

California Film & Television Tax Credit Program
AGREED UPON PROCEDURES
Oct. 20, 2010

I. Introduction

The California Film & Television Tax Credit Program provides tax credits for qualified expenditures incurred when producing qualified motion pictures. The tax credits can be used to offset either California personal or corporate income taxes or sales and use taxes. A production company requesting a tax credit must submit an Independent Certified Public Accountant's Report on Applying Agreed-Upon Procedures (the 'Report') to demonstrate compliance with the program's requirements.

II. Statutory References

California Revenue and Taxation Code Sections:

1. 6902.5 (sales and use tax)
2. 17053.85 (personal income tax)
3. 23685 (corporate income tax)
4. California Code of Regulations, Title 10, Chapter 7.75, Sections 5500-5507

III. General

The following Agreed Upon Procedures (AUP) are to be performed by a certified public accountant (CPA) with an active California license to perform attest services. The CPA cannot provide production accounting services and agreed upon procedures services to the same production company as per Rule 101 of the American Institute of Certified Public Accountants Code of Professional Conduct and its interpretations and rulings.

The selected CPA must have sufficient knowledge of accounting principles and practices generally recognized in the film and television production industry. The CPA shall read the statute, regulations, guidelines, Qualified Expenditure Charts, Tracking Tips, and all other materials posted on the California Film Commission (~~CFC~~) website.

1. The Report shall be prepared for the use of the following specified parties:
 - a. The production company; and
 - b. The California Film Commission
2. ~~The CPA's name, address, telephone number, The Report should include the California CPA license number or a copy of his or her the practice privilege permit number for the person and/or firm practicing assurance services.~~
3. The name of the production and its Credit Allocation Number must also appear on the Report.
4. The Report must be dated as of the last day of the performance of all procedures.

5. The production company's cost report must be presented in U.S. dollars.
6. The production company must provide documentation of all funds expended on the production including pre-production, production and post-production periods.
7. Please include CPA name and contact information for the CPA responsible for the review and final sign off of this Report.

IV. Agreed-Upon Procedures

The CPA shall perform the following procedures. Any exceptions are to be listed as a finding in the CPA's report on applying agreed-upon procedures utilizing Appendix B.

Eligibility:

1. Obtain the detailed cost ledger (e.g. Bible) of California Qualified Expenditures and Total Production Expenditures.
- 2- Obtain from the California Film Commission and read the production company's tax credit application with supporting documentation, including the following: Application Form (CFC Form A), Qualified Expenditure Budget and Production Budget. ~~and Independent Film Declaration (CFC Form C), if applicable.~~
3. Obtain and read the production company's Credit Allocation Letter.
4. Obtain and inspect post-production documents (e.g. facility invoices) evidencing the date the final elements (e.g., final composite answer print, air master, or digital cinema files) were created. Determine and document in the Report the Qualification Period of the production. Confirm that the Qualified Production Period does not exceed 30 months after the date in which the California Film Commission issued the Credit Allocation Letter.
5. Obtain and inspect documentation (e.g. call sheets and/or production reports, shooting schedules) for all principal photography days for the production during the Qualified Production Period in order to determine if production met the 75% principal photography day test. Based upon the inspection of the documentation, state the percentage of total principal photography days which occurred wholly in California. (The total principal photography days in California ratio can be obtained by dividing the number of days of principal photography in California by the total number of principal photography days).
6. If the production does not meet the 75% principal photography day test in Section 5 above, perform the following procedures:
 - a. Obtain a detailed cost ledger of Total California Expenditures (including qualified and non-qualified expenditures) and the Total Production Budget. State the ratio of Total California Expenditures to the Total Production Budget.
 - b. Select a sample of expenditures from the Total California Expenditure population (including qualified and non-qualified expenditures) according to the sampling methodology noted in Appendix A.
 - c. For each expenditure item selected, obtain and inspect invoices and cancelled checks or other equivalent documentation. Confirm that the expenditure amount is correct, agrees to the invoice, was incurred and paid for services and goods in California.
7. Inspect the detailed cost ledger of Total Production Expenditures to determine that the Total Production Expenditures met the maximum and minimum thresholds for Feature Films, Movies

of the Week, Miniseries, and Television Series per the statute. For Independent films, determine if the Total Production Expenditure met the minimum threshold and the total Qualified Expenditures met the maximum threshold per the statute and regulations.

- a. If applicable, determine if the completion bond fees were omitted from the Total Production Expenditures or Qualified Expenditure total (for Independent productions only) to meet maximum thresholds noted above. If so, confirm that the completion bond fees were excluded from California Qualified Expenditures.
 - b. If applicable, determine if litigation or insurance claims are causing a production to exceed its Total Production Expenditure maximum threshold. If so, inspect any litigation or insurance documentation for appropriateness and remove these costs in determining the Total Production Expenditures.
8. If the production has not met eligibility standards as noted above, there is no need to continue with the agreed upon procedures. Notify production company management to inform the CFC that they are ineligible for the tax credit program.

