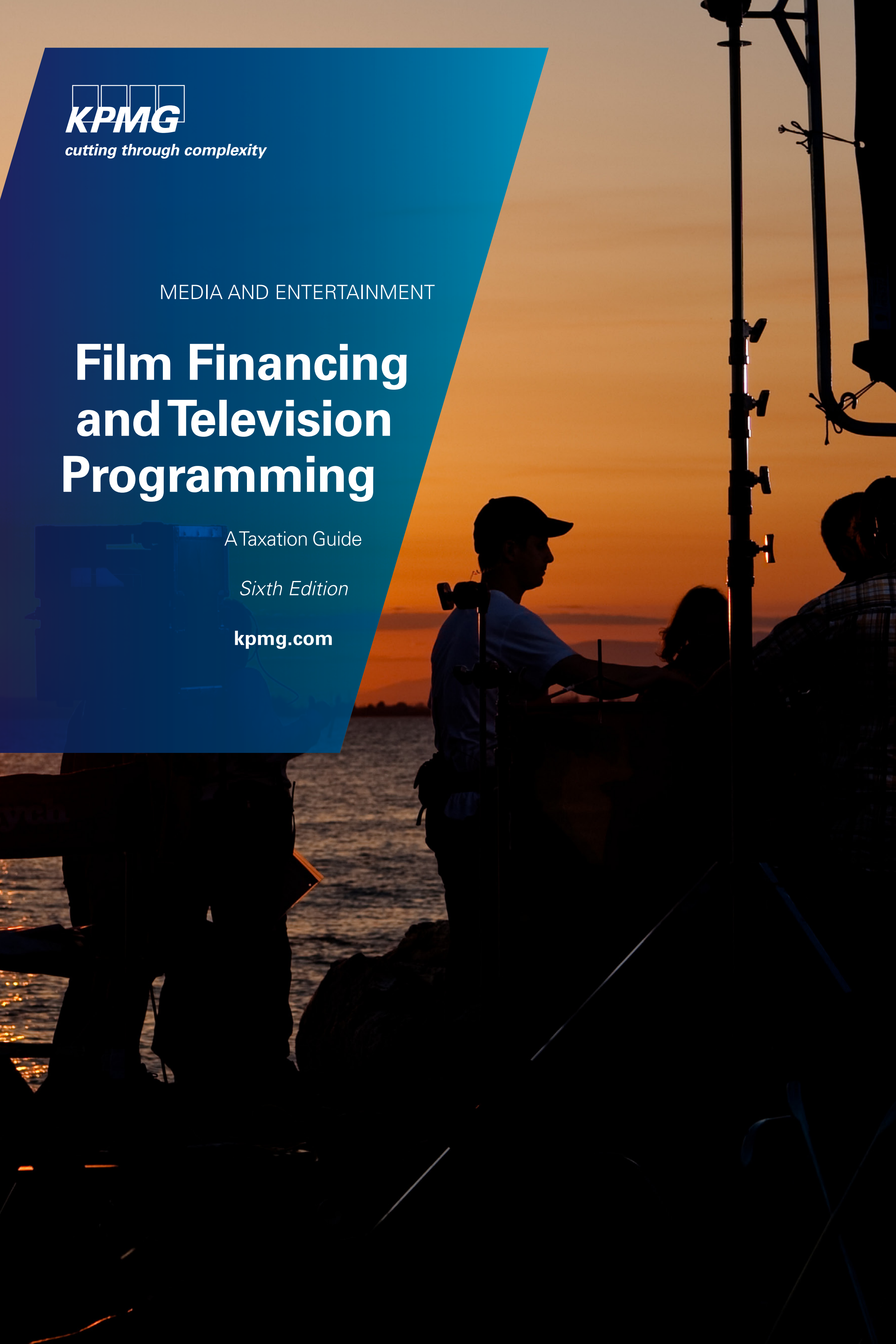

KPMG
cutting through complexity

MEDIA AND ENTERTAINMENT

Film Financing and Television Programming

A Taxation Guide

Sixth Edition

kpmg.com

Contents

Preface

KPMG LLP's (KPMG) Film Financing and Television Programming: A Taxation Guide, now in its sixth edition, is a fundamental resource for film and television producers, attorneys, tax, 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.
Its primary focus 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 media and entertainment Tax professionals.

