

## Guide to the Taxation of Film Owners

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# GUIDE TO THE TAXATION OF FILM OWNERS

## Foreword

This guide provides general guidelines regarding the taxation of film owners, as well as their liability in respect of some of the taxes, duties, levies and contributions administered by SARS. It is not meant to delve into the precise technical and legal detail that is often associated with taxation and should, therefore, not be used as a legal reference. The guide is not a binding general ruling in terms of Part IA of Chapter III of the Income Tax Act, No. 58 of 1962 (the Act).

This is an update of the previous guide dated November 2004 and is based on the legislation as at 8 August 2007, including the amendments effected by the Taxation Laws Amendment Act, No. 8 of 2007 and the Taxation Laws Second Amendment Act, No. 9 of 2007.

Should you require additional information regarding any taxes/duties/levies/contributions administered by SARS, you may –

- contact your local SARS branch;
- visit SARS website at [www.sars.gov.za](http://www.sars.gov.za);
- contact your own tax advisors;
- if calling locally, contact the SARS National Call Centre on 0860 12 12 18; or
- if calling from abroad, contact the SARS National Call Centre on +27 11 602 2093.

Comments and/or suggestions regarding this guide may be sent to the following e-mail address: [policycomments@sars.gov.za](mailto:policycomments@sars.gov.za).

Prepared by:

**Legal and Policy Division**

**SOUTH AFRICAN REVENUE SERVICE**

Date of first issue: November 2004

Date of second issue: February 2008

# CONTENTS

Foreword.....	i
<b>OVERVIEW.....</b>	<b>1</b>
<b>PART A: DETERMINATION OF THE TAXABLE INCOME OF A FILM OWNER .....</b>	<b>1</b>
<b>1. WHO IS A FILM OWNER? .....</b>	<b>1</b>
<b>2. HOW IS THE TAXABLE INCOME OF A FILM OWNER DETERMINED? .....</b>	<b>2</b>
2.1 GENERAL PROVISIONS.....	2
2.1.1 Determination of the gross income of a film owner.....	2
a) Film owners could be residents or non-residents .....	2
b) A film owner could be subject to taxation in more than one country .....	3
2.1.2 Deduction of exempt amounts .....	3
2.1.3 Deduction of all allowable deductions/allowances.....	4
2.1.4 Inclusion of the taxable capital gain .....	4
2.2 THE FILM ALLOWANCE (SECTION 24F) .....	5
2.2.1 Basic requirements and limitations .....	6
a) Only film owners qualify for the film allowance.....	6
b) The film allowance only applies to production and post-production costs.....	6
c) The costs must be paid within a certain period to qualify for the allowance.....	8
d) The film must be used in the production of income .....	8
e) The film must be completed.....	9
2.2.2 Films completed prior to 1 April 2006 .....	10
2.2.3 The quantum of the film allowance .....	10
a) The “at risk” limitation.....	11
(i) Basic concepts .....	11
(ii) Carry forward of disallowed amounts .....	12
(iii) When is a film owner deemed to be “at risk”? .....	12
(iv) When is a film owner not deemed to be “at risk”? .....	12
b) South African activity limitation .....	13
c) Actual cost limitation .....	14
2.2.4 How does the film owner claim the allowance? .....	15
2.3 ABUSE OF THE FILM ALLOWANCE .....	15
<b>PART B: OTHER TAXES/DUTIES/LEVIES/CONTRIBUTIONS .....</b>	<b>18</b>
<b>3. EMPLOYMENT INCOME RELATED TAXES/LEVIES/CONTRIBUTIONS (PAYE, SDL AND UIF) .....</b>	<b>18</b>
3.1 EMPLOYEES’ TAX (PAYE) .....	18
3.1.1 Employers are liable to withhold employees’ tax in respect of all remuneration paid/payable to employees.....	18
3.1.2 Employees’ tax is not deductible in respect of labour brokers that have exempt status.....	20
3.1.3 Employees’ tax is not deductible from amounts payable to certain foreign entertainers .....	21
3.2 SKILLS DEVELOPMENT LEVIES (SDL).....	21
3.3 UNEMPLOYMENT INSURANCE FUND CONTRIBUTIONS (UIF) .....	21

<b>4.</b>	<b>VALUE-ADDED TAX (VAT)</b> .....	<b>22</b>
4.1	WHEN MUST A FILM OWNER REGISTER FOR VAT? .....	22
4.2	VAT RATES AND TYPES OF SUPPLIES .....	22
4.3	TAX PERIODS AND PAYMENT OF VAT TO SARS .....	23
<b>4.4</b>	<b>ON WHICH AMOUNTS MAY FILM OWNERS CLAIM VAT (INPUT TAX)?</b> .....	<b>24</b>
<b>5.</b>	<b>CUSTOMS DUTIES</b> .....	<b>24</b>
5.1	CUSTOMS DECLARATION - NON RESIDENTS .....	25
5.1.1	Customs rebate for goods temporarily admitted for specific purposes .....	25
5.1.2	Agreement on Temporary Admission Carnet (ATA Carnet) .....	25
5.2	CUSTOMS DECLARATION - RESIDENTS .....	25
<b>6.</b>	<b>EXCISE DUTIES</b> .....	<b>26</b>
<b>7.</b>	<b>DONATIONS TAX</b> .....	<b>26</b>
<b>8.</b>	<b>WITHHOLDING TAX ON ROYALTIES</b> .....	<b>27</b>
<b>9.</b>	<b>WITHHOLDING TAX ON FOREIGN ENTERTAINERS</b> .....	<b>27</b>
<b>10.</b>	<b>TRANSFER DUTY</b> .....	<b>28</b>
	<b>PART C: GENERAL (INCOME TAX)</b> .....	<b>29</b>
<b>11.</b>	<b>REGISTRATION AS A TAXPAYER</b> .....	<b>29</b>
<b>12.</b>	<b>CHANGE OF ADDRESS</b> .....	<b>29</b>
<b>13.</b>	<b>SUBMISSION OF INCOME TAX RETURNS</b> .....	<b>29</b>
<b>14.</b>	<b>YEAR OF ASSESSMENT</b> .....	<b>29</b>
<b>15.</b>	<b>FILM OWNERS ARE PROVISIONAL TAXPAYERS</b> .....	<b>29</b>
<b>16.</b>	<b>OBJECTIONS AND APPEALS</b> .....	<b>30</b>
<b>17.</b>	<b>RETENTION OF RECORDS</b> .....	<b>30</b>
	<b>CONCLUSION</b> .....	<b>30</b>

## OVERVIEW

Due to the rapid growth of the film industry in South Africa SARS has identified a need to issue an information guide that deals with the taxation of film owners. The main aim of the guide is to explain the income tax consequences for film owners in South Africa. The first part of the guide deals with the determination of the taxable income of a film owner and takes into account all the amendments to date. Furthermore, it contains information about the responsibilities of film owners with regard to some of the other taxes, duties, levies and contributions administered by SARS. Finally, it contains information about certain of the administrative provisions of the Income Tax Act, No. 58 of 1962, as amended (the Act). All the definitions in this guide have been extracted from the Act, unless the context indicates otherwise. The words “taxpayer” and “film owner”, as well as “South Africa” and “the Republic” will be used interchangeably as they have the same meaning for purposes of this guide.

## PART A: DETERMINATION OF THE TAXABLE INCOME OF A FILM OWNER

Resident film owners (as any other persons that are regarded as residents for income tax purposes) are liable for the payment of income tax on their world-wide income, that is, all income from South African as well as foreign sources. Non-resident film owners (as any other persons that are not regarded as residents for income tax purposes) are only liable for the payment of income tax on their income from a South African source, for example where a non-resident film owner derives income from the distribution of a South African produced film in South Africa.

Special deductions for expenditure incurred with regard to production and post-production costs are allowed to film owners in the determination of their taxable income. These deductions are contained in section 24F of the Act. Where production companies receive consideration from film owners for the production of films, the production companies will not be eligible for these deductions, as they are not regarded as film owners. The income tax deductions applicable to persons that generate income from a trade will then apply.

Film owners can conduct their business in their individual capacity or through other entities, such as companies or close corporations. There are instances where film owners may also be required to register for Employees' Tax (PAYE), Skills Development Levies (SDL), Unemployment Insurance Fund Contributions (UIF) and/or Value-Added Tax (VAT) etc.

A partnership is not regarded as a person for income tax purposes. Each film owner that is a partner, therefore, has to register as a separate taxpayer and will be assessed as such. The assessments of the partners will be based on the ratios in which the profits or losses of the partnership are to be shared. Deductions will also be taken into account according to the same ratios when determining their taxable income.

### 1. WHO IS A FILM OWNER?

A film and a film owner are defined in section 24F(1) as follows:

“film” means –

a recording of moving visual images and sound by means of cinematographic film, video tape, video disc or otherwise, including any copy of the film and any right therein.

**“film owner”** means –

any person who owns, whether solely or jointly, a film.

In order to qualify as a “film owner” for purposes of section 24F of the Act, a person must acquire *bona fide* ownership of a film or film right. The determination of whether or not a person is a *bona fide* film owner rather than, for example, a mere licensee, must be based on all the facts and circumstances, including the terms of all the agreements entered into by or amongst parties to an arrangement.