Expenditures (other than payroll):

1. Select a sample of expenditures (other than payroll) from the detailed cost ledger according to the sampling methodology noted in Appendix A.
2. For each expenditure item selected in the sample perform the following procedures:
 - a. Inspect invoices and cancelled checks or other equivalent documentation. Confirm that expenditure amount is correct, incurred and paid for services and goods in California.
 - b. Confirm that the expenditure was not associated with activities specifically excluded by the statute.
 - c. Confirm that the expenditure was allowable as defined by statute. In particular, inspect travel costs, living allowances and per diems.
 - d. Confirm that the expenditure was not for in-kind services.
 - e. Confirm that the expenditure was recorded net of any refunds (not applicable to insurance claims), credit notes received for discounts, rebates, invoicing errors, and purchase returns, as recorded in the cost report and that completion bond expenditures are reported net after rebate.
 - f. Confirm that the expenditure was recorded net of proceeds from any sale of the production assets.
 - g. Confirm that the expenditure was not incurred prior to the date in which the Credit Allocation Letter (CAL) was issued. For qualified items which required full or partial payment, such as insurance premiums or office rent, made prior to the issuance of the CAL, confirm that these costs are pro-rated by the number of pre-production, production and post-production weeks and that only the pro-rated costs after the CAL date are included in California Qualified Expenditures.
 - h. Confirm that expenditure was not incurred more than 30 days after creation of the final elements.
 - i. Confirm that the expenditure is pro-rated to reflect any usage out of the state.

- j. Confirm that insurance deductible(s), if any, was not included in qualified expenditures.
3. Obtain ~~a~~ fixed asset listings from the production company of all assets used in the production ~~with a~~ as follows: (1) all office, post-production, digital and effects equipment; and (2) all other assets not considered office, post-production and effects equipment with an original purchase price over \$10,000. The listings should indicate the status of the assets (e.g. destroyed, sold, donated, being held for future productions, given to cast or crew, etc.). A copy of ~~the~~ both listings should be attached to the Report. For all assets on the listings perform the following procedures:
- a. For all office, post-production or effects equipment (including but not limited to computers, hardware and relevant components, printers, copiers, etc.), confirm that the California Qualified Expenditure is the lesser of the net costs of the asset after sales proceeds (if assets sold) or 20% of the original cost.~~s of office, post-production, or effects equipment, including but not limited to computers, hardware and relevant components, printers and copiers.~~
 - b. For all other assets over \$10,000, confirm the following: (1) If the asset is sold, confirm that the California Qualified Expenditure is the lesser of the net costs of the asset after sales proceeds or 50% of the original cost of such asset; (2) If the asset is retained, confirm that the California Qualified Expenditure is 50% of the original cost of such asset; (3) If the asset is destroyed during the process of production, confirm that the production company maintains documentation to support the destruction of the asset (e.g. call sheets, production reports, still photographs, video footage, etc.); and (4) If the asset is given to a non-qualifying above-the-line (ATL) cast or crew member or sold to a non-qualifying ATL cast or crew member for less than 50% of original purchase price, confirm that the cost of such asset is not included in the California Qualified Expenditures.
 - c. For exceptions noted in procedures (a) and (b) above, adjust the Qualified California Production Expenditures for known errors noted. Confirm that no assets purchased as part of a compensation package for above-the-line personnel are included as a California Qualified Expenditure.
4. Obtain a listing of customized leased or rented items which are manufactured, assembled, or fabricated to specification with lease payments aggregating \$10,000 or more. Confirm that these items are included on the asset listing noted above (expenditure, procedure 3) if they meet any one of the following four conditions:
- a. If the term of the lease exceeds 75% of the life of the asset;
 - b. If there is a transfer of ownership to the lessee at the end of the lease term;
 - c. If there is an option to purchase the asset for substantially less than fair market value ("bargain price") at the end of the lease term;
 - d. If the present value of the lease payments, discounted at an appropriate discount rate, exceeds 90% of the fair market value of the asset.
- Any such rental or lease agreement that meets the above standards for a capital lease will be considered a purchase and subject to the 50% limitation for purposes of determining California Qualified Expenditures.
5. Obtain a list from the production company of any and all visual effects, digital effects, post production sound and/or title companies who worked on the production. Confirm that all listed parties have provided the production company with documentation indicating the total dollar amount of work performed within the state and verify that only the amount of work performed within the state of California is included in the California Qualified Expenditures total.

6. For exceptions noted in the expenditure test in procedure 2 above (not including payroll), for the sample identified in the Top Stratum of Appendix A, adjust the Qualified California Production Expenditures to reflect the results of for known errors noted during your testing.

7. For exceptions noted in the expenditures test in procedure 2 above (not including payroll), for the sample identified in the Stratum 1 and Stratum 2 in Appendix A, adjust the Qualified California Production Expenditures for known errors noted during your testing and project the misstatement results of the sample to all items from which the sample was selected. For purposes of calculating the projected misstatement, divide the monetary amount of misstatement of the exceptions identified by the sample population total amount (rate of misstatement). Multiply this rate of misstatement to the total expenditure population from which the Stratum 1 and Stratum 2 sample was selected. Perform the following procedures based upon the results of the calculation of the projected misstatement:
 - a. If the projected misstatement does not exceed 2% of Qualified California Production Expenditures, document the projected misstatement in the Report. Do not make any adjustment to the California Production Expenditures for a projected misstatement.

