KPMG

Film Financing and Television programming

A Taxation Guide

Now in its eighth edition, KPMG LLP's ("KPMG") Film Financing and Television Programming: A Taxation Guide (the "Guide") is a fundamental resource for film and television producers, attorneys, tax executives, and finance executives involved with the commercial side of film and television production. The guide is recognized as a valued reference tool for motion picture and television industry professionals.

Doing business across borders can pose major challenges and may lead to potentially significant tax implications, and a detailed understanding of the full range of potential tax implications can be as essential as the actual financing of a project. The Guide helps producers and other industry executives assess the many issues surrounding cross-border business conditions, financing structures, and issues associated with them, including film and television development costs and rules around foreign investment. Recognizing the role that tax credits, subsidies, and other government incentives play in the financing of film and television productions, the Guide includes a robust discussion of relevant tax incentive programs in each country.

The primary focus of the Guide is on the tax and business needs of the film and television industry with information drawn from the knowledge of KPMG International's global network of member firm media and entertainment Tax professionals.

Each chapter focuses on a single country and provides a description of commonly used financing structures in film and television, as well as their potential commercial and tax implications for the parties involved. Key sections in each chapter include:

Introduction
A thumbnail description of the country's film and television industry contacts, regulatory bodies, and financing developments and trends.

Key Tax Facts
At-a-glance tables of corporate, personal, and value-added (VAT) tax rates; normal nontreaty withholding tax rates; and tax year-end information for companies and individuals.

Financing Structures
Descriptions of commonly used financing structures in film and television production and distribution in the country and the potential commercial tax implications for the parties involved. The section covers rules surrounding co-productions, partnerships, equity tracking shares, sales and leaseback, subsidiaries, and other tax-efficient structures.

Tax and Financial Incentives
Details regarding the tax and financial incentives available from central and local governments as they apply to investors, producers, distributors, and actors, as well as other types of incentives offered.

Corporate Tax
Explanations of the corporate tax in the country, including definitions, rates, and how they are applied.

Personal Tax
Personal tax rules from the perspective of investors, producers, distributors, artists, and employees.

Digital Media
For the first time, we have included a discussion of digital media tax considerations recognizing its growing role in the distribution of film and television content.

KPMG and Member Firm Contacts
References to KPMG and other KPMG International member firms' contacts at the end of each chapter are provided as a resource for additional detailed information.

Please note: While every effort has been made to provide up-to-date information, tax laws around the world are constantly changing. Accordingly, the material contained in this publication should be viewed as a general guide only and should not be relied upon without consulting your KPMG or KPMG International member firm Tax advisor.

Production opportunities are not limited to the countries contained in this Guide. KPMG and the other KPMG International member firms are in the business of identifying early-stage emerging trends to assist clients in navigating new business opportunities. We encourage you to consult a KPMG or KPMG International member firm Tax professional to continue the conversation about potential approaches to critical tax and business issues facing the media and entertainment industry.

Thank you and we look forward to helping you with any questions you may have.

Tony Castellanos
+1 212 954 6840
acastellanos@kpmg.com

Benson Berro
+1 818 227 6954
bberro@kpmg.com

Czech Republic

Introduction

The Czech Republic should continue to be an attractive location for film production in the 21st century.

Key Tax Facts

Corporate income tax rate	19%
Personal income tax rate	15%
VAT rates	15%, 21%
Annual VAT registration threshold	CZK 1,000,000 (approximately EUR 27,480) (no minimum threshold for foreign entities)
Normal non-treaty withholding tax rates:	
Dividends	15% (exemption based on parent subsidiary directive
Interest	15%
Royalties	15%
Tax year-end: Companies	Accounting year
Tax year-end: Individuals	December 31

Film Financing

Financing Structures

Co-Production

There are no specific legal rules in Czech legislation governing co-production in the form of joint ventures. It is possible for a Czech investor to enter into a co-production with a foreign investor without establishing a separate legal entity by concluding an Association Agreement under the Czech Civil Code.

Under Czech legislation, several investors may associate themselves for the purpose of achieving an agreed joint purpose. Such an association is not regarded as a legal entity. Therefore, all participants are treated as unrelated individuals, both legally and in terms of taxation, both direct and indirect.