A person is not considered a *bona fide* film owner, for example, where the net effect of such agreements is to grant that person no more than a limited right to income for a limited period of time, without transferring the risks and rewards incidental to the actual ownership of the film to such person.

A person that only renders a service to a film owner, for example, a production company that produces a film on behalf of the owner of such a film or a distribution company that merely holds distribution licences to sell films through cinemas and videos, is not regarded a film owner and cannot claim any deductions under section 24F. The income so derived from his or her trade would be subject to the normal income tax rules.

## **2. HOW IS THE TAXABLE INCOME OF A FILM OWNER DETERMINED?**

### **2.1 GENERAL PROVISIONS**

The taxable income of a film owner will be subject to the payment of normal tax. A person who carries on a trade as a film owner may earn income from various sources as a result of the exploitation of the film, for example, income from ticket sales, distribution fees, royalties as well as income from other sources such as interest on investments etc. All this income must be added together in order to arrive at the person’s “gross income”.

Exempt income must then be deducted from this amount in order to arrive at “income”. Once “income” has been determined, a film owner may be entitled to certain deductions and allowances in order to determine the person’s “taxable income” before any capital gains or losses have been taken into account. As a final step to arrive at taxable income that is subject to normal tax, the net capital gain on capital assets disposed of must be added.

#### **2.1.1 Determination of the gross income of a film owner**

In order to determine the gross income of a film owner, receipts or accruals from all sources must be added together. The following factors must, however, be taken into account:

##### **a) Film owners could be residents or non-residents**

For a resident film owner, the receipts and accruals from world-wide sources, must be added together in order to arrive at the person’s gross income, except where they are of a capital nature. In addition to this amount, certain specific amounts, for example expenditure in respect of which a deduction/allowance has been allowed that has subsequently been recovered or recouped as a result of, for example, the payment of a claim or the sale of a fixed asset, will also form part of the person’s gross income.

For a non-resident film owner, only the amounts received or accrued from a South African source will be regarded as gross income.

Two tests apply in determining whether a film owner, who is a natural person, is regarded as a South African resident for income tax purposes:

- The ordinarily resident test (that is normally the place to which a person will naturally and as a matter of course return to from his/her travels); and
- The physical presence test in the Republic (that is based on the number of days during which a person was physically present in the Republic during a year of assessment and prior years of assessment).

A film owner that is a company, close corporation or a trust that is –

- incorporated, established or formed in the Republic; or
- has its place of effective management in the Republic

will be regarded as a South African resident for income tax purposes.

Further information regarding the residence basis of taxation for individuals can be found on the SARS website [www.sars.gov.za](http://www.sars.gov.za) and can also be obtained from SARS branches.

**b) A film owner could be subject to taxation in more than one country**

Films owned by residents may earn income from foreign sources as a result of their distribution, usage etc. in foreign countries. Under these circumstances the income from foreign sources may be subject to both South African income tax and tax in the foreign countries, creating a potential for so-called “double taxation”. For example, if a film owner who is a South African resident earns income from the distribution of films in Canada, such income could be taxable in both countries. It will be taxable in the Republic, because the film owner is a resident in South Africa and it could also be taxable in Canada under that country’s sourcing rules.

Countries have entered into agreements for the avoidance of double taxation to eliminate or reduce the potential for such double taxation. These agreements commonly provide that income of a particular nature will be taxed in only one of the countries, or may be taxed in both countries with the country of residence allowing a credit for the tax imposed by the other, or exempting the income. South Africa uses the credit method.

South Africa has entered into double taxation agreements (DTAs) with various countries for the avoidance of double taxation. The existing DTAs between South Africa and other countries are available on the SARS website [www.sars.gov.za](http://www.sars.gov.za).

**2.1.2 Deduction of exempt amounts**

The next step to determine the taxable income of a film owner is to deduct all receipts and accruals that are exempt from income tax from the gross income of the film owner. The net amount constitutes “income” as defined in the Act.

The following receipts and accruals are examples of exempt amounts:

- An amount paid or payable to a film owner in terms of the Film and Television Production Rebate Programme administered by the Department of Trade and Industry.
- An amount received by or accrued to a non-resident film owner in the form of royalties or similar payments for the right or the grant of permission to use in the Republic –

- certain patents, designs, trademarks, copyright, models, patterns, plans, formulas or processes or any property of a similar nature; or
- any motion picture film, or any film or video tape or disc for use in connection with television, or any sound recording or advertising matter used or intended to be used in connection with such picture, film or video tape or disc,

that has been subject to 12% withholding tax on royalties.

- An amount received by or accrued to a film owner by way of a subsidy payable by the State as provided in section 10(1)(zG) of the Act.
- Basic exempt amounts applicable to investment income.

### **2.1.3 Deduction of all allowable deductions/allowances**

The next step in determining the taxable income of a film owner is to deduct all allowable deductions/allowances from the person's income. The allowable deductions/allowances will include –

- the special allowance provided for in section 24F of the Act (the film allowance) that relates to the acquisition/production of a film and post-production costs. Notably, the film allowance generally permits the deduction of expenditure for these costs regardless of whether the expenditure is of a revenue or capital nature or whether these costs would normally be categorised in the industry as pre-production costs. In addition, expenditure for assets such as machinery and equipment, in respect of which allowances will normally be allowed over a number of years, may generally be deducted in full during the year of assessment in which the completion date of the film falls. To the extent that the film allowance exceeds the film owner's income from the film itself, the deductions may be allowed against the film owner's income from other sources. For more information regarding the film allowance, see paragraph 2.2; and
- Those deductions allowable to taxpayers in respect of expenditure other than expenditure related to the production and post-production costs of the film, incurred in the production of income for the purposes of trade such as rental expenses.

### **2.1.4 Inclusion of the taxable capital gain**

As a final step in the determination of the taxable income of a film owner, the taxable capital gain or assessed capital loss arising from the disposal of capital assets must be determined. This determination is made in terms of the Eighth Schedule to the Act. As capital gains tax (CGT) only came into operation on 1 October 2001, only the portion of a capital gain or loss attributable to the period on or after 1 October 2001 is taken into account in the case of pre- 1 October 2001 assets.

A capital gain arises when the proceeds upon the disposal of a capital asset exceed the base cost of that asset and a capital loss arises when a capital asset is disposed of and the base cost exceeds the proceeds on disposal. Assets such as land and buildings, plant and machinery, listed and unlisted shares as well as rights of any kind, for example intellectual property rights and copyrights are regarded as capital assets.

Capital gains and losses must be disclosed in a person's return of income for the year of assessment in which the assets were disposed of. Where the sum of capital gains in a year of assessment exceeds the sum of capital losses, the net amount must be reduced by the annual exclusion in order to determine an aggregate capital gain.



This figure must be reduced by any assessed capital loss brought forward and the result will either be an assessed capital loss or net capital gain.

Where the sum of capital losses exceeds the sum of capital gains in a year of assessment, the resulting figure must be reduced by the annual exclusion (only applicable to individuals and special trusts), with the end result being an aggregate capital loss. This aggregate capital loss must be added to any assessed capital loss brought forward from the previous year to determine the assessed capital loss for the current year. An assessed capital loss is carried forward to the succeeding year and is only available for set off against future capital gains (that is, it does not reduce taxable income).

Where a film owner is an individual, 25% of the net capital gain will be included in the person's taxable income and where the film owner is a company or a trust, 50% of the net capital gain is included in its taxable income.

Individuals and special trusts (as defined in the Eighth Schedule) are entitled to an annual exclusion of R15 000 before capital gains or losses are taken into account. If the annual exclusion is not absorbed in a particular year of assessment, the excess may not be carried forward to the next year. This exclusion does, however, not apply to companies, close corporations and trusts.

Further information regarding CGT is available on the SARS website [www.sars.gov.za](http://www.sars.gov.za) and can also be obtained from SARS branches.

## **2.2 THE FILM ALLOWANCE (SECTION 24F)**

Special rules contained in section 24F of the Act determine the amount and timing of deductions allowable to film owners in respect of production and post-production costs incurred in respect of the acquisition or production of films (the film allowance). A deduction in respect of the film allowance will be allowed in lieu of other deductions that are normally allowable in respect of such expenditure incurred.

Prior to the introduction of the amendments to section 24F by section 32 of the Revenue Laws Amendment Act, No. 31 of 2005, section 24F of the Act provided for three special deductions for film owners, namely –

- A deduction in respect of production and post-production cost incurred in respect of a film;
- A deduction in respect of marketing expenditure incurred in respect of a South African Export Film; and
- A deduction in respect of the print costs incurred in making copies of a film.

These deductions were all subject to the “at risk” rule.

With effect from 1 April 2006 the provisions of section 24F were refined to *inter alia* –

- encourage the production of South African films by focusing on providing a more beneficial allowance for South African film productions;
- no longer provide for separate deductions in respect of expenditure relating to marketing and printing costs;
- introduce a time limit on the payment of production and post-production costs; and

- treat film owners not to be at risk in respect of loans and credit not payable within 10 years from the date of the completion of films.

### 2.2.1 Basic requirements and limitations

The film allowance is subject to five basic requirements.

#### a) Only film owners qualify for the film allowance

Only persons that are regarded as film owners may qualify for the film allowance. A production company that, for example, only produces a film on behalf of the owner of the film will not qualify for the film allowance. For more information regarding film owners, see paragraph 1 of this guide.