 - b. If the projected misstatement exceeds 2% of Qualified California Production Expenditures, select a second additional sample according to the sampling methodology noted in Appendix A for Stratum 1 and Stratum 2. Recalculate the projected misstatement for the second additional sample. If the projected misstatement for the second additional sample does not exceed 2%, document the projected misstatement in the Report. ~~and Do not make an adjustments~~ adjustment to the California Qualified Expenditures for a projected misstatement; however, do adjust the California Qualified Expenditures for noted known errors in this second sample. If the projected misstatement from the second sample selection exceeds 2% of Qualified California Production Expenditures, adjust the Qualified California Expenditures for the average of the two projected misstatements.

 - c. Attach a listing of any exceptions noted in the expenditure test in procedures 2 and 7(b) above (other than payroll). The listing should include amount, vendor/person, and nature of discrepancy.

Payroll:

1. Obtain detailed payroll reports by employee ~~and work state (e.g. an earning register by employee by work state)~~ for those individuals that are included in Qualified Wages. Compare and ~~agree~~ reconcile the detailed payroll reports ~~for earnings in California to the cost ledger of "qualified wages".~~ with the Qualified Wages in the Bible on a sum total basis. Understand all variances between the Bible and the detailed payroll report. Unexplained variances should total no more than \$25,000. For unexplained variances which total over \$25,000 in the aggregate, re-reconcile to no more than \$25,000 or remove unexplained variances from Qualified Expenditures.

2. Select a sample of employees from the ~~detailed payroll reports for~~ Qualified Wages account in the Bible according to sampling methodology noted in Appendix A. For each employee selected in the sample perform the following procedures:
 - a. Reconcile the amount of the Qualified Wages in the Bible for the individual with the payroll report.

 - b. Inspect time cards, production reports, call sheets or other equivalent documentation. Confirm that wage amount is incurred for services performed in California.

- c. Inspect invoices from “qualified entities”. Confirm the date the expenditure was incurred, and that the loan out company name and the amount of the expenditure agrees with supporting payroll records. Confirm that the expenditure was incurred in California.
 - d. Confirm that the “qualified wages” only include those expenses listed in Revenue and Taxation Code Section 17053.85(b)(18)(A)(i)-(iv) or Section 23685(b)(18)(A)(i)-(iv) and do not include any of the expenses listed in Section 17053.85(b)(18)(B)(i)-(iv) or Section 23685 (b)(18)(B) (i)-(iv).
 - e. Confirm that only “qualified individuals” as defined in Revenue and Taxation Code Section 17053.85(b)(14) or 23685(b)(14), received “qualified wages”.
 - f. Confirm that all Qualified Wages do not include compensation for any work incurred out of the state.
 - g. Confirm that all Qualified Wages were not incurred prior to the date of the Credit Allocation letter.
 - h. Confirm that all Qualified Wages were not incurred more than 30 days after the creation of the final elements.
3. Obtain the final “galley” or checker” of the main (if applicable) and end title credits for the production. ~~Confirm the qualified wages paid to any individuals who also are receiving an on screen producer~~ For those below the line individuals (e.g., Unit Production Managers, Production Supervisors, First Assistant Directors, Post Production Supervisors, Visual Effects Supervisors) who also are receiving an on screen producer (e.g. executive, line, co-, associate, visual effects, music, post) credit, ~~are considered by the CFC to be within industry standard wage scales or equivalent with other crew in similar positions~~, confirm that qualified wages only include: up to \$100,000 in DGA wages; industry standard wages; or wages equivalent with other crew in similar positions. For those receiving both above the line and below the line credits, please note in the Report the names and qualified compensation for each individual for each end title credit received.
 4. For exceptions noted in the payroll test in procedure 2 above, for the sample identified in the Top Stratum of Appendix A, adjust the Qualified California Production Expenditures ~~to reflect the results of~~ for known errors noted during your testing.
 5. For exceptions noted in the payroll test in procedure 2 above, for the sample identified in Stratum 1 in Appendix A, adjust the Qualified California Production Expenditures for known errors noted during your testing and project the misstatement results of the sample to all items from which the sample was selected. For purposes of calculating the projected misstatement, divide the monetary amount of misstatement of the exceptions identified by the sample population total amount (rate of misstatement). Multiply this rate of misstatement to the total expenditure population from which the Stratum 1 sample was selected. Perform the following procedures based upon the results of the calculation of the projected misstatement:
 - a. If the projected misstatement does not exceed 2% of Qualified California Production Expenditures, document the projected misstatement in the Report. Do not make adjustments to the California Production Expenditures for the projected misstatement.
 - b. If the projected misstatement exceeds 2% of Qualified California Production Expenditures, select a second additional sample according to the sampling methodology noted in Appendix A for Stratum 1. Recalculate the projected misstatement for the second additional sample. If the projected misstatement for the second additional sample does not exceed 2%, document the projected misstatement in the Report. ~~and Do~~

not make adjustments to the California Production Expenditures for a projected misstatement; however, do adjust the California Qualified Expenditures for noted known errors in this second sample. If the projected misstatement from the second sample selection exceeds 2% of Qualified California Production Expenditures, adjust the Qualified California Expenditures for the average of the two projected misstatements.

