident at the time of production.
- The Film Office had no evidence that this in-state company had carried out production activities prior to, during, or after the incentive project. In fact, according to the documentation the production company submitted to the Film Office, all of the production expenses for the incentive project were incurred by the out-of-state production company, suggesting that the in-state company was not involved in any production activities.
- Readily available online information about the film does not identify the in-state company as one of the several production companies associated with the film. Specifically, the film's production credits, information on the Internet Movie Database (an online database of information related to films and television programs), and Wikipedia do not include the name of this in-state company as one of the production companies associated with the film.

The Film Office paid the full incentive, which totaled about \$82,000, based on the out-of-state production company reporting it incurred

\$455,000 of local qualified expenditures, which exceeds the *in-state* spending threshold of \$100,000. If the Film Office had determined that the in-state company named on the application was not a Colorado production company, and therefore considered the applicant to be an out-of-state company, the company would not have met the out-of-state threshold of \$1,000,000 and would therefore not have been qualified for the incentive.

ONE PRODUCTION COMPANY DID NOT APPEAR TO MEET THE INTENT OF THE IN-STATE REQUIREMENT. This production company technically qualified for the in-state incentive as it was registered with the Secretary of State for at least 12 consecutive months, but if the intent is for the in-state incentive to be available to businesses that have long-term operations in Colorado, we found indications that this intent was likely not achieved in this case. Specifically:

- The incentive application, the purchase order executed by the Film Office, and the production company’s proof of performance all cite only an out-of-state address for the company.
- The Film Office had no evidence that the company engaged in any business activities in Colorado after the incentive project.

WHY DID THESE PROBLEMS OCCUR?

THE FILM OFFICE ENCOURAGES OUT-OF-STATE COMPANIES TO APPLY JOINTLY WITH IN-STATE COMPANIES. Film Office staff reported that they routinely recommend that out-of-state production companies apply jointly with in-state companies in order to apply for an in-state incentive. The Film Office believes that it has the authority to approve projects that are primarily operated by out-of-state companies based on the in-state criteria, but the Film Office does not verify that an in-state company actually participates in any way on an incentive project that is approved according to the in-state criteria. The Film Office reported that it believes that allowing out-of-state companies to take advantage of the lower minimum qualified local expenditure requirements through some type of association with an in-state company is a legitimate means

of promoting production and job creation in Colorado. For the same reason, the Film Office does not verify that the businesses listed on an application are production companies as defined in statute, rather than other types of businesses.

THE STATUTORY DEFINITION OF AN IN-STATE COMPANY IS LIMITED. Statute only specifies that a person or business entity must meet one of two requirements to be considered an in-state company for the purposes of the film incentive: (1) be registered with the Secretary of State for at least 12 consecutive months; or, (2) if a newly created business, be owned by someone who has been a Colorado resident for at least 12 months. These requirements provide only limited assurance that an applicant claiming in-state status is actually a legitimate, ongoing operation in Colorado. If the intent of the General Assembly was to incentivize companies that maintain some type of ongoing operations in Colorado, verifying registration with the Secretary of State or that a business owner had resided in Colorado for 12 months at some point in time does not accomplish that intent because they do not indicate that any business activity is actually occurring in Colorado. To date, the Film Office has not established additional requirements for applicants that could help achieve this intent.

We conducted research to try to determine what other information would indicate that a business is actively operating in Colorado and found no single source. For example, unless a business employs at least one employee on an ongoing basis, it does not need to carry workers' compensation insurance and would therefore not be known to the Colorado Department of Labor and Employment; if a business does not collect and remit state or local sales taxes, it is not required to obtain a business license from the Colorado Department of Revenue. Some businesses must file a business tax return with the Department of Revenue but the Department of Revenue is prohibited from sharing tax filing information with other state agencies. Although we found no readily available source to verify the in-state status of a business, the Film Office could require applicants to provide some type of additional evidence of their operations to gain greater assurance that the companies it approves for the in-state incentive are in-state companies.

For example, the Film Office could require a company seeking in-state status for the film incentive to provide one or more of the following as evidence that they have ongoing business in Colorado, such as:

- Current Colorado state business tax returns.
- Documents showing the company employs Colorado residents and pays the associated payroll taxes.
- Evidence that the company maintains worker’s compensation insurance for Colorado employees (if applicable).
- Utility bills or lease agreements that indicate the company’s presence in Colorado.