All participants shall own the activity jointly, each owning a share in the ratio corresponding to the extent of his contribution. All participants shall also own any revenue derived from the activity jointly. Each participant's share in the revenue from such activity (including exploitation) may be stipulated in the Association Agreement; otherwise, each participant's share shall be equal.

Czech tax legislation clearly states that even in the absence of a legal entity, any income of a nonresident participant derived from his participation in such an association is considered to be income generated by a permanent establishment. An applicable double tax treaty may modify this treatment.

Revenue from exploitation would be distributed to the participants according to the Association Agreement or, if not stipulated in the agreement, distributed equally. If no permanent establishment of a foreign participant is created, the taxation treatment of these revenues would be governed by the legislation of his country of residence. On the other hand, if a permanent establishment is created (the most likely scenario), all revenue attributable to the participant would be taxable in the Czech Republic.

Partnership

Financial investors and film producers from several countries may form a partnership with its registered office in the Czech Republic. Such a partnership may take the form of either a general (unlimited) commercial partnership *(verejna obchodni spolecnost)* or a limited partnership *(komanditni spolecnost)*. Both of these structures are more formal arrangements and involve the constitution of a legal entity separate from the founders of the partnership company (unlike the above-described Association Agreement). Partners may be either Czech or foreign individuals or companies. Although a general partnership is considered to be a legal entity, it is not treated as a taxable entity. Instead, the partners are taxed on their respective shares in the partnership's profits. Any income of a foreign partner derived from the Czech general partnership is automatically considered to be income generated by his permanent establishment in the Czech Republic. Subsequently, his share in the profits of the partnership (including revenue from exploitation rights) is subject to Czech corporate or individual income tax.

In the case of the limited partnership, the respective part of the partnership's profit attributable to the general (unlimited) partners is taxed under the same rules, which are applicable to the partners of a general commercial partnership. The part attributable to the limited partners is subject to corporate income tax and paid by the partnership under the general rules applicable to business companies. Any after-tax profit that is then distributed to limited partners is taxed as dividends.

An advantage for Czech partners of a general partnership and general (unlimited) partners of a limited partnership is that the profits/losses derived from their partnership are included in their particular tax base. This allows an immediate offset of losses resulting from one source of income against another positive source of income.

The liability for charging output VAT and the right to recover input VAT arises at the level of the legal entity and does not apply to the individual partners.

Other Tax-Effective Structures

The most common approach is the creation of a separate Czech legal entity—a Limited Liability Company (s.r.o.) or Joint Stock Company (a.s.). Both entities are regarded as separate legal entities.

A Limited Liability Company or Joint Stock Company is subject to standard taxation in the Czech Republic. The income of the company is subject to corporate income tax of 19%. For further details, see below.

Tax and Financial Incentives

A new act on audiovisual works and support in cinematography industry came into effect on 1 January 2013. A new institution, The Czech Republic State Fund for Support and Development of Cinematography (http://filmcenter.cz), was established as a separate entity independent of the Ministry of Culture. This act was amended several times. The last amendment came into force as of 1 January 2017.

New financial sources and fees were introduced, including fee on adopted TV broadcasting and fee on provision of audiovisual media services (effective from 2016). The current fee for cinematography performance has been increased to 1% of the entrance fee.

The decision procedures regarding projects to be supported have been changed. Separate calls for submission of applications have been introduced for particular areas and the projects are considered and always compared within the particular area. A system of incentives was communicated to the European Commission and it was approved.

What Projects Can Be Supported

The project must meet the following minimum runtime requirements:

- Feature, TV, animation, and documentary films (runtime of at least 70 minutes)
- TV series (runtime of at least 30 minutes per episode)
- Animation series (runtime of at least 5 minutes per episode)

How Much?

The following are the eligible costs:

- 20% of eligible costs on qualifying Czech expenditures
- 66% of withholding tax paid in the Czech Republic in connection with remuneration of nonresident cast and crew
- 20% of service production fee (provided that production applies for the incentives)

How to Qualify?