- c. Attach a listing of any exceptions noted in the payroll test in procedures 2 and 5(b) above. The listing should include amount, person or entity, and nature of discrepancy.

Related Parties & Other Affiliations:

1. Obtain from the production company a schedule listing of all related party transactions (including parties with a 5% or greater ownership in or affiliation with the production company) for which the production company is including the transactions in the California Qualified Expenditures. The listing should note the type of relationship between the related party and the production company and the nature and amount of the transactions.
 - a. ~~All Related Parties~~
 - b. ~~Type of Relationship between the related party and the production company.~~
 - c. ~~All transactions between the production company and the related party.~~
 - d. ~~Nature and amount of the transaction(s).~~
 - e. ~~A listing of all parties with a 5% or greater ownership in or other affiliation with the production company.~~
 1. ~~Document in the Agreed Upon Procedures Report the name, relationship, nature of transactions and amounts of transactions for all related parties and owners noted in schedule above.~~
2. Obtain a signed letter from a production company representative stating that the applicant (indicated in the Credit Allocation Letter) has properly disclosed all related parties and related party transactions and that the schedules produced in accordance with item number 1 above are complete and accurate.
3. From the schedule in item number 1, select a sample of related party transactions for testing. Select all transactions greater than \$25,000. For the transactions less than \$25,000, randomly select 15 transactions for testing.
4. ~~Compare the list of related parties and owners to the detailed cost report, noting wages and expenditures paid to individuals and entities that are related parties. Perform the following procedures for each related party transaction selection:~~
 1. For wages paid to related parties, confirm that no amounts are included in the California Qualified Expenditures.
 2. For non-payroll expenditures, inspect documentation to confirm that all related party transactions are made in accordance with an arm's length standard by inspecting comparison bids or studio rate cards. Whether transactions exhibit arm's length characteristics generally will be determined by reference to the results of comparable transactions under comparable circumstances.
5. For all transactions deemed to not be at arms length standard, from procedure 4, note the nature, description and amount in the report and deduct these transactions from the Qualified Expenditure Total.
6. Attach a listing of all related party transactions obtained in procedure #1.

Wrap Up Procedures

1. If applicable, recalculate the 75% spend test (e.g. eligibility procedure number 6) after accounting records are revised for findings in payroll and expenditure procedures. Confirm that 75% of the Total Production Budget was spent for California Qualified Expenditures.
2. Provide the following data requested on Exhibit A which agrees with the cost report utilized by the CPA for the procedures above, as adjusted for the exceptions noted above:
 - a. Qualified Wages & Fringes - excluding post-production
 - b. Qualified Non-wage Spend - excluding post-production
 - c. Total Qualified Expenditures – excluding post-production
 - d. Qualified Wages & Fringes – post-production
 - e. Qualified Non-wage Spend – post-production
 - f. Total Qualified Expenditures – post-production only
 - g. Total Tax Credit Allocation Due
3. The CPA must include the information requested above (wrap procedures, procedure 2) in the Report utilizing the format in “Exhibit A”.
4. The CPA must indicate on the Report that the specific program minimum and maximum thresholds as applicable to the type of production have been met.

EXHIBIT A

QUALIFIED EXPENDITURES:	
E: Qualified Wages & Fringes (excluding post): <hr style="width: 80%; margin: 5px 0;"/>	E2: Qualified Wages & Fringes - Post-Production only: <hr style="width: 80%; margin: 5px 0;"/>
F: Qualified (Non-Wage) Spend (excluding post): <hr style="width: 80%; margin: 5px 0;"/>	F2: Qualified (Non-Wage) Spend Post-Production only: <hr style="width: 80%; margin: 5px 0;"/>
* G: Total Qualified Expenditures (E+F) (excluding post): <hr style="width: 80%; margin: 5px 0;"/>	* G2: Total Qualified Expenditures Post-Production only (E2+F2) : <hr style="width: 80%; margin: 5px 0;"/>
* Tax Credit Allocation Due (G+G2): <div style="display: flex; align-items: center; justify-content: space-between; margin-top: 10px;"> <div style="flex: 1;"> <hr style="width: 80%; margin: 0;"/> </div> <div style="text-align: center; flex: 0.2;"> x </div> <div style="text-align: center; flex: 1;"> <hr style="width: 80%; margin: 0;"/> <div style="font-size: small; margin: 2px 0;">Eligible Tax Credit</div> <div style="background-color: yellow; padding: 2px; font-size: x-small;">Enter .20 or .25</div> </div> <div style="text-align: center; flex: 0.1;"> = </div> <div style="flex: 1;"> <hr style="width: 80%; margin: 0;"/> </div> </div>	
Credit Allocation Letter Amount: <hr style="width: 80%; margin: 0 auto;"/>	

* FINAL CREDIT AMOUNT (whichever is less): <hr style="width: 80%; margin: 0 auto;"/>

* Automatic calculations are programmed in the form.