WHY DO THESE PROBLEMS MATTER?

Statute does not specify why there is a lower spending threshold for in-state production companies to be eligible for incentives. However, given the overall intent and goals of the incentive program to increase jobs, spending in the state, and state income tax revenue, it is reasonable to infer that the intent may have been to encourage the establishment of long-term infrastructure and ongoing production activities within the state. By having a lower spending threshold for a Colorado business to qualify for the incentive, the State is more likely to encourage the development of such infrastructure and see longer-term financial benefits, such as additional state and local tax revenue and more permanent job opportunities. When the Film Office pays an incentive to an out-of-state company based on a production meeting the lower in-state spending threshold, the Film Office reduces the amount the production company is incentivized to spend in the state during the production, which reduces the short-term economic benefit to the State, and the Film Office is not maximizing the long term economic benefits of the incentive.

Finally, in treating projects that are primarily completed by out-of-state production companies as in-state, the Film Office may mislead the EDC

in its decision on whether to approve an application, and policymakers and the public about the extent to which the incentive supports long-term economic development in the state.

RECOMMENDATION 5

The Office of Economic Development and International Trade should clarify how the requirements for in-state production companies are applied to the film incentive program by:

- A Implementing policies and procedures that more narrowly define an in-state company. To maximize the value of the incentives, the definition should focus on companies that have, or plan to have, ongoing operations in the state. The Office of Economic Development and International Trade should work with the General Assembly, if needed, to seek statutory changes related to the definition of an in-state company.
- B Implementing and enforcing requirements that applicants seeking in-state status provide evidence that they meet the definition established in response to PART A. This could include requiring submission of proof of business operations such as business tax records, worker's compensation insurance coverage, employee payroll tax records, or utility bills.

RESPONSE

OFFICE OF ECONOMIC DEVELOPMENT AND INTERNATIONAL TRADE

- A AGREE. IMPLEMENTATION DATE: JULY 2017.

The Office of Economic Development and International Trade will implement policies and procedures that more narrowly define an in-state company. The Office can implement stricter guidelines within the current latitude of the statute. An in-state company is currently defined as being formed by a Colorado resident (who has been a resident for at least one year), or a company that has been registered

with the Colorado Secretary of State for at least one year. The Office will further define that an in-state company must be registered with the Colorado Secretary of State for at least one year AND engage in active production activities within that time period.

B AGREE. IMPLEMENTATION DATE: JULY 2017.

The Office of Economic Development and International Trade will require evidence that companies meet in-state status, as defined above, which may include business tax and insurance records, or other relevant documentation.

EFFECTIVENESS OF FILM OFFICE ACTIVITIES ON INDUSTRY DEVELOPMENT

Each year, the Governor's Office of Economic Development and International Trade (OEDIT) issues a report that contains information on the impact of the Film Office. According to the Film Office, between Fiscal Years 2013 and 2016, the 31 incentivized film projects created about 1,600 jobs, and the production companies spent an estimated \$72.8 million in the state. In addition, Film Office annual reports cite an estimated increase of about \$157.2 million in overall economic activity in the state due to the incentives over the 4-year period. The Film Office reports that this increase in economic activity is estimated using a multiplier calculated in 2014 by the University of Colorado, Leeds School of Business. In 2014 the Film Office contracted with Leeds to conduct a study on the economic impact of the incentives. Leeds used IMPLAN, an economic modeling software tool, to calculate an overall multiplier effect of the incentive program. Qualified local expenditures and Colorado jobs reported to the Film Office were input into IMPLAN, which measured their effects on the film and media industry in the state and calculated a multiplier of 1.71. The multiplier indicates that for every \$1 in incentives issued, an additional \$0.71 in economic benefit was generated.

In addition to managing the incentive program, the Film Office conducts other activities such as marketing Colorado as a destination for film production and offering educational seminars to promote the film industry and employment in Colorado.

WHAT AUDIT WORK WAS PERFORMED, WHAT WAS THE PURPOSE, AND HOW WERE THE RESULTS MEASURED?