#### b) The film allowance only applies to production and post-production costs

The film allowance is only applicable where production costs or post-production costs have been incurred. Any other costs, for example, marketing costs and printing costs can be claimed in terms of the normal provisions of the Act. The normal requirements pertaining to the claiming of deductions will be applicable to such other expenditure.

“**production cost**”, defined in section 24F means –

in relation to a film, the total expenditure incurred by the film owner in respect of the acquisition or production of such film, excluding expenditure incurred in the erection, construction or acquisition of any buildings or other structures or works of a permanent nature, but including, without in any way limiting the scope of this definition —

- (a) any remuneration, salary, legal, accounting or other fee, commission or other amount paid or payable to any person for the purpose of or in connection with the production of the film;
- (b) the cost of acquiring the story rights, script, screenplay, copyright or other rights in relation to the film;
- (c) insurance premiums in respect of insurance against injury to or death of persons, or loss of or damage to property employed or used, as the case may be, in the production of the film;
- (d) premiums or commission payable in order to secure a guarantee that the cost of the film will not exceed a specified amount;
- (e) interest, finance charges and raising fees incurred for the purpose of or in connection with the production of a film;
- (f) the cost of acquiring or creating music, sound and other effects which will form part of the film;
- (g) any allowance which but for the provisions of this section would be allowed under section 11(e) or (o) or 12C in respect of any machinery, implements, utensils or articles used in the production of a film: Provided that –
  - (i) any such allowance shall be deemed to be an amount of expenditure incurred;
  - (ii) an amount equal to the total amount of any such allowance which may be granted in respect of any year of assessment divided by the number of days in that year shall be deemed to have been incurred on each day of that year;
  - (iii) such expenditure shall be deemed to have been incurred in the country in which the asset in respect of which the allowance may be granted was acquired; and
  - (iv) no deduction or allowance shall be granted in respect of the cost of acquisition of any such machinery, implements, utensils or articles otherwise than as provided in this paragraph or paragraph (h); and

- (h) expenditure incurred in respect of –
- (i) the purchase, hire or construction of sets; and
  - (ii) the hire of any machinery, implements, utensils or articles used in the production of the film,

but excluding any such expenditure incurred after the completion date and any expenditure incurred in the marketing or promotion of, or soliciting of orders for, the film: Provided that where a film owner acquired the film directly or indirectly from a connected person the total expenditure incurred by the film owner in respect of the acquisition of the film must be limited to the total expenditure incurred by the connected person in respect of the acquisition thereof or production cost to that connected person in respect of the production of the film.

**“post-production cost”**, defined in section 24F means –

in relation to a film any expenditure of the nature referred to in the definition of “production cost” which is incurred after the completion date, but excluding any print cost in relation to such film.

**“print cost”**, defined in section 24F means –

in relation to a film, any expenditure incurred by the film owner in the making of copies of the film.

The cost pertaining to the acquisition of a film is included under the definition of “production cost” and qualifies for the allowance. To avoid an artificial increase in the cost of the acquisition, the cost of a film acquired directly or indirectly from a connected person is limited to the cost of acquisition of the film by the connected person or the production cost incurred by the connected person in producing the film. (This is in respect of films with a completion date on or after 1 April 2006).

**“connected person”** is defined in section 1 and means –

- (a) In relation to a natural person –
  - (i) any relative; and
  - (ii) any trust of which such natural person or such relative is a beneficiary;
- (b) in relation to a trust –
  - (i) any beneficiary of such trust; and
  - (ii) any connected person in relation to such beneficiary;
- (bA) in relation to a connected person in relation to a trust (other than a collective investment scheme in property shares managed or carried on by any company registered as a manager under section 42 of the Collective Investment Schemes Control Act, 2002, for purposes of Part V of that Act), includes any other person who is a connected person in relation to such trust;
- (c) in relation to a member of any partnership –
  - (i) any other member; and
  - (ii) any connected person in relation to any member of such partnership;
- (d) in relation to a company –
  - (i) its holding company as defined in section 1 of the Companies Act, 1973 (Act No. 61 of 1973);
  - (ii) its subsidiary as so defined;

- (iii) any other company where both such companies are subsidiaries (as so defined) of the same holding company;
- (iv) any person, other than a company as defined in section 1 of the Companies Act, 1973 (Act No. 61 of 1973), who individually or jointly with any connected person in relation to himself, holds, directly or indirectly, at least 20% of the company's equity share capital or voting rights;
- (v) any other company if at least 20% of the equity share capital of such company is held by such other company, and no shareholder holds the majority voting rights of such company;
- (vA) any other company if such other company is managed or controlled by –
  - (aa) any person who or which is a connected person in relation to such company; or
  - (bb) any person who or which is a connected person in relation to a person contemplated in item (aa); and
- (vi) where such company is a closed corporation –
  - (aa) any member;
  - (bb) any relative of such member or any trust which is a connected person in relation to such member; and
  - (cc) any other close corporation or company which is a connected person in relation to –
    - (i) any member contemplated in item (aa); or
    - (ii) the relative or trust contemplated in item (bb); and
- (e) in relation to any person who is a connected person in relation to any other person in terms of the foregoing provisions of this definition; such other person.

**c) The costs must be paid within a certain period to qualify for the film allowance**

There must be a binding, unconditional obligation to pay the production and post-production costs within a period of 18 months from the date of completion. Failing this, the production and post-production costs will not qualify for a deduction under the film allowance. This requirement is applicable to any film with a completion date on or after 1 April 2006.

**Example 1**

*Facts:*

Company G completed filming in May 2006. It was contractually bound to make payment of production costs incurred by June 2007.

*Solution:*

Company G may claim the allowance in respect of production costs in the 2008 year of assessment.

**d) The film must be used in the production of income**

The deduction for the allowance is restricted to production and post-production costs incurred in the production of income or from which the film owner receives or accrues income. Thus, for example, the deduction for the film allowance does not apply to films or videos made for personal use or those made as a hobby.

### **Example 2**

*Facts:*

Taxpayer A, an individual, buys a video cassette recorder and starts making home movies as a hobby.

*Solution:*

Taxpayer A may not claim a deduction for the film allowance in respect of any costs that are incurred in making these home movies, as these costs have not been incurred in the production of the film owner's income.

**e) The film must be completed**

The film owner may only claim a deduction for the allowance for a film in the year of assessment in which that film is completed.

“**completion date**”, defined in section 24F means –

in relation to –

- (a) the production of a film, the date on which it is first in a form in which it can be regarded as ready for copies of it to be made and distributed, for presentation to the general public; or
- (b) the acquisition of a film, means the date it was acquired.

### **Example 3**

*Facts:*

In June 2006, Taxpayer B, an individual, purchased the rights to a screenplay for a feature film. In November 2006, Taxpayer B started filming. In December 2006, due to citing cost overruns and “creative differences”, Taxpayer B suspended work on the project indefinitely. On 28 February 2007 the film has still not been completed.

*Solution:*

Taxpayer B may not claim any deduction for a film allowance for any of the eligible costs incurred in respect of this film in the 2007 year of assessment, as the film has not yet been completed.

### **Example 4**

*Facts:*

In June 2006, Taxpayer C, an individual, purchased the rights to a screenplay for a feature film. Taxpayer C began filming in November 2006 and finished filming in February 2007. The answer print was completed in April 2007.

*Solution:*

In this instance, the completion date for the film occurred in the 2008 year of assessment. Therefore, Taxpayer C may not claim the film allowance for any portion of the expenditure for eligible costs incurred during the 2007 year of assessment. These costs may, however, be carried forward and deducted by Taxpayer C in the 2008 year of assessment (subject to the other requirements and limitations under section 24F).

### Example 5

#### Facts:

Company D is engaged in the production of feature films for commercial distribution and exhibition. During its 2007 year of assessment, Company D was engaged in three film projects. It completed the first two projects during that year and began their theatrical release. The third project just began filming prior to the end of the year and will not be completed until sometime in 2008.

#### Solution:

Company D may claim the deduction for the film allowance for its expenditure for eligible costs in respect of the first two films during its 2007 year of assessment. It may, however, not claim the deduction for the film allowance in respect of any eligible costs it incurred during that year for the third film. Those costs must be carried forward and may only be deducted by Company D in the year of assessment in which the completion date of that film falls (subject to the other requirements and limitations of section 24F).

### 2.2.2 Films completed prior to 1 April 2006

In light of the amendments to the film allowance, any film completed prior to 1 April 2006 will be subject to the provisions of section 24F as it appeared before that date. In this regard, film owners are advised to refer to the *Guide to the Taxation of Film Owners* dated November 2004.

### 2.2.3 The quantum of the film allowance

A film owner that complies with the above requirements may claim a film allowance, subject to certain limitations.