Appendix A

California Film & Television Tax Credit Program
 Sampling Chart
 Feature Films/Movies of the Week/Miniseries
 Television Series*

	Payroll		Non-Payroll*		
	Top Stratum	Stratum 1	Top	Stratum 1	Stratum 2
Total Qualified Expenditures	Employees with total qualified wages in excess of \$100,000	Employees with total qualified wages under \$100,000	Items \$25,000 and over	Items under \$25,000 and over \$500	Items \$500 and less
0 - \$500,000	All Items	10	All Items	50	25
\$500,001 - \$1,000,000	All Items	20	All Items	50	25
\$1,000,001 - \$5,000,000	All Items	25	All Items	50	25
\$5,000,001 - \$10,000,000	All Items	25	All Items	60	25
\$10,000,001 - \$25,000,000	All Items	25	All Items	75	25
\$25,000,001 - 50,000,000	All Items	25	All Items	100	25
\$50,000,001 +	All Items	25	All Items	100	25

*For a Television Series, excluding payroll, the sampling should be based upon aggregating all episode and amortization costs together from a series for purposes of determining the total qualified expenditures above. Once a sample size is determined, the CPA must apportion the sampling size so as to sample at least one expenditure item from each episode, including amortization costs.

APPENDIX B
California Film & Television Tax Credit Program
Independent Accountants' Report
On Applying Agreed-Upon Procedures

Title of Production: _____ Credit Allocation #: _____

Contact Name: _____ Phone#: _____

Firm: _____

CPA reviewing/signing report: _____ License # _____ OR

CA Practice Privilege Permit Identifier # _____

To [Name of Company] and the California Film Commission:

We have performed the procedures enumerated below, which were agreed to by the [Name of Company] (the Company) and the California Film Commission (CFC), solely to assist you in evaluating the completeness and accuracy of the accompanying Schedule of Qualified California Production Expenditures (SQCPE) at Exhibit A for the motion picture entitled [Name of Motion Picture] (the MP). We followed these procedures to demonstrate compliance with the criteria specified by the CFC for qualifying SQCPE of the Company for the MP for the period beginning [Date] and ending [Date]. The Company's management is responsible for maintaining records of the information contained in the SQCPE for the MP. This agreed-upon procedures engagement was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants. The sufficiency of these procedures is solely the responsibility of those parties specified in this report. Consequently, we make no representation regarding the sufficiency of the procedures described below either for the purpose for which this report has been requested or for any other purpose.

Using information provided to us by the Company, we performed the following procedures and noted the following findings:

Eligibility:

1. Obtain the detailed cost ledger (e.g. Bible) of California Qualified Expenditures and Total Production Expenditures.

[Note results and any details of exceptions noted]

2. Obtain from the California Film Commission and read the production company's tax credit application with supporting documentation, including the following: Application Form (CFC Form A), Qualified Expenditure Budget and Production Budget.

[Note results and any details of exceptions noted]

3. Obtain and read the production company's Credit Allocation Letter.

[Note results and any details of exceptions noted]

4. Obtain and inspect post-production documents (e.g. facility invoices) evidencing the date the final elements (e.g., final composite answer print, air master, or digital cinema files) were created. Determine and document in the Report the Qualification Period of the production. Confirm that the Qualified Production Period does not exceed 30 months after the date in which the California Film Commission issued the Credit Allocation Letter.

[The Qualification Period of the production is from {Date} to {Date}. This period does not exceed 30 months after the date in which the CFC issued the Credit Allocation Letter.] OR [Note details of any exceptions]

5. Obtain and inspect documentation (e.g. call sheets and/or production reports, shooting schedules) for all principal photography days for the production during the Qualified Production Period in order to determine if production met the 75% principal photography day test. Based upon the inspection of the documentation, state the percentage of total principal photography days which occurred wholly in California. (The total principal photography days in California ratio can be obtained by dividing the number of days of principal photography in California by the total number of principal photography days).

[The percentage of total principal photography days occurred wholly in California is {%.}]

6. If the production does not meet the 75% principal photography day test in Section 5 above, perform the following procedures:
 - a. Obtain a detailed cost ledger of Total California Expenditures (including qualified and non-qualified expenditures) and the Total Production Budget. State the ratio of Total California Expenditures to the Total Production Budget.

[The ratio of Total California Expenditures to the Total Production Budget is {%.}] OR [Not Applicable]

- b. Select a sample of expenditures from the Total California Expenditure population (including qualified and non-qualified expenditures) according to the sampling methodology noted in Appendix A.

[Note results and any details of exceptions noted] OR [Not Applicable]

- c. For each expenditure item selected, obtain and inspect invoices and cancelled checks or other equivalent documentation. Confirm that the expenditure amount agrees to the invoice, was incurred and paid for services and goods in California.

[Note results and any details of exceptions noted] OR [Not Applicable]

7. Inspect the detailed cost ledger of Total Production Expenditures to determine that the Total Production Expenditures met the maximum and minimum thresholds for Feature Films, Movies of the Week, Miniseries, and Television Series per the statute. For Independent films, determine if the Total Production Expenditure met the minimum threshold and the total Qualified Expenditures met the maximum threshold per the statute and regulations.

