



Guide to the Exemption from Normal Tax of Income from Films

Income Tax

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Preface

This guide provides general guidance on the exemption from normal tax for the receipts and accruals of income derived from the exploitation rights of a film. It does not go into the precise technical and legal detail that is often associated with tax and should not be used as a legal reference. While this guide reflects SARS's interpretation of the law, taxpayers who take a different view are free to use the normal avenues for resolving such differences.

This guide is not an "official publication" as defined in section 1 of the Tax Administration Act 28 of 2011 and therefore does not create a practice generally prevailing under section 5 of that Act. It is also not a binding general ruling under section 89 of the Tax Administration Act. Should an advance tax ruling be required, visit the SARS website for details of the application procedure.

This guide is based on legislation as at the date of issue.

The interpretation notes referred to in this guide are available on the **SARS website** and are as at the date of this publication.

For more information you may –

- visit SARS website at **www.sars.gov.za**;
- contact the SARS National Call Centre –
 - if calling locally, on 0800 00 7277; or
 - if calling from abroad, on +27 11 602 2093 (only between 8am and 4:30pm South African time).
- have a virtual consultation with a SARS consultant by making an appointment via the **SARS website**;
- visit your nearest SARS branch, after making an appointment via the **SARS website**;
or;
- contact your own tax advisor or practitioner.

Comments on this guide may be e-mailed to **policycomments@sars.gov.za**.

Leveraged Legal Products

SOUTH AFRICAN REVENUE SERVICE

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Glossary

In this guide unless the context indicates otherwise –

- “**completion date**” means the date on which a film, which qualifies for the exemption under section 12O, is for the first time 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;
- “**co-production treaty**” means an international co-production agreement between the government of the Republic and the government of another country, which agreement must be subject to the Constitution;
- “**DTIC**” means the Department of Trade, Industry and Competition;
- “**DTIC incentive**” means the South African Film and Television Production and Co-Production Incentive;
- “**DTIC Programme Guidelines**” means the DTIC’s Programme Guidelines for the DTIC incentive;
- “**NFVF**” means the National Film and Video Foundation established by the National Film and Video Foundation Act 73 of 1997;
- “**section**” means a section of the Act;
- “**SPCV**” means a special purpose corporate vehicle, namely, a company that is responsible for the production of a film as required by the DTIC under the DTIC Programme Guidelines;
- “**the Act**” means the Income Tax Act 58 of 1962; and
- any other word or expression bears the meaning ascribed to it in the Act.

1. Background

Section 12O¹, provides for the exemption from normal tax of income derived from the exploitation rights of approved films. Section 12O came into effect on 1 January 2012 and applies to all receipts and accruals of approved films if principal photography commenced on or after this date but before 1 January 2022.

The exemption under section 12O is still available to new investors after 1 January 2022 for receipts and accruals in respect of films of which principal photography commenced before 1 January 2022. An investor can thus acquire rights to a film after 1 January 2022 provided principal photography on that film commenced before that date but before completion and claiming exemption for the next 10 years. Commencement of principal photography refers to the day on which the actual shooting of the film begins.²

¹ See the **Annexure** for the relevant section.

² See the DTIC website at www.thedtic.gov.za for the DTIC Programme Guidelines and any amendments to the guidelines.

2. Exemption requirements

The receipts and accruals of income derived from the exploitation rights of a film are exempt from income tax under section 12O –³

- if the NFVF has approved the film as a local production or a co-production;⁴
- if the income is received by or accrues to an investor;⁵ and
- only to the extent that the income is received or accrues within a 10-year period after the film’s completion date.⁶

These requirements are considered in **2.1 – 2.4**.

2.1 Income derived from the exploitation rights of a film

2.1.1 Income

Section 12O uses “income” in the context of receipts or accruals from the exploitation rights of a film and not in the context of the definition of “income” in section 1(1).

2.1.2 Exploitation rights

As noted above, in order to qualify for the exemption, the income must be derived from the exploitation rights of a film. The term “exploitation rights” is defined in section 12O(1) as –

the right to any receipts and accruals in respect of—

- (a) the use of;
- (b) the right of use of; or
- (c) the granting permission to use,

any film to the extent that those receipts and accruals are wholly dependent on profits and losses in respect of the film.

The words “wholly dependent on profits and losses in respect of the film” indicate that the receipts and accruals must be dependent on the success of the film activity in respect of which the taxpayer undertook risk. That is, the receipt or accrual must be solely dependent on the production of a viable film. For example, the money received or accrued from the sale and licensing rights of a film potentially qualifies for the exemption as it is derived from the use and the right of use of the film and the receipt or accrual is dependent on the success of the film. The holder of the exploitation rights undertook risk because there was no guarantee that the film would be a success and give rise to any income.