The amount of the allowance which may be granted for any one film is the sum of –

- in the year of assessment in which the completion date of the film falls, the production costs of such film and any post-production cost incurred during that year (production costs are therefore carried forward until the year of completion) provided that –
  - such costs have been paid other than by utilising a loan or credit;
  - where a loan or credit has been used by the film owner for the financing of the whole or any portion of such production cost or post-production cost and any portion of such loan or credit is owed by the film owner on the last day of the year of assessment, the film owner is deemed to be “at risk” in respect of such unpaid amount on the last day of the year of assessment; and
  - the South African activity limitation will be applicable in the case of any expenditure not relating to South African activities or co-production agreements; and
- in any subsequent year of assessment post-production cost incurred during that year of assessment, and the amount of –
  - any film allowance disallowed in the preceding year of assessment in terms of the “at risk” limitation which is discussed in paragraph **(a)** below; or
  - the film allowance allowable in that year of assessment according to the South African activity limitation which is discussed in paragraph **(b)** below.

In total the film allowance in respect of the film may not exceed the total production and post-production costs of such a film.

**a) The “at risk” limitation**

**(i) Basic concepts**

The film allowance is subject to the “at risk” limitation. This limitation is intended to counter “abusive” schemes that manipulate tax relief to create claims for losses in excess of the capital, if any, actually invested by a taxpayer in a film.

If a film owner uses a loan or credit to finance expenditure, and that loan or credit is still outstanding, in whole or in part, on the last day of the year of assessment, the film owner must reduce the amount of any film allowance deduction by any portion of that outstanding balance for which the film owner is deemed not to be “at risk”. Due to the proliferation of abusive tax schemes, the “at risk” limitation often involves complex technical issues. Some of these issues are discussed in more detail below.

In respect of the basic “at risk” concept, it may be useful to keep in mind the difference between recourse and non-recourse financing. In recourse financing the lender is typically entitled to repayment from the borrower even if the income from the financed project and/or the value of the assets acquired is insufficient to service the loan. By contrast, in non-recourse financing the lender is only entitled to repayment from the profits of the financed project and/or the value of the assets acquired - the lender has no “recourse” against the borrower or the borrower’s other assets.

**Example 6**

*Facts:*

Company H purchased film equipment of R100 000 for use in producing a feature film during its 2007 year of assessment. It finances the purchase of the film equipment in part with a recourse loan from Bank Y for R80 000. The loan is unconditionally payable in full in 2009 and Company H is liable for repaying it, regardless of the performance of the film or the value of the equipment.

*Solution:*

Under these circumstances Company H is deemed to be “at risk” in respect of the outstanding balance of R80 000 and may claim a deduction for the film allowance in the amount of R100 000 in the 2007 year of assessment. It is assumed for the purposes of this example that Company H has not entered into any other transaction, agreement, arrangement, understanding or scheme either before or after incurring the expenditure in question.

**Example 7**

*Facts:*

Company J purchased film equipment of R100 000 for use in producing a feature film during its 2007 year of assessment. It financed the purchase of the film equipment in its 2007 year of assessment with a non-recourse loan from Bank Z for R80 000, payable in 2009. In particular, Bank Z is only entitled to repayment from the profits, if any, from the film and/or the value of the film equipment, which has been pledged as security for the loan.

*Solution:*

Under these circumstances, Company J is not “at risk” in respect of the outstanding balance of R80 000 on the last day of the 2007 year of assessment. Consequently, the amount of the film allowance Company J may claim for that year is limited to R20 000. The remaining expenditure of R80 000 may be carried forward to future years of assessment and deducted only if and when the “at risk” limitation is met. This period is limited to 10 years after the completion of the film.

**(ii) Carry forward of disallowed amounts**

The amount of the film allowance that has not been allowed during a year of assessment due to the fact that the film owner was not “at risk” in respect of such an amount on the last day of the year of assessment, may be carried forward to the subsequent year(s) of assessment.

**(iii) When is a film owner deemed to be “at risk”?**

The “at risk” rule seeks to ensure that a deduction is only allowed to the film owner to the extent that the film owner is exposed to a real liability.

A film owner is deemed to be “at risk” only to the extent that the payment of expenditure incurred, or the repayment of a loan or credit used to finance expenditure, would result in an economic loss to the film owner were no income to be received by or accrue to the film owner in future years from the exploitation of the film.

The determination of whether, or to what extent, a film owner is “at risk” must be made having regard to any transaction, agreement, arrangement, understanding or scheme entered into before or after any expenditure has been incurred.

It has become clear that in a limited number of cases film owners are extending the period within which a loan or credit to finance production and post-production costs of a film is repayable for as long as possible. This has the effect of extending the period between which the expenditure is deducted and the date of settlement of the loan or credit.

Section 24F has, therefore, been amended to provide that with regard to any film with a completion date on or after 1 April 2006, the film owner will only be deemed to be “at risk” to the extent that the loan or credit is repayable within a period of 10 years from the completion date.

**(iv) When is a film owner not deemed to be “at risk”?**

There are situations where a film owner will not be deemed to be “at risk”. A simple example would be a situation in which the film owner finances the acquisition of certain equipment with a non-recourse loan. Another example would be a situation in which a taxpayer invests in the film through *en commandite* partnership. In such a partnership, the undisclosed partner’s liability is limited to the amount invested and such partner cannot be called upon to make any further contributions to the partnership should further debts be incurred by the partnership, thus the partner will only be “at risk” to the extent of the contribution.

Other examples of situations in which a film owner would be deemed not to be “at risk” include the following:

- The film owner’s liabilities would be waived or expunged if certain minimum sales targets are not reached;
- The film owner is reimbursed for part or all of the losses as a result of a binding contract or stop-loss agreement between the film owner and any other person (the film owner is only “at risk” for the portion of capital for which he is not entitled to reimbursement); or
- The payment of costs is guaranteed in whole or in part by a third party.



### **Example 8**

#### *Facts:*

Taxpayer K, an individual, enters into an arrangement with Producer P and Bank Z. As part of this arrangement, Taxpayer K enters into a recourse loan with Bank Z in order to finance the acquisition of a film from Producer P. The loan is repayable, in full, at the end of 10 years. As part of the same arrangement, Taxpayer K and Producer P also enter into a side agreement, either directly or through one or more accommodating parties, pursuant to which Producer P (or an accommodating party) agrees to repurchase the film in 10 years for an amount that is equal to or greater than the amount of the loan, without regard to the actual performance of the film or to its actual market value.

#### *Solution:*

In this situation, while the recourse nature of the loan might, in isolation, give rise to an impression that Taxpayer K would suffer an economic loss were no income to be derived from the exploitation of the film (since the repayment of the loan would then have to be financed out of the investor's own resources), the repurchase agreement ensures that the investor will immediately, at a minimum, be made whole for any amount due under the loan. Thus Taxpayer K is not exposed to any economic liability and deemed not to be at risk. The repurchase of the film involves a transaction of a capital nature and, therefore, does not result in income from the exploitation of the film.

### **b) South African activity limitation**

Subject to the "at risk" limitation, the amount of the film allowance will be as follows:

- The total amount of all production costs and post-production costs if at least 75% of the total costs incurred is paid or payable in the Republic in respect of services rendered or goods supplied in the Republic;
- The total amount of all production costs and post-production costs actually incurred where the film is approved as a co-production in terms of an agreement on audiovisual or film co-production between the South African government and any other government; and
- In any other case, so much of any production costs or post-production costs actually incurred as is paid or payable in the Republic in respect of services rendered or goods supplied in the Republic.

Any production costs or post-production costs incurred that does not relate to South African activities or co-production agreements are, however, allowed on a straight line basis over a period of 10 years. The deduction is limited to –

- 10% in the year of assessment during which the film is completed and
- 10% in each of the nine following years of assessment.

This limitation provision is applicable to any film with a completion date on or after 1 April 2006.

It is apparent from the above that the allowance favours film owners who have incurred production costs or post-production costs which are paid or payable in the Republic or who have entered into a co-production agreement.

### **Example 9**

*Facts:*

Taxpayer A, a film owner, incurs production costs and post-production costs of R100 000 on a film. Of this amount, R60 000 relates to expenditure in South Africa in respect of services rendered and goods supplied, and the balance of R40 000 relates to expenditure in a foreign country.

*Solution:*

Taxpayer A may not claim the total costs of R100 000 as a deduction in the year of assessment when the film is completed as the costs attributed to the Republic is less than the minimum of 75%. He may claim R60 000 in the year of assessment when the film is completed and the balance may be written off as follows: R4 000 in the year of assessment when the film is completed and R4 000 per year in the nine years thereafter.

### **Example 10**

*Facts:*

Taxpayer B, a film owner, has entered into a co-production in terms of an agreement with Italy.

*Solution:*

Taxpayer B may claim a deduction for the total production and post-production costs incurred in the year of assessment when the film is completed.

### **c) Actual cost limitation**

The film allowance in respect of a film may not in the aggregate exceed the total production and post-production cost actually incurred by the film owner in respect of that film. The film allowance, moreover, is granted in lieu of any deduction or allowance in respect of expenditure for eligible costs which may otherwise be allowable in terms of the provisions of the Act.

Subject to the "at risk" rule, the allowance may be claimed either when the expense is incurred or when it is paid and may not be claimed twice. Should an expense be financed, the allowance may only be claimed when that expense is incurred or paid and not again once the finance has been paid.

### **Example 11**

*Facts:*

Company C paid R100 000 for film equipment for use in producing a feature film during its 2006 year of assessment. It began filming immediately but didn't complete the film until the following year.