[Note results and any details of exceptions noted]

- a. If applicable, determine if the completion bond fees were omitted from the Total Production Expenditures or Qualified Expenditure total (for Independent productions only) to meet maximum thresholds noted above. If so, confirm that the completion bond fees were excluded from California Qualified Expenditures.

[Note results and any details of exceptions noted] OR [Not Applicable]

- b. If applicable, determine if litigation or insurance claims are causing a production to exceed its Total Production Expenditure maximum threshold. If so, inspect any litigation or insurance documentation for appropriateness and remove these costs in determining the Total Production Expenditures.

[Note results and any details of exceptions noted] OR [Not Applicable]

8. If the production has not met eligibility standards as noted above, there is no need to continue with the agreed upon procedures. Notify production company management to inform the CFC that they are ineligible for the tax credit program.

[Note results and any details of exceptions noted]

Expenditures (other than payroll):

1. Select a sample of expenditures (other than payroll) from the detailed cost ledger according to the sampling methodology noted in Appendix A.

[Note results and any details of exceptions noted]

2. For each expenditure item selected in the sample perform the following procedures:

- a. Inspect invoices and cancelled checks or other equivalent documentation. Confirm that expenditure amount is correct, incurred and paid for services and goods in California.

[Note results and any details of exceptions noted]

- b. Confirm that the expenditure was not associated with activities specifically excluded by the statute.

[Note results and any details of exceptions noted]

- c. Confirm that the expenditure was allowable as defined by statute. In particular, inspect travel costs, living allowances, box rentals, car allowances and per diems.

[Note results and any details of exceptions noted]

- d. Confirm that the expenditure was not for in-kind services.

[Note results and any details of exceptions noted]

- e. Confirm that the expenditure was recorded net of any refunds (not applicable to insurance claims), credit notes received for discounts, rebates, invoicing errors, and purchase returns, as recorded in the cost report and that completion bond expenditures are reported net after rebate.

[Note results and any details of exceptions noted]

- f. Confirm that the expenditure was recorded net of proceeds from any sale of the production assets.

[Note results and any details of exceptions noted]

- g. Confirm that the expenditure was not incurred prior to the date in which the Credit Allocation Letter (CAL) was issued. For qualified items which required full or partial payment, such as insurance premiums or office rent, made prior to the issuance of the CAL, confirm that these costs are pro-rated by the number of pre-production, production and post-production weeks and that only the pro-rated costs after the CAL date are included in California Qualified Expenditures.

[Note results and any details of exceptions noted]

- h. Confirm that expenditure was not incurred more than 30 days after creation of the final elements.

[Note results and any details of exceptions noted]

- i. Confirm that the expenditure is pro-rated to reflect any usage out of the state.

[Note results and any details of exceptions noted]

- j. Confirm that insurance deductible(s), if any, was not included in qualified expenditures.

[Note results and any details of exceptions noted]

- 3. Obtain fixed asset listings from the production company of all assets used in the production as follows: (1) all office, post-production, digital and effects equipment; and (2) all other assets not considered office, post-production and effects equipment with an original purchase price over \$10,000. The listings should indicate the status of the assets (e.g. destroyed, sold, donated, being held for future productions, given to cast or crew, etc.). A copy of both listings should be attached to the Report. For all assets on the listings perform the following procedures:

- a. For all office, post-production or effects equipment (including but not limited to computers, hardware and relevant components, printers, copiers, etc.), confirm that the California Qualified Expenditures is the lesser of the net costs of the asset after sales proceeds (if assets sold) or 20% of the original cost.

[Note results and any details of exceptions noted]

- b. For all assets over \$10,000, confirm the following: (1) If the asset is sold, confirm that the California Qualified Expenditure is the lesser of the net costs of the asset after sales

proceeds or 50% of the original cost of such asset; (2) If the asset is retained, confirm that the California Qualified Expenditure is 50% of the original cost of such asset; (3) If the asset is destroyed during the process of production, confirm that the production company maintains documentation to support the destruction of the asset (e.g. call sheets, production reports, still photographs, video footage, etc.); and (4) If the asset is given to a non-qualifying above-the-line (ATL) cast or crew member or sold to a non-qualifying ATL cast or crew member for less than 50% of original purchase price, confirm that the cost of such asset is not included in the California Qualified Expenditures.

[Note results and any details of exceptions noted]

- c. For exceptions noted in procedures (a) and (b) above, adjust the Qualified California Production Expenditures for known errors noted.

[Note results and any details of exceptions noted]

4. Obtain a listing of customized leased or rented items which are manufactured, assembled, or fabricated to specification with lease payments aggregating \$10,000 or more. Confirm that these items are included on the asset listing noted above (expenditure, procedure 3) if they meet any one of the following four conditions:
 - a. If the term of the lease exceeds 75% of the life of the asset;
 - b. If there is a transfer of ownership to the lessee at the end of the lease term;
 - c. If there is an option to purchase the asset for substantially less than fair market value ("bargain price") at the end of the lease term;
 - d. If the present value of the lease payments, discounted at an appropriate discount rate, exceeds 90% of the fair market value of the asset.

