



STATE BOARD OF EQUALIZATION

August 30, 1965

Gentlemen:

Reference is made to your letter of August 9, 1965 regarding our progress in clarifying the animated motion picture question and the suggested changes submitted by the above-referenced association.

Coincidentally, your letter arrived only a few days before we met on a scheduled conference to go over the question. Therefore, I held off writing you until after the conference.

The conference concluded with an agreement that no changes would be made to bulletin 61-4 and no new bulletin would be issued at the present time. We do not feel it is necessary for several reasons.

In the first place, it is our conclusion that a literal interpretation of the annotation appearing in Cal. Tax Service at pages 3509 and 3510, and which describes six steps in the process of producing an animated film, has resulted in a departure from provisions of Ruling 19 and bulletin 61-4 to say nothing of creating the confusion that presently exists. The annotation was written long before the bulletin was adopted, and if a strict literal application of the annotation was intended it would have been included in the bulletin.

As we see the problem and understand how it arises, an animation studio is automatically precluded from being found to be a producer of an animated film merely because it did not produce the "storyboard" (step No.1) even though, for example, the studio did all of the remaining five steps. This approach or test has apparently been used in recent audits of animated film studios, and where the studio subcontracted to have a storyboard produced or where an advertising agency furnished one, the animation studio producing the film has been precluded from being the producer of the film.

We think this approach or test is wrong because it tends to, and almost always does, result in a departure from the provisions of bulletin 61-4, which defines a producer as the person who is responsible for and in general charge of making a production, either for himself or for his principal. Thus, if an animation studio is responsible for making the picture and is in general charge of the job, it should not matter how the storyboard was developed, whether it was subcontracted or given to the studio by the principal, since in either case the studio could still be the one responsible for and in general charge of making the production (meaning turning out the finished film for the client or principal, including an ad agency contracting with the studio to do the entire job).

Conceivably no one could be the producer of a film if an ad agency entered into six separate contracts with six different studios for the six steps. To this extent no one would be the producer, but the ad agency would be the consumer of each step ordered. In effect, this is saying the ad agency (who did nothing) was the producer, since under the ruling the producer is the consumer. This is most improbable, but I think it serves to illustrate how there has been a departure from the definition of a producer when so much weight is placed on one simple step, such as the creation of the storyboard.

We understand that another problem area arises when an ad agency contracts with an animation studio to produce a film and furnishes a 1/4" tape with some sounds to be used when the sound track is fabricated (dub-in sound). We understand that the position has been taken that the mere furnishing of the tape precludes the studio from being the producer on the theory that since the tape was furnished the studio, the studio did not perform all six steps. (Step No.6 is dub-in sound.)

This also we find to be a departure from bulletin 61-4. In the first place, furnishing the tape is not dubbing in the sound, and we do not think it should preclude a studio from being found to be the one responsible and in general charge of making the film. In fact, we think an animation studio could subcontract the sound work and still be the producer of the film. However, where this is done, the sound studio doing the dubbing and mixing would be liable for tax on its charges to the animation studio producing the film. This is what bulletin 61-4 provides.

We also understand that there has been a tendency to treat fully animated films (that contain no live action shots) as something other than motion pictures. This, we think, is wrong because Ruling 19 and bulletin 61-4 do not distinguish between animation, live action or any combination thereof.

Our conclusion, therefore, is to disregard the application of the so-called six step test when looking to see who was the producer of an animated film, and instead, strictly adhere to the provisions of bulletin 61-4 and Ruling 19.

With respect to the Association's proposed interpretation of Ruling 19 and bulletin 61-4, we went over it carefully and reached the following conclusions:

Paragraph (a): This seems to be a restatement of provisions already found in bulletin 61-4 and 64-5. We are not going to treat "complete" television commercials any different from any other complete motion picture, regardless of whether they are entirely animated, partially animated, or all live action.

CAVEAT: An animation studio might do only the animation work on a commercial that contains live action as well, and be only responsible for the animation which is, as to the entire production, an incomplete segment. In such a circumstance, the animation studio would not be considered as having produced a complete production within the meaning of bulletin 61-4 since the animation portion, standing alone, is not complete as far as the finished film is concerned. Thus, even though the studio produced the animation it would not be the consumer, and tax would apply to charges for the animation work the same as other studios would charge tax on sales of films consisting of "stock shots", "inserts", "titles", etc., produced independently of the picture, by someone other than the producer of the picture. In such a situation the animation studio would be a subcontractor.

Paragraph (b): We agree that the source of the audio or visual content of a film should not be solely determinative when looking to see who produced the film. If the source is from an independent contractor under a subcontract, the producer of the finished film would still be the consumer of the segments he might subcontract to have done. It is our opinion that this section is not necessary when we properly apply the provisions of bulletin 61-4. If an animation studio has to subcontract some work, and if the animation studio is the one responsible for and in general charge of making the finished complete production, it will be the consumer of the the subcontracted work and the subcontractor will be liable for tax (if any) on the work performed.

Paragraph (c) (1): This is a radical departure from provisions of bulletin 61-4 and has the effect of making every subcontractor a subproducer. It is contrary to the present definition of a subproducer and coproducer, which we do not contemplate or recommend redefining. It makes everyone the producer-consumer no matter how little or how much he does so long as he is responsible for what he does. It is just as much a departure from the bulletin provisions as holding that an animated film is not a motion picture.

Paragraph (c) (2): This is also a radical departure from the bulletin and the definition of a coproducer. It is, in a sense, another way of saying what was said in (c) (1) above. It says, in effect, that if a person contracts to produce the titles and credits for a film under a contract for a fixed fee, he is the coproducer.

Summarily, we do not think paragraphs (a) and (b) are necessary under the present provisions of bulletin 61-4, and we reject paragraphs (c) (1) and (c) (2) entirely.

From the foregoing conclusions we are going to recommend a reaudit of the pending petitions, as we are sure that there will be some adjustments in order, particularly where audit procedure has been to follow a strict or literal test based on the application of the aforementioned anno containing the six steps in animation production.

It is our opinion that this, then, will put everyone back on the track of following bulletin 61-4, which we have had with us since 1961 and which we conclude should not be expanded or contracted at this time.

Robert H. Anderson
Associate Tax Counsel

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