*Solution:*

Company C may not claim the film allowance in respect of its expenditure for the film equipment during its 2006 year of assessment. It must carry the entire amount forward to its 2007 year of assessment. Company C, moreover, may neither claim any allowance for wear and tear in respect of the equipment under section 11(e) of the Act, nor may it claim any other deduction or allowance that might otherwise be allowable for expenditure for such equipment in terms of any provision of the Act.

### **Example 12**

*Facts:*

Company D purchased film equipment of R80 000 for use in producing a film during its 2006 year of assessment, which was payable in its 2007 year of assessment. In addition the expense was financed by a loan of R90 000 which was payable in full during its 2008 year of assessment (R80 000 capital and R10 000 finance costs).

*Solution:*

In the 2006 year of assessment, Company D may claim R80 000 for the costs incurred in respect of the film equipment and R10 000 for the finance charges incurred, provided that Company D is regarded to be at risk in respect of such costs. Company D may then not claim the same amount again in the 2007 or 2008 year of assessment when the loan is repaid.

In any year of assessment the film allowance in respect of any one film, together with the total of the film allowance granted for that film in preceding years of assessment may not exceed the sum of –

- production costs and post-production costs paid by the film owner provided that where the film owner has used a loan or credit for the payment or financing of the whole or part of the costs and any portion thereof is owed by the film owner on the last day of the year of assessment, the amount that may be taken into account will be reduced by that portion owed by him for which he is not deemed to be at risk on the last day of the year of assessment; and
- the amount of any production costs and post-production costs that the film owner has not paid and for which he is deemed to be at risk on the last day of the year of assessment.

#### **2.2.4 How does the film owner claim the allowance?**

The film owner must complete and submit an annual tax return at the end of each year of assessment. The total film allowance claimed for that year must be disclosed and any part of the income tax return that contains questions relating to this allowance must be completed. A schedule of these expenses must be kept for audit purposes.

### **2.3 ABUSE OF THE FILM ALLOWANCE**

Unfortunately, South Africa has experienced some instances in which taxpayers have attempted to abuse the deductions under section 24F. Similar attempts have also arisen in other countries that had tried to assist their local film industries through similar allowances, including Australia, New Zealand and the United Kingdom. Not surprisingly, these abuses prompted a crack down by the local revenue authorities and in some cases forced those countries to withdraw or restrict the allowances in question.

These abusive schemes can take a number of different forms, but typically involve the formation of a partnership comprised of high net worth South African residents. A common example involves a purported sale and leaseback of so-called “film rights” between a film’s producers and such a partnership.

These abusive schemes generally have a number of common features, including one or more of the following:

- The payment of an inflated or non-arm's length price for the acquisition of so-called "film rights";
- A high level of gearing or leverage by the partnership;
- A circular flow of funds (in which the proceeds from the loan used to gear or leverage the partnership's "investment" in the so-called "film rights" flow back to the lender itself, or a connected person to that lender or the film's producer, or to an accommodating party) and are used to fund or "guarantee" the payments due under the purported "lease" or "licence back" arrangement;
- The absence of commercial film risk for the partnership and/or partners; or
- A pre-tax return to the partnership that is only a fraction of the after-tax return to the partners, after taking the anticipated film allowance into account.

The recent amendments to section 24F have largely been introduced to prohibit these kinds of abusive schemes or transactions.

Schemes or transactions that have the effect of avoiding or postponing the liability for tax will be closely scrutinised by the Commissioner of SARS. The tax consequences of any impermissible tax avoidance arrangements will be determined by the Commissioner in terms of section 80B of the Act.

#### **Example 13**

*Facts:*

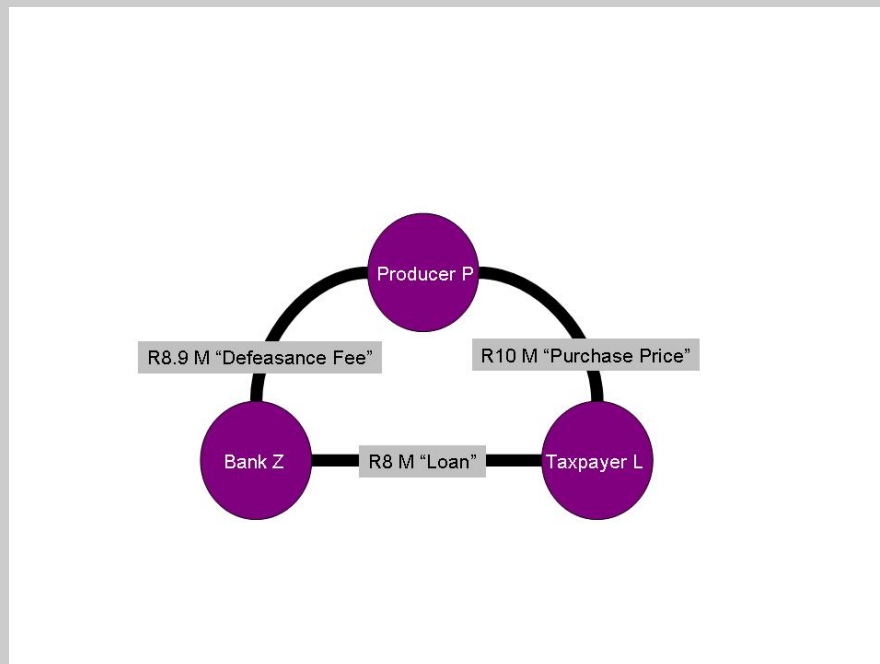
Taxpayer L, a high net worth South African resident, entered into a complex arrangement with Producer P and Bank Z. Pursuant to this arrangement, Producer P purported to "sell" certain "film exploitation rights" to Taxpayer L. These "film rights" are in fact subordinate to primary exploitation rights for the film that have already been sold to *bona fide* distributors in all the major potential markets for the film. Despite the limited value of these subordinated rights, the purchase price was arbitrarily set at R10million, the total amount of the production and post-production costs for the film.

As part of the same arrangement, Taxpayer L also entered into what purports to be an R8million loan with Bank Z in order to "finance" the "acquisition" of the subordinated "film rights" in question. The full principal amount of this loan is repayable at the end of 10 years.

Also as part of the same arrangement, Producer P entered into an agreement with Taxpayer L pursuant to which Producer P agreed, either directly or through one or more accommodating parties, to immediately licence back the subordinated "film rights" in exchange for a licence fee approximately equal to the carrying charges on Taxpayer L's loan with Bank Z. Producer P also entered into a second agreement with Taxpayer L pursuant to which Taxpayer L agreed to sell, and Producer P agrees, either directly or through one or more accommodating parties, to repurchase the subordinated "film rights" for R8,9million at the end of 10 years, without regard to the actual performance of the film or the actual market value of the subordinated "film rights".

Finally, as part of the same arrangement, Producer P entered into an agreement with Bank Z pursuant to which Producer P purported to "pay" R8,9million to Bank Z in exchange for Bank Z's assumption of Producer P's obligations to Taxpayer L under the "license back" and "repurchase" agreements (in addition, Producer P also may pay Bank Z a fee for structuring the transaction).

**Diagram: Circular Cash Flow in an Abusive Film Scheme**



*Solution:*

The transaction in question contains all of the features common to abuse film schemes:

- Taxpayer L paid an inflated, non-arm's length price for the subordinated film rights;
- Taxpayer L's investment is highly leveraged, with a 4 to 1 debt/equity ratio;
- There is a circular flow of funds among the parties to the transaction, with the loan proceeds moving from Bank Z through Taxpayer L and Producer P and back to Bank Z all on the same day;
- Taxpayer L bears no commercial risk in connection with the film itself; and
- The pre-tax return to Taxpayer L is only a fraction of Taxpayer L's after-tax return, after taking into account the anticipated film allowance. In particular, the pre-tax return to Taxpayer L consists of the minimal difference between the "licence" fee payable by Producer P and the carrying charges on the purported loan with Bank Z. More importantly, Taxpayer L has actually locked itself into a pre-tax capital loss of R1,1million in connection with the subordinated "film rights", being the difference between the R10million purchase price and the R8,9million price under the "repurchase" agreement. By contrast, the after-tax return to Taxpayer L would take into account the anticipated film allowance of R4million (R10million x 40%), an amount equal to twice Taxpayer L's purported "equity" investment in the "film rights".

The Commissioner will disallow the entire film allowance claimed by Taxpayer L. Taxpayer L will *inter alia* also be subject to 200% additional tax under section 76 of the Act.

## PART B: OTHER TAXES/DUTIES/LEVIES/CONTRIBUTIONS

Film owners are also liable for other taxes, duties, levies and contributions administered by SARS.

### 3. EMPLOYMENT INCOME RELATED TAXES/LEVIES/CONTRIBUTIONS (PAYE, SDL AND UIF)

A film owner who is an employer will be obliged to withhold employees' tax in the circumstances where such film owner pays remuneration to an employee. Such film owner could also be obliged to pay a Skills Development Levy (SDL) and to make contributions to the Unemployment Insurance Fund (UIF) in respect of such remuneration paid or payable to any employee. Details about the payment of such amounts are set out below.

#### 3.1 EMPLOYEES' TAX (PAYE)

##### 3.1.1 Employers are liable to withhold employees' tax in respect of all remuneration paid/payable to employees

A film owner is required to withhold employees' tax from any amount payable to another person where the following three elements are present: employer, employee and remuneration. The employment contract that is entered into by the person rendering a service and the person making a payment will determine whether these three elements are present.