To qualify, the project must meet the following requirements:

- Pass a cultural test; and
- Meet the following minimum expenditures requirements in the Czech Republic:
  - CZK 15 million (approximately USD 729,000, EUR 589,000) for a feature or TV film
  - CZK 2 million (approximately USD 97,000, EUR 78,75000) for a theatrical documentary

- CZK 1 million (approximately USD 48,5000, EUR 39,000) for each animation episode
- CZK 8 million (approximately USD 390,000, EUR 314,000) for each TV episode.

How to Apply?

The application process consists of three stages. The application must be submitted to the State Cinematography Fund. All applications must be submitted electronically.

- The first stage (i.e., project registration application) focuses on whether the project satisfies the cultural test (and includes a refundable administrative fee of CZK 30,000). To pass the cultural test, the project must score at least 4 points from the cultural criteria and receive at least 23 points overall (out of a possible total of 46 points). The registration period has been abolished as of 1 January 2017. Thus, the application for project registration can be submitted at any time. The applicant must be a tax resident in the Czech Republic or, under certain conditions, also a tax resident in another EU state (e.g., with a PE in the Czech Republic). When the conditions within the first stage are fulfilled, the applicant receives a certificate of registration.
- The second stage of the application (i.e., project record application) focuses on the project's financial information. The applicant must submit information on all expenditures and a form proving the applicant's integrity. Since the institute of disposable resources has been abolished as of 1 January 2017, the applicant does not have to submit the application for project record as soon as possible after obtaining the certificate of registration. When the conditions within the second stage are fulfilled, the applicant receives a certificate of project record.
- The applicant must regularly inform the appropriate authorities on the current status of project realization and follow the stated deadlines during realization of the project. If the applicant fails to comply with these requirements, the applicant may face certain penalties (e.g., disqualification from the incentives regime for two years).
- The third stage (i.e., film incentive application) consists of the submission of the film incentive application, which must be filed within four years after the receipt of the project record certificate. The recipient of film incentives can divide the project in two phases and apply for each phase separately. The first application can be submitted when the shooting is finished. The recipient must have a bank account that dedicated to the project's incentives to prove the amount of the eligible costs incurred in connection with the project. The final application requires audited statements demonstrating that the total eligible costs are in accordance with the project documentation (the interim audit is not required).

How Are Funds Paid?

- The funds will be paid as a cash grant into the applicant's bank account within 30 days after the film incentive is granted. Bank charges will be paid by the applicants.

How Much Is Available?

- There is no cap on the amount of grant per project.
- Simultaneously, the full amount of film incentive is allocated in compliance with the certificate of project record.

— The program had in excess of CZK 800 million (approximately USD 39 million or EUR 31.4 million) in 2016.

More Information Can Be Found On http://www.fondkinematografie.cz/

Other Financing Considerations

Tax Costs of Share and Bond Issues

Generally, no form of stamp duty or capital duty is charged on the issue or the transfer of shares, partnership interests, or debt instruments.

Exchange Controls and Regulatory Rules

There are no exchange controls preventing foreign investors from repatriating profits to their home territory. There is a duty to notify some operations, such as receiving a financial debt from a foreign resident, to the Czech National Bank.

Corporate Taxation

Recognition of Income

Film Production Company – Production Fee Income

Czech-resident Company

The tax rate on corporate income is 19%.

Foreign Company

A foreign company not having its registered office in the Czech Republic shall be liable for tax on income arising only from sources in the Czech Republic. Such income shall mean, in particular, income generated by the activities of a permanent establishment. Any double tax treaty may modify the rules for constituting a permanent establishment. The permanent establishment is liable to the same tax rate as a resident company.

Film Production Company – Sale of Distribution Rights

Gain on the sale of intangibles will be recognized as regular income at the time the contract payment becomes enforceable, irrespective of when the payment is received. Should the distribution rights be granted only for a limited period of time, it would be possible to accrue the revenue over such time period.

Film Distribution Company

If a Czech-resident company acquires rights in a film from an unrelated production company, the transaction is regarded as the granting of a license.

If the license is granted for a limited time period, the costs connected with the granting of the license should be accrued over this period. If an unlimited license is granted, the expenditures must be capitalized and depreciated (for details, refer to the section Amortization of Expenditure).

If any of the above-mentioned payments is made to a foreign entity, the Czech company is obliged to deduct a withholding tax rate of 15%. This rate could be reduced by the applicable double tax treaty.