KPMG published the first guide more than 15 years ago as a resource for global coverage of incentives and tax updates as they apply to the film and television industry. Subsequent editions expanded into coverage of financing techniques, credits/incentives, and a thorough appendix of withholding tax rates–a valuable reference tool for all finance and tax professionals.

Each chapter of the sixth edition 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. Additionally, the United States chapter focuses on both federal and state incentives, highlighting the states that offer the more popular and generous tax and financial incentives. 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 VAT tax rates; normal non-treaty withholding tax rates; and tax year-end information for companies and individuals.

Financing Structures
Descriptions of commonly used financing structures in film and television 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-effective 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.

Appendices

Additionally, withholding tax tables setting forth the non-treaty and treaty-based dividend, interest, and film royalty withholding tax rates for the countries surveyed are included as an appendix and can be used as a preliminary source for locating the applicable withholding rates between countries.

KPMG and Member Firm Contacts

References to KPMG and KPMG International member firm contacts at the end of each chapter are provided as a resource for additional detailed information.

The sixth edition of KPMG's Film and Television Tax Guide is available in an online PDF format at www.kpmg.com/filmtax and on CD. The guide is searchable by country.

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 book 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.

Finally, we would sincerely like to thank all of the KPMG International member firm Tax professionals from around the world who contributed their time and effort in compiling the information contained in this book and assisting with its publication. Production opportunities are not limited to the 35 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

January 2012

Chapter 08
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	10%, 20%
Annual VAT registration threshold	CZK 1,000,000 (approx. EUR 41,500) (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 revenues derived from the activity jointly. Each participant's share in the revenues 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 non-resident 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.

Revenues 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 revenues attributable to the participant would be taxable in the Czech Republic.

It is worth considering carrying out the production through a Czech special purpose company (e.g., a "camera for hire" company) set up in the Czech Republic by the contractual parties of the Association Agreement. This company would produce the film under a production contract with the association participants, entitling it to an appropriate production fee (e.g., on a cost-plus basis) but no further rights over the film. The film rights would then be exploited by the parties to the Association Agreement from their respective locations. As there would not be any permanent establishment of the participants of the association in the Czech Republic, in this case, the resulting revenues would be taxable in the country of their residence.

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. However, please note that such structures are not common in the Czech Republic.

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 revenues 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 which 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 percent – for further details see below.

Tax and Financial Incentives

A new system of financial incentives for filmmakers working in the Czech Republic was launched in June 2010. This program was approved by the European Commission. The program is targeted at domestic filmmakers having domicile in the Czech Republic and at foreign filmmakers having a branch in the Czech Republic. A subsidy is granted by the Czech Ministry of Culture to applicants who meet the so called cultural and production test (e.g. director, actors having domicile in the Czech Republic or any of European Economic Area ("EEA") country; the screenplay is about person or event belonging to the Czech or European culture or history).

The subsidy can be granted up to 20 percent of a film's expenditures on goods and services, which were acquired from Czech firms or firms that are registered for taxes in the Czech Republic. Further a subsidy up to 10 percent can be granted on foreign actors' remuneration if it is taxed in the Czech Republic.

Subsidies are paid out retrospectively after the project has been accomplished.

A company or individual that is resident in the Czech Republic can further benefit from the Czech National Fund for the support and development of Czech cinematography. If foreign entities have shares in the Czech company, the company can apply for this subsidy only if the shares held by the foreign entities do not exceed 50 percent of the total. However, there is no legal entitlement to this kind of state support and the granting of support is at the discretion of the Council.

The following projects are eligible for support:

- Creation of a Czech film;
- Production of a Czech film;
- Distribution of a worthy film;
- Promotion of Czech cinematography;
- Technical development and modernization of Czech cinematography; and
- Production, distribution and promotion of the films of national and ethnic minorities that live in the Czech Republic.