We reviewed statute and the Film Office's goals; documentation of incentivized productions, including how much the production companies reported spending, the length of the productions, and state income taxes withheld for local employees; and the information reported in OEDIT's Fiscal Years 2013 through 2016 annual reports about Film Office outcomes. We also reviewed and analyzed data for 2006 through 2015 from the Bureau of Labor Statistics for information on employment and businesses in the Motion Picture and Video Production Industries on a national level and to compare Colorado with Utah and New Mexico, nearby states that sometimes compete with Colorado for production activity. The Bureau of Labor Statistics gives estimates on paid part-time and full-time workers in different occupation classifications as well as business numbers and locations.

The 10-year period we reviewed covers the changes in the incentive program, from the initial appropriation of \$500,000 in 2006, to the increase in funding and incentive percentage for productions that began in Fiscal Year 2013, to the most recently available data in 2015. The purpose of the audit work was to evaluate the Film Office's effectiveness in accomplishing legislative intent. According to the legislative declaration in House Bill 12-1286, which reestablished the Film Office and increased the incentive from 10 to 20 percent, the General Assembly intended the Film Office to promote growth in the film industry in Colorado and thereby have a positive impact on Colorado's economy and job creation. This intent is reflected in the Film Office's goals, which include attracting new jobs and maximizing economic development in the state related to the film industry. Our audit work also reviewed the extent to which the Film Office tracks relevant outcome data that can be used to guide its strategies and operations as well as to inform the public and policy makers about the costs and benefits of the Film Office.

WHAT PROBLEMS DID THE AUDIT WORK IDENTIFY AND WHY DID THEY OCCUR?

The Film Office routinely tracks and reports on a number of outcomes of its activities, such as the number of jobs created and the amount of increased spending in Colorado due to incentivized projects. However, we found that it is difficult to determine a comprehensive benefit the State receives from the Film Office for two reasons, as discussed in this section.

SOME OF THE DATA THAT THE FILM OFFICE USES TO REPORT ITS OUTCOMES CONTAIN INACCURACIES. The Film Office gathers information on the number of jobs created and in-state spending due to film production from the incentivized productions' CPA reports. However, as we noted in the Incentive Payments finding, these reports sometimes contain inaccurate workforce and/or expenditure information. Additionally, the Film Office policy requires the CPAs to *verify* total expenditures and workforce numbers, but not to *report* these figures to the Film Office. While most of the CPA firms do report the figures, one firm simply reported that it verified that the minimum requirements for the incentive were met for the productions it reviewed. As a result, the information the Film Office receives from the CPAs and uses to report outcomes is inconsistent.

THE FILM OFFICE LACKS INFORMATION ON FTE AND INCOME TAX REVENUE FROM INCENTIVE PROJECTS. A 2015 study completed by the Pew Charitable Trusts for the state of Maryland identified best practices for evaluating film tax credits in order to fully measure economic benefit. The study recommended states include a variety of factors in evaluating the benefits of their programs, including the number of FTE created (rather than simply counting jobs) and the amount of state income taxes collected due to the programs.

Currently, the Film Office does not track these measures. The Film Office does not request information such as the number of days or hours

Colorado residents worked on incentivized productions so that it can calculate FTE jobs, or the amount of income tax withheld for all jobs. Typically, one FTE represents one full-time job over a 1-year period. For example, for budgeting purposes, state agencies define one FTE as one employee who works full-time (2,080 hours) for a 1-year period. Some production companies and CPAs provided detailed information to the Film Office on the number of hours production employees worked and on income taxes withheld, but this detailed reporting is not required. Collecting information to be able to calculate and report FTE jobs as a consistent measure of job creation for each incentivized project and across projects is important because not only are jobs in the film industry often temporary, the variance in length of employment among different kinds of productions is significant. Also, collecting and reporting the amount of income tax revenue generated through incentivized productions would allow the Film Office to review and report the benefit of the program to the State. Currently, the Film Office reports total payroll amounts as a benefit of the program, however, it is likely that the wages for out-of-state employees will not be spent in the state. Therefore, a more accurate measurement of the benefit to the State would be to calculate wages for in-state employees and only payroll taxes for out-of-state employees, instead of the total payroll amounts.