It often happens in the film industry that artists, models and crew members are introduced to film makers by agents. Employment contracts are entered into between the artists, models or crew members and the film owner and an introduction fee is payable to the agent. The fees due to the artists, models or crew members are sometimes paid over to the agents who are requested to deduct their fees and employees' tax before the net amounts are paid over to the artists, models or crew members. It is important to note that despite such an agreement with an agent, the film owner that employs the artists, models or crew members is still obliged to ensure that employees' tax are paid over to SARS in respect of such amounts paid and that the relevant employees' tax certificates are issued.

A film owner that is obliged to withhold and pay over employees' tax must register as an employer for these purposes at SARS. The amount to be withheld should be determined in accordance with the tax deduction tables that can be found in the *Guidelines for Employers* which is available on the SARS website [www.sars.gov.za](http://www.sars.gov.za) and can also be obtained from SARS branches.

An employer, employee and remuneration are defined in paragraph 1 of the Fourth Schedule as:

**“employer”** means –

any person (excluding any person not acting as a principal, but including any person acting in a fiduciary capacity or in his capacity as a trustee in an insolvent estate, an executor or an administrator of a benefit fund, pension fund, provident fund, retirement annuity fund or any other fund) who pays or is liable to pay to any person any amount by way of remuneration, and any person responsible for the payment of any amount by way of remuneration to any other person under the provisions of any law or out of public funds (including the funds of any provincial council or any administration or undertaking of the State) or out of funds voted by Parliament or a provincial council.

**“employee”** means –

- (a) any person (other than a company) who receives remuneration or to whom any remuneration accrues;
- (b) any person who receives any remuneration or to whom any remuneration accrues by reason of any services rendered by such person to or on behalf of a labour broker;
- (c) any labour broker;
- (d) any person or class or category of person whom the Minister of Finance by notice in the *Gazette* declares to be an employee for the purpose of this definition;
- (e) any personal service company;
- (f) any personal service trust; and
- (g) any director of a private company who is not otherwise included in terms of paragraph (a).

**“remuneration”** means –

any amount of income which is paid or payable to any person by way of salary, leave pay, wage, overtime pay, bonus, gratuity, commission, fee, emolument, pension, superannuation allowance, retiring allowance or stipend, whether in cash or otherwise and whether or not in respect of services rendered ...but not including –

- (ii) any amount paid or payable in respect of services rendered or to be rendered by any person (other than a person who is not a resident or an employee contemplated in paragraph (b), (c), (d), (e) or (f) of the definition of “employee” ) in the course of any trade carried on by him independently of the person by whom such amount is paid or payable and of the person to whom such services have been or are to be rendered: Provided that for the purposes of this paragraph a person shall not be deemed to carry on a trade independently as aforesaid–
  - (aa) if he is subject to the control or supervision of any other person as to the manner in which his duties are performed or to be performed or as his hours of work; or
  - (bb) if the amounts paid or payable for his services consists of or include earnings of any description which are payable at regular daily, weekly, monthly or other intervals.

The following amounts paid or payable to an employee are, for example, regarded as remuneration:

- Salary, overtime fee, bonus, wage, leave gratuity;
- 60% of a travel allowance;
- Commission; and
- Restraint of trade compensation

The following amounts are, for example, not regarded as remuneration:

- Amounts paid or payable to an employee for reimbursement of business expenses incurred, that is, expenses incurred on behalf of the employer on an agency basis in the course of his or her employment; and
- Amounts paid or payable to common law independent contractors who are not subject to control or supervision of any person as to the manner in which their duties are performed or as to the hours of work and to whom the amounts paid or payable are not payable at regular daily, weekly, monthly or other intervals.

Any film owner that, as an employer or a representative employer pays remuneration to an employee is obliged to withhold employees' tax from such amount and pay it over to SARS within seven days after the end of the month during which the amount was deducted or withheld. Failure to make such payments within the prescribed periods will be regarded as an offence and will result in the payment of penalties and interest at the prescribed rate of interest. The film owner is also responsible for issuing employees' tax certificates (IRP 5s) for amounts deducted from employees in respect of employees' tax.

Further information regarding the employer/employee relationship and the deduction of PAYE in the case of independent contractors can be obtained in Interpretation Note No. 17 and the *Guide on the Employees' Tax Responsibilities with regard to artists/models/crew in the Film Industry* that is available on the SARS website [www.sars.gov.za](http://www.sars.gov.za) and can also be obtained from SARS branches.

### **3.1.2 Employees' tax is not deductible in respect of labour brokers that have exempt status**

Film owners often enter into agreements with labour brokers in terms of which the labour brokers provide artists, models or crew members to the film owners.

A “**labour broker**”, defined in the Fourth Schedule to the Act means –

any person who for reward provides a client of such business with other persons to render a service or perform work for such client, or procures such other persons for the client, for which services or work such other persons are remunerated by such person.

Agents often also act as labour brokers. All payments made to labour brokers are also subject to employees' tax since they are “employees”, as defined. Labour brokers may, on an annual basis, apply to the Commissioner for exemption certificates (IRP 30s) in this regard. It is, however, important to examine the employment contract or other contracts to determine the relationship between the artist/model/crew member, the film owner and the agent in order to determine whether the agent complies with the above-mentioned definition of a “labour broker”.

Where film owners have entered into agreements with agents to provide artists, models or crew members to the film owners and IRP 30s have been issued to such agents, the film owners will not be obliged to deduct employees' tax from any payments made to such agents or in respect of the artists, models or crew members provided by such agents. In these instances artists, models or crew members are not employees of the film owners, but are employees of the agents and the agents would be responsible for the deduction of employees' tax from amounts paid or payable to the artists, models or crew members and the issuing of the relevant employees' tax certificates.

Further information regarding labour brokers in the film industry can be obtained in the *Guide on the Employees' Tax Responsibilities with regard to artists/models/crew in the Film Industry* that is available on the SARS website [www.sars.gov.za](http://www.sars.gov.za) and can also be obtained from SARS branches.



### **3.1.3 Employees' tax is not deductible from amounts payable to certain foreign entertainers**

Employees' tax should not be withheld from any amounts payable to a foreign entertainer in respect of any activity exercised in the Republic as an entertainer, unless the foreign entertainer –

- is an employee of a film owner that is a resident; **and**
- is physically present in the Republic for a period or periods exceeding 183 days in aggregate during any 12-month period commencing or ending during the year of assessment in which an activity is exercised by the person as an entertainer,

as the foreign entertainer would be subject to 15% Withholding Tax on Foreign Entertainers in this regard.

Please see paragraph 9 of this guide for more information regarding the obligation of film owners to pay over Withholding Tax on Foreign Entertainers with regard to amounts paid to foreign entertainers.

### **3.2 SKILLS DEVELOPMENT LEVIES (SDL)**

As an employer, a film owner is also obliged to pay skills development levies amounting to 1% of any remuneration paid or payable to an employee, unless the employer is exempt from such payment, for example, where the total remuneration payable to all its employees during a determined 12-month period does not exceed R500 000.

Skills development levies are, however, not payable in respect of, for example, remuneration payable by way of pension, lump sum payments from annuity or pension funds and amounts payable to learners in terms of registered learnership agreements. The remuneration in respect of employees earning below the threshold is also taken into consideration for the purposes of calculating the SDL.

The levies must be paid to SARS not later than seven days after the end of the month in respect of which the levies are payable. Failure to make such payments within the prescribed periods will be regarded as an offence and will result in the payment of penalties and interest at the prescribed rate of interest. Further information regarding skills development levies is available on the SARS website [www.sars.gov.za](http://www.sars.gov.za) and can also be obtained from SARS branches.

### **3.3 UNEMPLOYMENT INSURANCE FUND CONTRIBUTIONS (UIF)**

As an employer, a film owner is also obliged to make contributions to the Unemployment Insurance Fund in respect of the remuneration paid or payable to an employee and to pay over any such contributions deducted or withheld from the employee for purposes of UIF.

Unemployment insurance contributions are, however, not payable on remuneration paid or payable by way of any pension, superannuation, annuity, compensation for restraint of trade, termination or loss of employment, lump sum from pension, provident or retirement annuity fund, or commission.

The UIF is calculated based on the gross remuneration before the deduction of pension fund and retirement annuity fund contributions and, where the employee is older than 65 years, medical aid contributions.

The employer must pay over a total contribution of 2% of the total remuneration paid or payable to the employees, of which 1% must be deducted from the employees' remuneration.

Where an employer is registered at SARS for employees' tax or skills development levies purposes, the amounts must be paid over to SARS not later than seven days after the end of the month in respect of which the contributions should be made. Where an employer is, however, not registered at SARS for employees' tax or skills development levies purposes, the amounts must be paid over to the Unemployment Insurance Commissioner not later than seven days after the end of the month in respect of which the contributions should be made.

Failure to make such payments within the prescribed period will be regarded as an offence and will result in the payment of penalties and interest at the prescribed rate of interest.

#### **4. VALUE-ADDED TAX (VAT)**

A film owner will in certain circumstances, as a supplier of goods and/or services, be required to register as a vendor for VAT purposes and to pay the balance of output tax to SARS after deducting as a credit the amount of input tax incurred for supplies received for the tax period concerned.