The grants are provided in the form of purpose subsidy, loan or returnable grant-in-aid. Aid could also be provided in the form of a guarantee for a bank loan.

Czech resident companies can also benefit from European Union funds for the support and development of European cinematography.

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 amounts to 19 percent in 2011.

Foreign Company
A foreign company not having its registered office in the Czech Republic shall be liable to 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 revenues 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.

Should the license be granted for a limited time period, the costs connected with the granting of the license should be accrued over this period. Should an unlimited license be 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 withholding tax in the amount of 15 percent. 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 intra-group 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. Audio visual work must be depreciated over a period of 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 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 non-deductible 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, which 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, 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 20 percent. If the supplier of the film is a taxable person, he must account for VAT as at the day on which the license for the completed film is granted 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 to or by a person registered for VAT in another EU member state or to a person with a registered office outside the EU, provided the recipient does not have an establishment in the Czech Republic.

Sale of Distribution Rights, 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 percent of the content) are subject to the reduced rate of 10 percent, whereas supplies of clothes or recorded music are subject to 20 percent.

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 of the promotional item does not exceed CZK500 (EUR 21); 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 CZK500 are provided without consideration, the provision of such goods is subject to VAT provided the related input VAT was deducted.

Catering Services and Accommodation

Catering services are subject to the standard rate of 20 percent. The reduced tax rate (10 percent) is applied to accommodation services.

Purchasing of Goods

Goods imported from a non-EU country are subject to import VAT (in most cases 20 percent) 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 obliged to account for input 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. Such VAT is in principle recoverable by claiming input VAT credit in the tax return.

Personal Taxation

Non-Resident Artists (self-employed)

Income Tax Implications

Czech tax non-residents 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 percent. 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 that the income has a character of copyright payment it will be subject to a withholding tax of 15 percent (subject to exemption or reduction in rate according to a particular Double Tax Treaty).

Social Security Implications

EU Regulation No. 883/2004 (former No. 1408/71) must be followed to determine where social security contributions should be paid in the case of Artists resident 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 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 percent. 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 expenses, he may deduct 40 percent of his income as a lump sum expense.

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 is obliged to pay health insurance contributions.

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 percent. The tax on employment income is calculated on the "super-gross" salary, which is the gross salary increased by 34 percent (social security and health insurance contributions payable by the employer in the Czech Republic). Thus, the effective tax rate is not 15 percent but a higher rate depending on the income level.

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 February 15 of the following year. If an employee has other income in addition to the income from the dependent activity, the Czech company should issue a standard confirmation of the employee's taxable income and tax withheld ("Potvrzeni o zdanitelne mzde a srazenych zalohach na dan ze mzdy") 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.

An employee is entitled to reduce his income by tax allowances and his tax by tax reliefs. A non-resident employee is entitled to reduce his tax only by the basic tax relief. Other tax reliefs will be applicable to a non-resident only if the income from Czech sources exceeds 90 percent of his total income.

Social Security Implications

EU Regulation No. 883/2004 on Social Security (the "Regulation") came into effect on May 1, 2010. The general rule of the Regulation is that persons to whom the 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 13 of the Regulation, which states that the legislation of the state in which the employee works, will apply.

However, an employee may apply for an exemption 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 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 security 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 percent and the employer's part is 34 percent of the gross remuneration. There is an annual cap on social and health insurance contributions equal to 72-times the average national salary (CZK 1,781,280 in 2011).

KPMG Contacts

KPMG's Media and Entertainment tax network members:

Jan Zurek

KPMG Ceska republikas.r.o.
Pobrezni 1a
186 00 Praha 8
Czech Republic

Phone: +420 222 123 441
Fax: +420 222 123 446

Petr Toman

KPMG Ceska republikas.r.o.
Pobrezni 1a
186 00 Praha 8
Czech Republic

Phone: +420 222 123 602
Fax: +420 222 123 446