We conducted a limited analysis of the FTE impact, cost per job, and cost per FTE for three productions for which the data were available. As EXHIBIT 2.6 shows, using the cost per reported job to assess or report the workforce benefits of a project could be misleading. We found that for the three projects, the variations in length of resident employment had a significant impact on the number of FTE generated. Even though the video game production reported the fewest Colorado resident jobs, it actually created more FTE than the other two projects. Using an FTE measure, rather than a jobs measure, allows for a more accurate picture of the workforce impact that can be compared across different types of productions.



ANALYSIS OF COST PER JOB AND FTE FOR VARIOUS PRODUCTION TYPES

	VIDEO GAME	FEATURE FILM	COMMERCIAL
Incentive Amount Paid	\$764,000	\$82,000	\$20,900
Total Colorado Jobs reported	30	40	33
Cost per job	\$25,500	\$2,050	\$630
Length of Production	1 year	3 weeks	3 days
Total Colorado FTE ¹	33.82	1.95	0.43
Cost Per FTE ²	\$22,600	\$42,000	\$48,400

SOURCE: Office of the State Auditor analysis of Film Office production data.

¹ Total Colorado FTE was calculated by taking the total number of hours worked by Colorado residents, as reported by the production company, and dividing it by 2,080 for each resident employee.

² Cost per FTE was calculated by taking the total incentive paid to the production divided by the FTE.

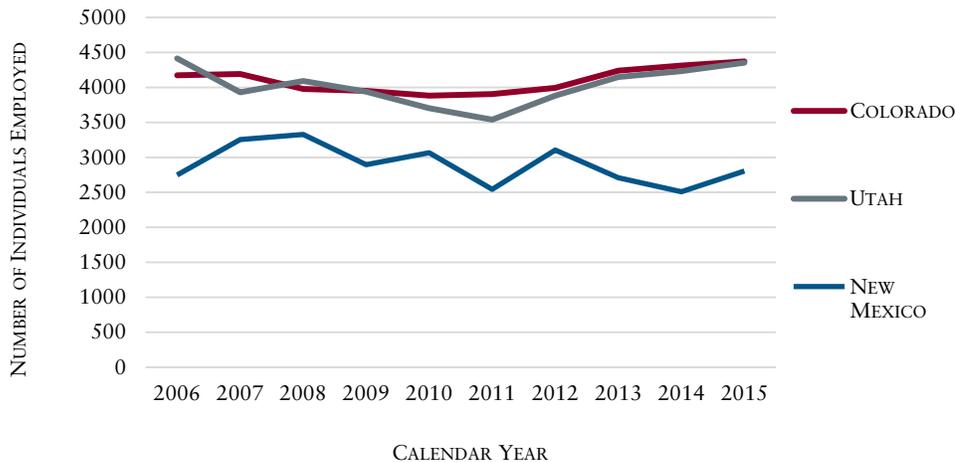
THE FILM OFFICE DOES NOT ANALYZE HOW INCENTIVIZED PRODUCTIONS IMPACT OVERALL COLORADO INDUSTRY CHANGES. According to the Film Office, as well as professionals in the film and media industry who participated on a recent panel presentation on the state of film in Colorado, the incentive program has been achieving its purpose in drawing more productions to the state, competing with other states, and increasing the production infrastructure in the state. However, the Film Office does not collect data on the changes that have occurred in the Colorado film industry overall and compare that to information from the projects it incentivizes.

We assessed the changes in employment and number of establishments in the media professional industry using data from the Federal Bureau of Labor Statistics from Calendar Year 2006 to 2015. EXHIBIT 2.7 shows Colorado employment in the media professional categories from 2006 to 2015. EXHIBIT 2.7 also shows the number of individuals employed in the media professional industry in Utah and New Mexico, which sometimes compete with Colorado for film production projects and which annually give roughly \$7 million and \$50 million in tax credit incentives, respectively. Between Calendar Years 2006 and 2015, the number of individuals employed in the media professional industry increased an average of about 0.6 percent annually in Colorado compared to average increases of about 0.05 and 1.1 percent annually,

respectively, in Utah and New Mexico. Since the Film Office incentive increased from 10 to 20 percent, effective in Calendar Year 2012, growth in the industry in Colorado, averaged 3.1 percent annually, lagging behind Utah, with average annual growth of 3.9 percent, but outpacing New Mexico, whose annual growth averaged a 2.8 percent decrease annually over the same period.