Any such rental or lease agreement that meets the above standards for a capital lease will be considered a purchase and subject to the 50% limitation for purposes of determining California Qualified Expenditures.

[Note results and any details of exceptions noted]

5. Obtain a list from the production company of any and all visual effects, digital effects, post production sound and/or title companies who worked on the production. Confirm that all listed parties have provided the production company with documentation indicating the total dollar amount of work performed within the state and verify that only the amount of work performed within the state of California is included in the California Qualified Expenditures total.

[Note results and any details of exceptions noted]

6. For exceptions noted in the expenditure test in procedure 2 above (not including payroll), for the sample identified in the Top Stratum of Appendix A, adjust the Qualified California Production Expenditures for known errors noted during your testing.

[Note results and any details of exceptions noted]

7. For exceptions noted in the expenditures test in procedure 2 above (not including payroll), for the sample identified in the Stratum 1 and Stratum 2 in Appendix A, adjust the Qualified California Production Expenditures for known errors noted during your testing and project the

misstatement results of the sample to all items from which the sample was selected. For purposes of calculating the projected misstatement, divide the monetary amount of misstatement of the exceptions identified by the sample population total amount (rate of misstatement). Multiply this rate of misstatement to the total expenditure population from which the Stratum 1 and Stratum 2 sample was selected. Perform the following procedures based upon the results of the calculation of the projected misstatement:

- a. If the projected misstatement does not exceed 2% of Qualified California Production Expenditures, document the projected misstatement in the Report. Do not make any adjustment to the California Production Expenditures for a projected misstatement.

[Note results and any details of exceptions noted]

- b. If the projected misstatement exceeds 2% of Qualified California Production Expenditures, select a second additional sample according to the sampling methodology noted in Appendix A for Stratum 1 and Stratum 2. Recalculate the projected misstatement for the second additional sample. If the projected misstatement for the second additional sample does not exceed 2%, document the projected misstatement in the Report. Do not make an adjustment to the California Qualified Expenditures for a projected misstatement; however, do adjust the California Qualified Expenditures for noted known errors in this second sample. If the projected misstatement from the second sample selection exceeds 2% of Qualified California Production Expenditures, adjust the Qualified California Expenditures for the average of the two projected misstatements.

[Note results and any details of exceptions noted]

- c. Attach a listing of any exceptions noted in the expenditure test in procedures 2 and 7(b) above (other than payroll). The listing should include amount, vendor/person, and nature of discrepancy.

[Note results and any details of exceptions noted]

Payroll:

1. Obtain detailed payroll reports by employee for those individuals that are included in Qualified Wages. Compare and reconcile the detailed payroll reports with the Qualified Wages in the Bible on a sum total basis. Understand all variances between the Bible and the detailed payroll report. Unexplained variances should total no more than \$25,000 in the aggregate. For unexplained variances which total over \$25,000 in the aggregate, re-reconcile to no more than \$25,000 or remove unexplained variances from Qualified Expenditures.

[Note results and any details of exceptions noted]

2. Select a sample of employees from the Qualified Wages account in the Bible according to sampling methodology noted in Appendix A. For each employee selected in the sample perform the following procedures:
 - a. Reconcile the amount of the Qualified Wages in the Bible for the individual with the payroll report.

[Note results and any details of exceptions noted]

- b. Inspect time cards, production reports, call sheets or other equivalent documentation. Confirm that wage amount is incurred for services performed in California.

[Note results and any details of exceptions noted]

- c. Inspect invoices from “qualified entities”. Confirm the date the expenditure was incurred, and that the loan out company name and the amount of the expenditure agrees with supporting payroll records. Confirm that the expenditure was incurred in California.

[Note results and any details of exceptions noted]

- d. Confirm that the qualified wages only include those expenses listed in Revenue and Taxation Code Section 17053.85(b)(18)(A)(i)-(iv) or Section 23685(b)(18)(A)(i)-(iv) and do not include any of the expenses listed in Section 17053.85(b)(18)(B)(i)-(iv) or Section 23685 (b)(18)(B) (i)-(iv).

[Note results and any details of exceptions noted]

- e. Confirm that only “qualified individuals” as defined in Revenue and Taxation Code Section 17053.85(b)(14) or 23685(b)(14), received “qualified wages”.

[Note results and any details of exceptions noted]

- f. Confirm that all Qualified Wages do not include compensation for any work incurred out of the state.

[Note results and any details of exceptions noted]

- g. Confirm that all Qualified Wages were not incurred prior to the date of the Credit Allocation letter.

[Note results and any details of exceptions noted]

- h. Confirm that all Qualified Wages were not incurred more than 30 days after the creation of the final elements.

[Note results and any details of exceptions noted]

- 3. Obtain the final “galley” or checker” of the main (if applicable) and end title credits for the production. For those below the line individuals (e.g. Unit Production Managers, Production Supervisors, First Assistant Directors, Post Production Supervisors, Visual Effects Supervisors) who also are receiving an on screen producer (e.g., executive, line, co-, associate, visual effects, music, post) credit, confirm that qualified wages only include: up to \$100,000 in DGA wages; industry standard wages; or wages equivalent with other crew in similar positions. For those receiving both above the line and below the line credits, please note in the report the names and qualified compensation for each individual for each end title credit received.