Transfer of Film Rights between Related Persons

Czech tax legislation incorporates the arm's length principle. Based on the special provision of the Income Tax Act, the prices in transactions between related parties should be at arm's length. If any of the above-mentioned transactions take place between related parties, the Czech tax authorities may apply the arm's length test to determine whether the contractually agreed price is acceptable. Otherwise, the tax authority is entitled to adjust the tax base of the Czech taxpayer. Related parties are considered to include all companies within a group, companies where the same individuals participate in the management of such companies, and companies entering into the transaction with the aim of reducing the tax base.

In particular, the transfer of rights and the granting of licenses between related parties are likely to be of interest to the tax authorities if the other party is not subject to taxation in the Czech Republic. It is, therefore, advisable to document the intragroup transfer pricing policy for all such transactions and to ensure that the policy is defensible and consistently applied.

The Czech transfer pricing rules are based on the OECD transfer pricing guidelines.

Amortization of Expenditure

Production Expenditure

Where a company produces a film in order to exploit the film itself, the production costs should be capitalized as an intangible asset and depreciated. Audiovisual work must be depreciated over a period of at least 18 months.

Where a company acquires rights to a film from another person, the rights must also be capitalized and depreciated. If the contract limits the rights to a film for a certain tax period, the right should be depreciated over that period. In other cases, the right should be depreciated over at least 18 months.

Where a company produces a film without the intention to exploit the film itself, i.e., the production company solely renders production services to a third party at the full risk of the third party, the costs incurred by the production company are fully deductible as business expenses.

Other Expenditure

There are no special rules applicable to film or distribution companies. Business expenses not related to the production costs of the film are deductible as incurred. Entertainment costs and gifts are nondeductible for tax purposes.

Expenditures on acquiring fixed assets, such as land and buildings, office furniture, and equipment should be capitalized and depreciated in accordance with Czech tax law.

Losses

According to the Income Tax Act, a tax loss that was recorded and assessed in the preceding taxable period may be carried forward, but no more than five taxable periods immediately following the taxable period in which the tax loss was assessed.

Foreign Tax Relief

A Czech film production or distribution company that receives income from abroad may, in many cases, be subject to foreign withholding tax. The method of avoidance of double taxation depends on the particular double tax treaty.

Indirect Taxation

Value Added Tax (VAT)

As a member of the European Union (EU), the Czech Republic applies VAT to the supply of goods and services in a way that is, generally, consistent with EU law.

Supply of a Completed Film

The supply of a film is regarded as a transfer of rights. Generally, the VAT rate applicable to the supply of a completed film is 21%. If the supplier of the film is a Czech taxable person registered for VAT purposes in the Czech Republic, he must account for VAT as at the day on which the license for the completed film is granted to a Czech entity, or the date of issue of the invoice, or the date of payment (whichever occurs earlier).

However, the supply of a film is subject to the reverse charge mechanism if the license is granted by a Czech taxable person to a taxable person with a registered office in another EU member state or outside the EU, provided the recipient does not have a permanent establishment in the Czech Republic. In addition, the reverse charge mechanism applies if the license is granted to a Czech taxable person by a person with a registered office in another EU member state or outside the EU, provided the supply is not carried out by the supplier's permanent establishment (if any) located in the Czech Republic.

If the recipient is not a taxable person (i.e., person carrying out economic activities), a special rule described in the Digital Media section below applies in the Czech Republic.

Sale of Distribution Rights and Royalty Payments

The sale of distribution rights and royalty payments are subject to the same taxation principles as the supply of a completed film.

Peripheral Goods

The VAT treatment of sales of peripheral goods (items connected to the distribution of a film) depends on the nature of the goods involved.

Thus, supplies of books and magazines (provided advertisements represent less than 50% of the content) are subject to the second reduced rate of 10%, whereas supplies of clothes or recorded music are subject to 21%.

However, should the peripheral goods be considered as an ancillary supply to a principal supply (e.g., supply of the completed film), the VAT treatment of the supplied peripheral goods should follow the VAT treatment of the principal supply.

Promotional Goods and Services

The VAT rate applicable to the supply of promotional goods and services depends on the nature of goods and services.