TOTAL MEDIA PROFESSIONAL¹ EMPLOYMENT CALENDAR YEARS 2006 THROUGH 2015



SOURCE: Office of the State Auditor analysis of Bureau of Labor Statistics data for Occupational Employment Statistics data.

¹ Individuals employed were listed under BLS Occupation Codes for arts, design, entertainment, sports, and media occupations (North American Industry Classification System code 5121) with the sub-occupations of creative media and include occupations such as, actors, camera operators, film and video editors, graphic designers, multimedia artists and animators, music directors and composers, producers and directors, set and exhibit designers, sound engineering technicians, and media and communication equipment workers.

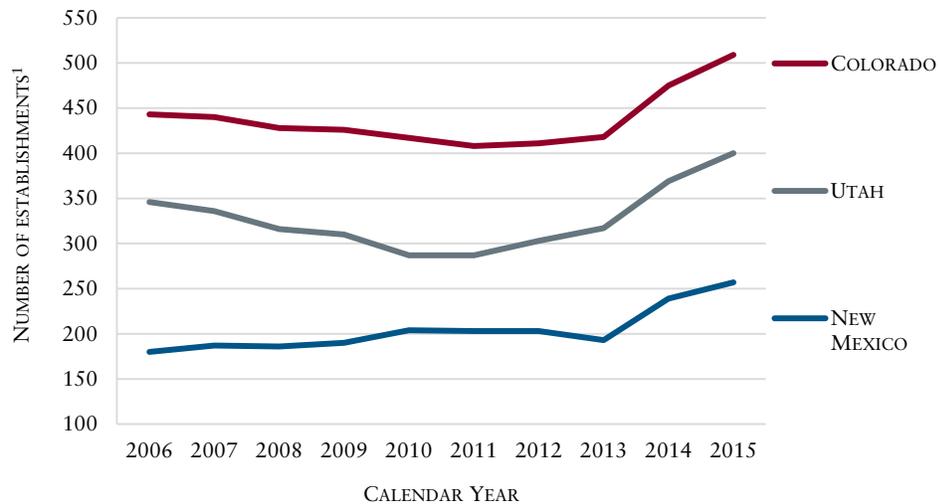
According to Film Office data, between Calendar Years 2013 and 2015 incentivized productions created between 318 and 743 jobs annually and grew at an average rate of 56 percent.

As shown in EXHIBIT 2.8, between 2006 and 2015, the number of motion picture and video businesses in Colorado increased, with average annual growth of 1.7 percent. Utah saw a similar increase

averaging 1.9 percent annually whereas New Mexico’s rate increased 4.3 percent on average annually. All three states saw more rapid growth between 2012 and 2015, ranging from an annual average increase in Colorado of 7.5 percent up to an annual average of 9.8 percent growth in Utah. The Film Office does not attempt to determine whether any of its activities impact the number of motion picture and video businesses operating in Colorado.



TOTAL MOTION PICTURE AND VIDEO INDUSTRY ESTABLISHMENTS CALENDAR YEARS 2006 THROUGH 2015



SOURCE: Office of the State Auditor’s analysis of Bureau of Labor Statistics data for Quarterly Census of Employment and Wages data.

¹ Establishments were listed under BLS Motion Picture and Video Industries, NAICS Code 5121.

Another source of information on production activity in the state may be the 10 film commissions that operate within local governments. The commissions are typically in contact with any production companies working in their area, regardless of whether the companies have sought an incentive through the Film Office. However, the Film Office does not collect and analyze information on production activities from the film commissions to gain a broader understanding of production activities

around the state. While these commissions are not required to keep any specific data on production activity, we surveyed all 10 commissions and three of the four that responded noted that there has been an increase in production activities in their areas over the last 5 years. It is likely that most of the information provided by the commissions would be anecdotal; however data on industry activities is not easy to find, so any information would help the Film Office better determine the effectiveness of the incentive program.

WHY DO THESE PROBLEMS MATTER?

When information collected and reported on the outcomes of the Film Office's activities is incomplete or inaccurate, the public and policymakers cannot rely on the information to fully understand the overall impact of the Film Office in relation to its costs to the State. As the charts above show, there has been growth in Colorado's industry over the past 10 years, but the Film Office is not evaluating whether its activities are contributing to any of the growth and is not fully informing the public or policy makers about the total benefits of its operations.