##### **4.1 WHEN MUST A FILM OWNER REGISTER FOR VAT?**

The VAT Act requires any film owner who carries on an enterprise to register as a vendor if the turnover of taxable supplies of that film owner exceeds R300 000 within any consecutive 12-month period or where there is reason to believe that turnover in the next 12 months will exceed R300 000. A person can also register voluntarily if turnover in a 12-month period has exceeded or is likely to exceed R20 000.

An “**enterprise**” is defined in the VAT Act as –

in the case of a vendor other than a local authority, any enterprise or activity which is carried on continuously or regularly by any person in the Republic or partly in the Republic and in the course or furtherance of which goods or services are supplied to any other person for a consideration, whether or not for profit, including any enterprise or activity carried on in the form of a commercial, financial, industrial, mining, fishing or professional concern or any other concern of a continuing nature or in the form of an association or club.

Royalties or other income of film owners as a result of, or in connection with, the rights from a film (or any other taxable supplies) will fall into the scope of “consideration”. If the consideration is earned in the course of conducting an enterprise, that film owner may be liable to register for VAT. Similarly, any supplier whose total taxable supplies in a 12-month consecutive period exceed the R300 000 registration threshold should charge VAT on supplies made to a film owner.

A partnership or joint venture is regarded as a “person” for VAT purposes. An enterprise which is carried on in the form of a partnership or joint venture may, therefore, also be liable to register and account for VAT.

##### **4.2 VAT RATES AND TYPES OF SUPPLIES**

VAT is calculated at two rates, namely a standard rate of 14% and a zero (0%) rate, depending on the nature of the supply.

Examples of consideration received in respect of taxable supplies that are subject to VAT at 14% are the following:

- Income which relates to the exploitation of the rights pertaining to the film of any kind and activities taking place in the Republic, for example, box office sales, royalties, video sales, distribution fees and sale of screening rights or copyrights;
- Rental income from assets leased to other persons in the Republic; and
- Sale or disposal of assets acquired to make a film after the film has been completed, for example, sale of the lighting and sounding equipment.

Examples of consideration received in respect of taxable supplies that are subject to VAT at 0%, are the following:

- Consideration received in respect of the supply of the intellectual property rights, where and to the extent that it is for the use of those rights outside the Republic;
- Fees for services physically performed outside the Republic;
- The physical exportation of the film or other goods from the Republic;
- Consideration received for filming, producing and other services performed in South Africa for a person who is not a resident in the Republic, not a registered vendor or not in the Republic at the time when the services are rendered; and
- Grants or subsidies received from the public or local authority for the making of a film (except for the making of a film for the use of such authority).

Both these rates are levied on supplies known as “taxable supplies”.

A “**taxable supply**” is defined in the VAT Act as follows –

any supply of goods or services which is chargeable with tax under the provisions of section 7(1)(a), including tax chargeable at the rate of zero per cent under section 11.

There is also a limited range of goods which are exempt from VAT, for example, the supply of financial services and the letting of land outside South Africa. These are commonly known as exempt supplies. The main difference between zero and exempt supplies is that registered vendors are not allowed to claim input tax on goods and services acquired to make exempt supplies. On the other hand, input tax may be claimed on goods and services acquired to make zero rated supplies. If a person only makes exempt supplies he cannot be registered as a vendor.

#### **4.3 TAX PERIODS AND PAYMENT OF VAT TO SARS**

Film owners that are vendors are required to pay over the tax that they charge on taxable supplies (known as output tax) to SARS at the end of each tax period. They are entitled to claim back the tax charged on them (known as input tax) for the purchasing of goods or services to produce taxable supplies. Most vendors pay VAT over every month or bi-monthly, depending on the taxable turnover and the requirements of that vendor.

Failure to make such payments within the prescribed periods will be regarded as an offence and will result in the payment of a penalty of 10% and interest at the prescribed rate. On the other hand, where any amount is refundable to the vendor, interest at the prescribed rate will be payable by the Commissioner.

#### **4.4 ON WHICH AMOUNTS MAY FILM OWNERS CLAIM VAT (INPUT TAX)?**

Except for a few exclusions, input tax may be claimed by a film owner on any expenses that include VAT at the standard rate which have been incurred for purposes of making taxable supplies, for example, the production of a film.

The following are examples of VAT inclusive expenses on which input tax may be claimed:

- Marketing and advertising expenses;
- Capital expenses such as cameras, sound and lighting equipment;
- Service fees and commission for agents, designers and promoters who are registered for VAT;
- Film, stage props, clothing and other consumables;
- Royalties paid for the use or outright purchase of copyrights from other VAT registered film owners in South Africa for use in the country; and
- Transport cost such as airfare for the production staff and movement of production equipment between shooting locations.

The following are examples of expenses on which input tax may not be claimed:

- Petrol, diesel and other supplies where VAT has not been included in the consideration at the standard rate;
- Expenses which are incurred for private (non-enterprise) purposes or for the purpose of making exempt supplies;
- Salaries and wages of employees who earn remuneration;
- The acquisition of a motor car (including acquisition by means of rental, hire, instalment sale and financial lease);
- Club subscriptions of a recreational nature, for example country club membership fees; and
- Expenses relating to entertainment, unless the vendor is in the business of continuously or regularly supplying entertainment in the ordinary course of that enterprise at a charge which covers all the direct and indirect costs (or open market value) of making the supply.

Further information regarding the registration and payment of VAT is available on the SARS website [www.sars.gov.za](http://www.sars.gov.za) and can also be obtained from SARS branches.

## **5. CUSTOMS DUTIES**

A film owner could be liable for the payment of customs duties when goods are imported. Such a person may enter the Republic at any appointed place of entry and all goods in the film owner's possession must be declared to a customs official at the port of entry. When dutiable goods are in the possession of the film owner, the relevant duties and VAT must be paid thereon. Customs duties are usually calculated on the value of the goods, but certain goods attract specific rated duties where the duty is based on the quantity of goods imported.

Non-resident film owners and film producers have two options of importing their film-making equipment into the Republic free from customs duties and VAT, which are briefly discussed below.

## **5.1 CUSTOMS DECLARATION - NON RESIDENTS**

### **5.1.1 Customs rebate for goods temporarily admitted for specific purposes**

Schedule 4 to the Customs and Excise Act, 1964 contains provisions for a full customs rebate in respect of goods temporarily admitted for specific purposes. The rebate in respect of the temporary admission of film-making equipment is contained under the provisions of Rebate Item 480.15. This rebate item provides for a full rebate of customs duty in respect of professional equipment (including ancillary apparatus and accessories) owned by non-residents and which would otherwise be dutiable in terms of Schedule 1, Part 1 or 2, of the Customs and Excise Act. This equipment must be used solely by or under the supervision of the non-resident.

The equipment would have to be clearly identifiable and would go through the normal Customs clearing route. It would have to be re-exported through the same procedure within six months from the date of entering the Republic. The Commissioner may require security to be lodged in order to cover the duty applicable to such equipment, and this is refunded after the goods have been re-exported.

### **5.1.2 Agreement on Temporary Admission Carnet (ATA Carnet)**

The ATA Carnet is an international Customs document that is accepted as a Customs declaration for a specified period. This document is approved by member countries who are signatories to the Convention on Temporary Admission - The Istanbul Convention (26 June 1990), as well as the Customs Convention on the ATA Carnet for Temporary Admission of Goods - The ATA Convention (18 December 1975).

The ATA Carnet serves as an internationally valid cover for import duties and taxes on specified goods. The owner of the film equipment has to register the goods to be imported into the Republic with a Chamber of Commerce in his resident country in order to obtain an ATA Carnet in respect of the equipment. The ATA Carnet simplifies the temporary importation of goods into the Republic and there is no additional security required. The equipment can, then, remain in the Republic for the validity period of the ATA Carnet, not exceeding one year.

## **5.2 CUSTOMS DECLARATION - RESIDENTS**

There is no special Customs rebate available for goods temporarily admitted for specific purposes for residents and they cannot make use of an ATA Carnet either. However, the Commissioner may grant permission for temporary admission of goods duty-free, provided that the goods would be re-exported in the same state. These provisions are contained in Rebate Item 490.90 for goods not specified elsewhere in other rebate items relating to the temporary admission of goods. Therefore, residents wishing to temporarily import filmmaking equipment without payment of customs duty may apply to the Commissioner for permission to admit such equipment in terms of the abovementioned Rebate Item. Failure to do so will lead to full payment of customs duty and VAT on the admitted goods.

Further information on Customs duties is available on the SARS website [www.sars.gov.za](http://www.sars.gov.za) and can also be obtained from SARS branches.

## 6. EXCISE DUTIES

A film owner could be liable for the payment of excise duties.

Excise duties (based on the specific quantity or volume of the product) are levied on certain locally manufactured products and counter-veiling duties equal to the specific excise duties are levied on their imported counterparts. These duties are levied as specific duties on certain items such as tobacco products, liquor products, petroleum products and hydro-carbons. The excise duties are included in the purchase price of the goods.

Ad Valorem Excise Duty (based on the value of the product) is levied on various goods such as cosmetics, television receptors and audio equipment. For example, an excise duty of 7% is payable in respect of television sets, video recording machines, video tape duplicators, still image video cameras and digital cameras.