The provision of promotional goods free of charge is not regarded as a taxable supply of goods, provided the acquisition value (without VAT) of the promotional item does not exceed CZK 500 (EUR 19.50); the provider of promotional goods up to this value is still allowed to deduct input VAT relating to the acquisition of the goods.

If promotional goods with a value exceeding CZK 500 (without VAT) are provided without consideration, the provision of such goods is subject to VAT, provided the related input VAT was deducted.

Catering Services and Accommodation
Both catering and accommodation services are subject to the reduced rate of 15%.

Purchasing of Goods
Goods imported from a non-EU country are subject to import VAT (in most cases, 21%) and is payable by the importer. If the imported goods are used for the economic activities of the importer, he may recover input VAT. It is possible to settle import VAT by means of the regular VAT return; provided the importer is entitled to claim input VAT on the goods imported, it will be possible to claim the credit in respect of input VAT in the same period and no tax will have to be paid.

Where goods are purchased and delivered from a person registered for VAT in another EU member state, the recipient is in general obliged to account for output VAT; if the general conditions for the entitlement to input VAT credit are met, the credit may be claimed in the same period as output VAT and no tax has to be paid.

If goods are purchased from local entrepreneurs, VAT will be charged by the supplier (if local reverse charge regime is not applicable). Such VAT is, in principle, recoverable by claiming input VAT credit in the tax return.

Personal Taxation

Nonresident Artists (self-employed)

Income Tax Implications
Czech tax nonresidents are liable to tax only on Czech source income, i.e., remuneration for work (activities) performed in the Czech Republic. Most Czech double tax treaties stipulate that income derived by a resident of a contracting state, as an entertainer from his personal activities exercised in the other contracting state, may be taxed in the contracting state in which the activities of the entertainer are exercised. This means that the activities of foreign artists exercised in the Czech Republic shall be taxed in the Czech Republic. Therefore, gross income from an activity performed personally in the Czech Republic is subject to withholding tax at the rate of 15%. The withholding tax is collected by a Czech person paying remuneration for the artistic performance. According to Czech double tax treaties, any double taxation of such income from Czech sources may be avoided in the artist's home country by using the relevant method stipulated by the treaty. Administrative or support staff, e.g., cameramen, producers, film directors, choreographers, technical staff, are subject to different rules than performing artists. If they are not employees, they will be taxed in the Czech Republic only if they have a permanent establishment therein, or in case the income has a character of copyright payment, it will be subject to a withholding tax rate of 15% (subject to exemption or reduction in rate, according to a particular Double Tax Treaty).

Social Security Implications
EU Regulation No. 883/2004 (EU Regulation) must be followed to determine where social security contributions should be paid in the case of artists residing in other EU member states.

Resident Artists (self-employed)

Income Tax Implications
Artists are not usually treated as carrying on trade. Their income is classified as income from an independent activity, and the person who exercises such activity is obliged to register

himself/herself at the tax authority for personal income tax. Resident artists will be liable to tax in the Czech Republic on their worldwide income. The net Czech income is subject to a flat tax rate of 15%. The net income is calculated as the income after deduction of related expenses; however, no obligatory social security insurance may be deducted. Artists' standard business expenses are tax deductible. Provided that a taxpayer does not claim actual expenses, he may deduct 40% of his income as a lump-sum expense. The maximum amount of lump-sum expense is CZK 400,000. Income from an independent activity exceeding cap for social insurance, i.e., CZK 1,438,992 in 2018 (please see below), is further subject to 7% solidarity tax.

Social Insurance of Czech Artists

A self-employed artist is subject to the same rules as other independent entrepreneurs.

Health Insurance of Czech Artists

A self-employed artist who exercises independent activities may be obliged to pay health insurance contributions depending on residence permit status.

Employees

Income Tax Implications

The employer is obliged to withhold tax in respect of personal income tax from dependent activities. The income of individuals is subject to a flat tax rate of 15%. The tax on employment income is calculated on the "super-gross" salary, which is the gross salary increased by social security and health insurance contributions payable by the employer in the Czech Republic (34% or 9% if the cap for social insurance was reached). In addition, gross employment income exceeding the cap for social insurance (CZK 1,438,992 in 2018) is further subject to 7% solidarity tax. The 7% solidarity tax is also due as an advance payment, on a monthly basis, on gross salary exceeding CZK 119,916 per month.