[Note results and any details of exceptions noted]

4. For exceptions noted in the payroll test in procedure 2 above, for the sample identified in the Top Stratum of Appendix A, adjust the Qualified California Production Expenditures for known errors noted during your testing.

[Note results and any details of exceptions noted]

5. For exceptions noted in the payroll test in procedure 2 above, for the sample identified in Stratum 1 in Appendix A, adjust the Qualified California Production Expenditures for known errors noted during your testing and project the misstatement results of the sample to all items from which the sample was selected. For purposes of calculating the projected misstatement, divide the monetary amount of misstatement of the exceptions identified by the sample population total amount (rate of misstatement). Multiply this rate of misstatement to the total expenditure population from which the Stratum 1 sample was selected. Perform the following procedures based upon the results of the calculation of the projected misstatement:
 - a. If the projected misstatement does not exceed 2% of Qualified California Production Expenditures, document the projected misstatement in the Report. Do not make adjustments to the California Production Expenditures for the projected misstatements.

[Note results and any details of exceptions noted]

- b. If the projected misstatement exceeds 2% of Qualified California Production Expenditures, select a second additional sample according to the sampling methodology noted in Appendix A for Stratum 1. Recalculate the projected misstatement for the second additional sample. If the projected misstatement for the second additional sample does not exceed 2%, document the projected misstatement in the Report. Do not make adjustments to the California Production Expenditures for a projected misstatement; however, do adjust the California Qualified Expenditures for noted known errors in this second sample. If the projected misstatement from the second sample selection exceeds 2% of Qualified California Production Expenditures, adjust the Qualified California Expenditures for the average of the two projected misstatements.

[Note results and any details of exceptions noted]

- c. Attach a listing of any exceptions noted in the payroll test in procedures 2 and 5(b) above. The listing should include amount, person or entity, and nature of discrepancy.

[Note results and any details of exceptions noted]

Related Parties & Other Affiliations:

1. Obtain from the production company a schedule listing all related party transactions (including parties with a 5% or greater ownership in or affiliation with the production company) for which the production company is including the transactions in the California Qualified Expenditures. The listing should note the type of relationship between the related party and the production company and the nature and amount of the transactions.

[Note results and any details of exceptions noted]

2. Obtain a signed letter from a production company representative stating that the applicant (indicated in the Credit Allocation Letter) has properly disclosed all related parties and related party transactions and that the schedules produced in accordance with item number 1 above are complete and accurate.

[Note results and any details of exceptions noted]

3. From the schedule in Procedure 1, select a sample of related party transactions for testing. Select all transactions greater than \$25,000. For the transactions less than \$25,000, randomly select 15 transactions for testing.

[Note results and any details of exceptions noted]

4. Perform the following procedures for each related party transaction selection:
 1. For wages paid to related parties, confirm that no amounts are included in the California Qualified Expenditures.

[Note results and any details of exceptions noted]

2. For non-payroll expenditures, inspect documentation to confirm that all related party transactions are made in accordance with an arm's length standard by inspecting comparison bids or studio rate cards . Whether transactions exhibit arm's length characteristics generally will be determined by reference to the results of comparable transactions under comparable circumstances.

[Note results and any details of exceptions noted]

5. For all transactions deemed to not be at arms length standard, from procedure 4 , note the nature, description and amount in the report and deduct these transactions from the Qualified Expenditure Total.

[Note results and any details of exceptions noted]

6. Attach a listing of all related party transactions obtained in procedure #1.

[Note results and any details of exceptions noted]

Wrap Up Procedures

1. If applicable, recalculate the 75% spend test (e.g. eligibility procedure number 6) after accounting records are revised for findings in payroll and expenditure procedures. Confirm that 75% of the Total Production Budget was spent for California Qualified Expenditures.

[Note results and any details of exceptions noted]

2. Provide the following data requested on Exhibit A which agrees with the cost report utilized by the CPA for the procedures above, as adjusted for the exceptions noted above:

- a. Qualified Wages & Fringes - excluding post-production
- b. Qualified Non-wage Spend - excluding post-production
- c. Total Qualified Expenditures – excluding post-production
- d. Qualified Wages & Fringes – post production
- e. Qualified Non-wage Spend – post –production
- f. Total Qualified Expenditures – post production only
- g. Total Tax Credit Allocation Due

[Note results and any details of exceptions noted]

3. The CPA must indicate on the Report that the specific program minimum and maximum thresholds as applicable to the type of production have been met.

[Note results and any details of exceptions noted]

Final Results:

As a result of the procedures performed, the eligible tax credit as shown in the attached Exhibit A totaled **[Tax Credit Amount]**.

We were not engaged to, and did not; conduct an audit, the objective of which would be the expression of an opinion on the completeness and accuracy of the accompanying SQCPE for the MP. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the information and use of the Company and the CFC and is not intended to be and should not be used by anyone other than these specified parties.

[CPA Signature]
(Firm)

[Date]
[Address, City, State]