As liability for excise duty is based on consumption within the local country borders, relief from excise duty in the form of full rebates is granted where excisable products are exported.

## 7. DONATIONS TAX

A resident film owner could be liable for the payment of donations tax. Donations tax is, unlike other taxes, not imposed on income, but on the transfer of assets or wealth. The purpose of donations tax is to discourage the avoidance of tax and estate duty by the distribution of assets to other persons.

A donation and property are defined in section 55 as follows:

**“donation”** means –

any gratuitous disposal of property or any gratuitous waiver or renunciation of a right.

**“property”** means –

any right in or to property whether movable or immovable, corporeal or incorporeal (tangible or intangible), wheresoever situated.

Donations tax is payable by the donor on the value of any property disposed of under a donation at a rate of 20%. Where property is disposed of by a film owner for an inadequate amount, a “deemed donation” is regarded to have taken place.

Donations made by a film owner that is a natural person are exempt up to an amount of R100 000 with effect from 1 March 2007 and in respect of a film owner that is not a natural person (for example, a trust or company) up to an amount of R10 000 per year of assessment.

Donations tax must be paid within three months, or such longer period as the Commissioner of SARS may allow, from the date upon which the donation has taken effect. A donor and the donee are jointly and severally liable for the tax. Failure to pay the donations tax within the prescribed period will be regarded as an offence and will result in the payment of penalties and interest at the prescribed rate of interest.

## 8. WITHHOLDING TAX ON ROYALTIES

A resident film owner will be responsible to withhold and pay over a final withholding tax of 12% in respect of royalties or similar payments made to non-resident film owners for the right of, or the granting of permission for use in the Republic –

- certain patents, designs, trademarks, copyright, models, patterns, plans, formulas or processes or any property or right of a similar nature; or
- any motion picture film, or any film or video tape or disc for use in connection with television, or any sound recording or advertising matter used or intended to be used in connection with such motion picture film, film or video tape or disc. Such tax must be paid over to SARS within 14 days after the end of the month during which the liability to pay the royalty was incurred.

No final withholding tax should, however, be withheld from any amount of royalty that is received by or accrues to any –

- company which is not a resident, if the amount is derived by the company from a trade carried on through a branch or agency in the Republic and the amount is subject to tax in the Republic; or
- person (other than a person whose place of residence is in a neighbouring country) in respect of the use in any printed publication of any copyright as aforesaid, unless it is used for advertising purposes in connection with any motion picture or film or in connection with television.

Failure to withhold and pay over such tax within the prescribed period will be regarded as an offence and will result in the payment of penalties and interest at the prescribed rate of interest.

## 9. WITHHOLDING TAX ON FOREIGN ENTERTAINERS

The tax payable by a foreign entertainer is a final tax levied at the rate of 15% on the amount received by or accrued to any person who is not a resident, in respect of any activity exercised in the Republic by that person as an entertainer.

A foreign entertainer includes any person who for reward –

- performs any activity as a theatre, motion picture, radio or television artiste or a musician;
- takes part in any activity which is usually regarded as of an entertainment character.

The tax is not applicable if the foreign entertainer is an employee of an employer who is a resident **and** is physically present in the Republic for a period or periods exceeding 183 full days in aggregate during any 12-month period commencing or ending during the year of assessment in which the activity is exercised. The foreign entertainer would then be subject to taxes in accordance with the legislation applicable to residents.

If an amount is paid by a resident film owner to the foreign entertainer, the resident film owner is obligated to withhold the tax from the payments made and pay over that tax before the end of the month following the date of withholding. Failure to do so will result in the film owner being held personally liable for the amount of the tax unless the foreign entertainer has already paid over the tax.

A resident film owner who has not withheld the tax from the foreign entertainer and pays the tax in his personal capacity, may recover the amount of the tax from the foreign entertainer.

If an amount is paid by a non-resident film owner, the obligation to pay the tax rests on the foreign entertainer and such tax must be paid over within 30 days.

A film owner who is primarily responsible for founding, organising or facilitating the activity of the foreign entertainer in the Republic and who will be rewarded directly or indirectly for it, must notify the Commissioner within 14 days of that activity being concluded and provide details, if so requested by the Commissioner.

Further information regarding the taxation of foreign entertainers can be obtained from the SARS *Non-Resident Entertainers and Sportspersons Team* on e-mail: [nres@sars.gov.za](mailto:nres@sars.gov.za).

## 10. TRANSFER DUTY

A film owner will be liable for the payment of transfer duty on acquisition of any property (land, buildings and certain real rights). All transactions relating to a taxable supply of goods and subject to VAT are, however, exempt from transfer duty.

Transfer duty is calculated as follows:

ENTITY	FAIR VALUE*	RATE
Natural Persons	On the first R500 000 of purchase consideration	0%
	On the amount that exceeds R500 000 but not R1 000 000	5% on the value above R500 000
	On the amount that exceeds R1 000 000	R25 000 plus 8% on the value above R1 000 000
Companies & Trusts	On purchase consideration	8%

\*Fair value is usually the purchase price.

Failure to pay transfer duty within the prescribed period will be regarded as an offence and will result in the payment of penalties and interest at the prescribed rate of interest..

Further information regarding the payment of transfer duty is available on the SARS website [www.sars.gov.za](http://www.sars.gov.za) and can also be obtained from SARS branches.



## **PART C: GENERAL (INCOME TAX)**

The following general administrative provisions of the Act are, for example, also applicable to film owners:

### **11. REGISTRATION AS A TAXPAYER**

Any resident that carries on a trade as a film owner in the Republic or in a foreign country, or non-resident that carries on a trade as a film owner in the Republic, is obliged to register as a taxpayer at SARS within 60 days after commencement of such trade.

### **12. CHANGE OF ADDRESS**

A registered taxpayer will be required to notify SARS of any change of address within 60 days of such change.

### **13. SUBMISSION OF INCOME TAX RETURNS**

A film owner like any other registered taxpayer is required to submit an income tax return within a prescribed period after the end of each year of assessment. Late submission or failure to do so is an offence punishable by the imposition of fines, penalties and additional taxes.

### **14. YEAR OF ASSESSMENT**

The year of assessment of a film owner that is a natural person or a trust will commence on 1 March of a year and end on 28 or 29 February of the following year.

The year of assessment of a film owner that is a company or close corporation will for tax purposes be the same as its financial year for accounting purposes. Should the year of assessment of a company or close corporation change for accounting purposes, the Commissioner of SARS needs to approve a change in the financial year of the company for tax purposes.

### **15. FILM OWNERS ARE PROVISIONAL TAXPAYERS**

Film owners must register as provisional taxpayers, as they derive income from a trade (in the case of a company this will be done automatically upon registration). Income from carrying on a trade does not constitute "remuneration" and is, therefore, not subject to employees' tax.

Provisional tax is not a separate tax, but simply a provision for the final tax liability of a person for a particular year of assessment. All provisional tax payments made during a year of assessment will be allowed as a credit when a person's normal tax liability is determined in respect of that year of assessment. Failure to pay provisional tax may lead to the imposition of interest and penalties.

Two provisional tax payments must be made by a film owner during a year of assessment as follows:

- Where a film owner is a natural person or trust, at the end of August and February; and
- Where a film owner is a company or close corporation, the first payment must be made six months before its year-end and the second payment by the end of its year of assessment.

A third voluntary payment can be made by a film owner six months after the end of the year of assessment. If the year of assessment ends on the last day of February, the third payment must be made within seven months after the end of the year of assessment.

Further information regarding the payment of provisional tax can be obtained on the SARS website [www.sars.gov.za](http://www.sars.gov.za) or from SARS branches.

## **16. OBJECTIONS AND APPEALS**

Where a film owner is not satisfied with an assessment issued or any modification made by the Commissioner to the declared income of such film owner and/or any deductions or allowances claimed in the return of income of such film owner, the film owner has the right to object to such an assessment.

Such an objection must state the grounds on which the objection is lodged and must reach the Commissioner within a period of 30 business days after the date of assessment, viz the due date of the assessment.

The Commissioner will either –

- allow the objection;
- disallow the objection; or
- allow the objection in part and disallow the other part.

Where an objection is disallowed in full or in part, a film owner has the right to appeal to the disallowance of the objection. The appeal must be delivered to the Commissioner within a period of 30 business days from the date of the disallowance of the objection.

Further information regarding the objection and appeal procedures is available on the SARS website [www.sars.gov.za](http://www.sars.gov.za) and can also be obtained from SARS branches.

## **17. RETENTION OF RECORDS**

Any film owner who has submitted an income tax return is required to retain all records relevant to that return for a period of five years from the date upon which the return relevant to the last entry in those records was received by the Commissioner.

In addition to this requirement, any film owner that has lodged an objection or appeal to an assessment, is required to retain the records relevant to the objection or appeal until the date the objection or appeal has been finalised.

## **CONCLUSION**

SARS has identified a need to issue this information guide. It is trusted that it will contribute to greater clarity to film owners with regard to the determination of their tax liability.

Further information regarding the topics discussed in this guide and any information about SARS is available on the SARS website [www.sars.gov.za](http://www.sars.gov.za) or can be obtained from SARS branches.