A taxpayer (employee) who was receiving taxable remuneration in a taxable period from only one employer, or consecutively from more than one employer, may submit a written request to the last employer for an annual settlement of tax prepayments. Such a request must be made no later than 15 February of the following year. If an employee has other income exceeding CZK 6,000 per year, in addition to the income from the dependent activity or if his/her employment income was subject to solidarity tax, the Czech company should issue a standard confirmation of the employee's taxable income and tax withheld *(Potvrzeni o zdanitelnych prijmech ze zavisle cinnosti a z funkcnich pozitku, srazenych zalohach na dan a danovem zvyhodneni)* after the year-end. This confirmation would be filed as an enclosure to the employee's Czech personal income tax return for the year concerned.

A resident employee is entitled to reduce his/her income by tax deductible items and his/her tax liability by tax credits. A nonresident employee is entitled to reduce his/her tax liability only by the basic tax credit. Other tax credits and tax deductible items will be applicable to a nonresident from EU/EEA member states only if the income from Czech sources exceeds 90% of his total income.

The Ministry of Finance of the Czech Republic has published the proposal to amend the Income Tax Act, which should become effective as of 1 January 2019. The 15% flat rate and 7% solidarity tax will be abolished. Current calculation of personal income tax on super-gross salary shall also be abolished. Instead, there should be progressive tax rates of 19% for income of up to CZK 1.5 million and 24% (may be 23%) for income above this amount.

Similarly, self-employed individuals will also be subject to the above progressive tax rates; however, they should be entitled to deduct 75% of their social security and health insurance contributions.

The effective tax rate of employees and self-employees should not therefore change significantly.

Social Security Implications

The general rule of the EU Regulation is that persons to whom the EU Regulation applies, i.e., EU nationals and non-EU nationals (third-country national) who are legal residents of an EU state, should be subject to social security only in one member state, which should be the state in which they perform the work, i.e., in the Czech Republic. This follows from Article 11 of the EU Regulation, which states that the legislation of the state in which the employee works will apply.

In addition, the EU Regulation provides special rules for posted employees and for employees performing activities in two and more EU states.

Moreover, an employee may apply for an exemption from the basic and special rules, and from the liability to pay social security contributions in the Czech Republic, in accordance with Article 17 of the Regulation, if the prospective period of employment by an employer residing in the Czech Republic would be limited and if the employee was paying social security contributions in another EU member state before this employment, provided it is in the best interest of the employee to remain in the home country system.

In other cases, the salary of the expatriate is subject to Czech social insurance and health insurance contributions. A Czech employer is obliged to withhold these contributions from the employee's remuneration. The employee's contribution amounts to 11% and the employer's part is 34% of the gross remuneration. There is an annual cap on social insurance contributions equal to 48 times the average wage (CZK 1,438,992 in 2018). No cap applies to health insurance.

Digital Media

There is no special tax treatment of digital media in the Czech Republic. The Czech Republic's position regarding cross-border transactions and the application of double tax treaties is fully in accordance with the commentary on electronic commerce in Article 5 of the OECD Model Tax Convention.

VAT in EU

New EU VAT rules in relation to supplies of telecommunications, broadcasting, and e-services to consumers (B2C) came into effect from 1 January 2015. The place of supply in respect of all supplies of telecommunications, broadcasting, and e-services to consumers is the place where the consumer resides. To simplify obligations of suppliers of such services, a new special scheme known as the Mini One Stop Shop (MOSS) came into operation on 1 January 2015. The MOSS allows business to submit returns and pay the relevant VAT due to member states through the Web portal of one member state. Otherwise, the business is required to register and submit returns in several member states.

Media and Entertainment Tax Network Members:

Tomáš Kroupamáš Kroupa
KPMG Ceska republika' s.r.o.
Pobøežní 1a
186 00 Praha 8
Czech Republic
Phone: +420 222 123 623
Fax: +420 222 123 446

Petr Toman
KPMG Ceska republika' s.r.o.
Pobøežní 1a
186 00 Praha 8
Czech Republic
Phone: +420 222 123 602
Fax: +420 222 123 446