In addition, the Film Office needs to have complete and accurate data on the in-state expenditures, income tax revenue, and FTE jobs created through its activities to be able to strategically use its limited funds to have the greatest economic impact, which is one of its goals. Without this information, the Film Office and the Economic Development Commission may not select the most advantageous projects to incentivize, and therefore not maximize the benefit derived from the incentive program. Similarly, if the Film Office collected and used more detailed data on the cost and economic benefit of its marketing and educational activities, it would be able to make strategic decisions to leverage its resources for these activities towards outreach in industries that have the greatest economic impact. The Film Office's activities outside of the incentive program, such as education panels, industry networking and festivals, and support towards student productions, tend to focus on film creation, but the Film Office does not have data to evaluate if this focus helps the State attract the productions that

provide the most economic development or greatest return on investment.

Analyzing and reporting overall information on growth in the industry in Colorado and how it compares to other states could also help the Film Office and policymakers determine whether changes in the Film Office's activities are needed to maximize their impact. For example, as shown in EXHIBITS 2.7 and 2.8 above, the number of individuals employed and the number of businesses in the film industry appear to have increased since Fiscal Year 2013 when the incentive was doubled, which may indicate the higher incentive is encouraging growth in the industry. However, it is important for a variety of information to be considered in evaluating the effectiveness of the program and making decisions about how to use limited incentive funds going forward.

The Film Office's funding for the incentive program is subject to an annual appropriation by the General Assembly. Between Fiscal Years 2013 and 2017, the Film Office requested a total of \$19 million for the incentive program (roughly \$4 million each year), citing the program's success in promoting industry growth and the need to turn away major productions due to a lack of funds. The Film Office received appropriations over this period of \$15 million, or 21 percent less than requested. Due to the data inaccuracies and lack of comprehensive measurements, as discussed above, the Film Office does not have complete or accurate information that the Joint Budget Committee can rely on to make a decision about whether the Film Office's requests for funding are warranted.

RECOMMENDATION 6

The Office of Economic Development and International Trade should implement policies and procedures to expand its data collection and reporting on the benefits the State receives from the incentive program by:

- A Collecting and reporting on FTE jobs created by incentivized projects. This could involve either requiring the reporting of days or hours worked by each Colorado resident on each incentivized project so that the Office of Film, Television, and Media can calculate the FTE, or requiring production companies to calculate and report the FTE for their incentivized projects using a formula determined by the Office of Film, Television, and Media.
- B Expanding the information it collects on each incentivized project to include detailed data on the amount of income tax withheld for employees and compiling, analyzing, and reporting the data as part of the benefits of the Office of Film, Television, and Media.
- C Including statewide industry data in evaluating and reporting about the Office of Film, Television, and Media's activities and comparing the Office of Film, Television, and Media's information when possible with statewide data. For example, this should include collecting, analyzing, and reporting the total number of productions each year, and the number of film industry jobs in Colorado each year along with the FTE jobs created through the Office of Film, Television, and Media's activities.

RESPONSE

OFFICE OF ECONOMIC DEVELOPMENT AND INTERNATIONAL TRADE

A AGREE. IMPLEMENTATION DATE: SEPTEMBER 2017.

The Office of Economic Development and International Trade will hire a program analyst to collect, assess, and report additional data including hours worked, FTE jobs, income tax withholdings, number and impact of productions, statewide industry data, and other relevant information.

B AGREE. IMPLEMENTATION DATE: SEPTEMBER 2017.

The Office of Economic Development and International Trade will hire a program analyst to collect, assess, and report additional data including hours worked, FTE jobs, income tax withholdings, number and impact of productions, statewide industry data, or other relevant information.

C AGREE. IMPLEMENTATION DATE: SEPTEMBER 2017.

The Office of Economic Development and International Trade will hire a program analyst to collect, assess, and report additional data including hours worked, FTE jobs, income tax withholdings, number and impact of productions, statewide industry data, and other relevant information.

APPENDIX A





**INCENTIVES PAID
JULY 1, 2012, TO MARCH 31, 2017**

FISCAL YEAR	PRODUCTION COMPANY	PROJECT TITLE	TYPE OF PRODUCTION	INCENTIVE AMOUNT
2013	Gartner/Block Carter	Coors	Commercial	\$67,500
2014	Clean Guys Entertainment	Clean Guys Comedy	Television Show	\$28,000
	Detour Films	Coors	Commercial	\$66,900
	FF5 Productions	Fast and the Furious 5	Film	\$700,000
	High Noon Entertainment	Prospectors Season 1	Television Show	\$345,100
	Nine Nights	Dear Eleanor	Film	\$395,100
	Rocky Mountain PBS	Colorado Experience, Season 1	Television Show/Documentary	\$53,700
	The Frame	The Frame	Film	\$63,800
	World Championship Sports (Universal Sports)	Relocation Agreement	Television Show	\$307,300
TOTAL:				\$1,959,900
2015	Being Evel	Being Evel	Film	\$94,300
	Christmastime	Christmastime–Heaven Sent	Film	\$516,600
	Discovery Communications	Catch and Release and Pawn in the Game	Television Show	\$452,200
	High Noon Entertainment	Prospectors Season 3	Television Show	\$546,600
	Hyundai Motor America	Hyundai Running Footage	Commercial	\$101,200
	Rocky Mountain PBS	Colorado Experience, Season 2	Television Show/Documentary	\$20,700
	Impossible Pictures/Visual Approach	Moneygram	Commercial	\$20,100
	Cop Car	Cop Car	Film	\$82,000
	Universal Sports	Countdown to Sochi, Podium 360, Rugby Rising	Television Show	\$99,700
	TOTAL:			
2016	Being Evel	Verizon/Samsung	Commercial	\$20,900
	Calvary, Inc.	Coors	Commercial	\$57,000
	Cine-Manic Productions	Hateful 8	Film	\$5,000,000
	Cloud Imperium Games	Star Citizen	Video Game	\$763,900
	Colorado Public Television	Colorado Inside Out	Television Show/Documentary	\$22,100
	Great Divide Pictures	Heart of the World: Colorado's National Parks	Documentary	\$75,400
	High Noon Entertainment	Prospectors Season 4	Television Show	\$250,000
	Intrepid Adventures ¹	Hondros	Documentary	\$20,300
	James Havey Productions	The Great Divide	Documentary	\$70,100
	Listen Productions	Casting Jon Benet	Film	\$50,000
	Orion Entertainment	Ultimate Sportsman's Lodge	Television Show	\$156,500
	Walk the Line Films	Play Along!	Television Show	\$148,000
	Universal Sports	2015 Alpine World Championships, Podium 360	Television Show	\$27,200
	TOTAL:			

2017	72 and Sunny	Coors	Commercial	\$51,500
	Intrepid Adventures	Hondros	Documentary	\$27,300
	Addie and Louis Productions	Our Souls at Night	Film	\$1,500,000
	Amateur 5	Amateur	Film	\$293,400
	Canyon Entertainment	The Joey Canyon Show	Television Show	\$75,100
	Contrast Audio Visual	Max Lucado–Traveling Light	Television Show	\$29,100
	Don't Pose Productions	Star Raiders	Film	\$41,000
	Ease Commercial Services	Toyota Rav 4	Commercial	\$111,700
	Project Gnaw	Gnaw	Film	\$58,200
	Hoax	Hoax	Film	\$160,000
	James Havey Productions	Colorado Fuel and Iron	Documentary	\$39,200
	Janicek Entertainment	Xfinity Latino Entertainment	Television Show	\$148,700
	Lifted Life	The Lifted Life	Television Show	\$39,300
	Rocky Mountain PBS	Standing in the Gap	Television Show/Documentary	\$24,900
	SIV	Shooting in Vein	Film	\$34,100
	Walden the Movie	Walden: Life in the Woods	Film	\$177,100
	TOTAL:			\$2,810,600
	TOTAL:	46		\$13,432,800

SOURCE: Office of the State Auditor analysis of CORE data of paid incentives between July 1, 2012, and March 31, 2017.

¹This film was paid in two separate installments, the first for \$20,300 in Fiscal Year 2016 and the second for \$27,300 in Fiscal Year 2017 for a total of \$47,600.