In contrast, the exemption does not apply to the extent that any receipt or accrual is subject to a guaranteed minimum. For example, if an actor in a film receives a fixed salary, that receipt will not qualify for the exemption as it is not derived from the use, right of use or granting of permission to use the film and the receipt is not dependent on the success of the film. The actor does not undertake any risk because the actor must be paid the agreed amount irrespective of the amount of income which the film generates.

³ Section 12O(2).

⁴ Section 12O(2)(a).

⁵ Section 12O(2)(b).

⁶ Section 12O(2)(c).

These rules seek to exclude income from set salaries and loan repayments. However, parties taking salary compensation in the form of exploitation rights will qualify for the exemption (assuming all the requirements of section 12O are met) to the extent that the income from those rights is fully dependent on the film's profits and losses. That is, parties who take contingent film rights which are not subject to guaranteed minimums in lieu of a salary potentially qualify for the exemption.⁷ In this situation it is important to note that there are two receipts or accruals which need to be considered, namely the receipt or accrual of the exploitation rights in respect of the services rendered which may require inclusion in gross income, and the subsequent receipt or accrual from the exploitation rights which may qualify for exemption under section 12O. See Example 1 below. The same principle applies to other goods and services rendered in exchange for exploitation rights.

Although influenced by the success of the film, receipts and accruals from the sale of film branded products such as toys, clothing, posters and mugs are not attributable to the use of, the right of use of or the granting of permission to use the film itself and the profits or losses are not wholly dependent on the success of the film. Therefore, the receipt or accrual from a film branded product is not a receipt or accrual derived from the exploitation right of a film and does not qualify for the exemption in section 12O(2).

Example 1 – Exploitation rights and services rendered

Facts:

A agreed to play the leading role in a local film in return for exploitation rights which entitle A to receive 5% of the proceeds from film sales subject to a guaranteed minimum of R50 000. The film, which was started and completed in 2021, generated R3 million of sales income in 2022.

Result:

2021 year of assessment:

A must include the market value of the exploitation rights⁸ that entitle A to 5% of the proceeds from film sales in gross income under paragraph (c) of the definition of "gross income" in section 1(1). The exploitation rights were received in respect of acting services rendered by A. Section 24M may delay the timing of accrual in circumstances where the amount cannot be quantified

2022 year of assessment:

A earns income* of R150 000 (R3 000 000 × 5%) from the exploitation rights related to film sales. Assuming the detailed requirements of section 12O are met, R150 000 will be included in gross income but A will obtain an exemption for R100 000.

A may claim the exemption as principal photography commenced before 1 January 2022.

* In context income refers to the amount that is received by or accrues to A; it does not refer to the definition of "income" in section 1(1).

⁷ *Explanatory Memorandum on the Taxation Laws Amendment Bill, 2011* – at 89.

⁸ The guaranteed minimum is an aspect which will be taken into account in determining the market value of the exploitation rights received for the services rendered.

Example 2 – Exploitation rights and a guaranteed minimum in film sales

Facts:

A is a film producer that owns the production rights to produce a local film which is completed in 2021. A has exploitation rights that entitle A to receive 10% of the proceeds from film sales with a minimum of R100 000. The film generated R3 million of sales income.

Result:

A earns income* of R300 000 ($R3\,000\,000 \times 10\%$) from the exploitation rights related to film sales. Assuming the detailed requirements of section 12O are met, A will obtain an exemption for the receipt or accrual of R200 000 but not for the receipt or accrual of R100 000. The amount of R100 000 is guaranteed and does not meet the requirement of being dependent on the profit and losses of the film.

A may claim the exemption as principal photography commenced before 1 January 2022.

* In context income refers to the amount that is received by or accrues to A; it does not refer to the definition of “income” in section 1(1).

Example 3 – Exploitation rights and additional amounts not derived from exploitation rights

Facts:

A is a film producer that owns the production rights to produce a local film which is completed in 2021. A has exploitation rights that entitle A to receive 10% of the proceeds. A’s share of the profits will, by agreement, only be paid to A 2 years after the film’s completion date. The amount paid to A will be increased by 5% on the date of payment to compensate A for the delayed receipt. The film generates R3 million of sales income in 2023, 2 years after the film’s completion date.

Result:

A earns income* of R300 000 ($R3\,000\,000 \times 10\%$) from the exploitation rights related to film sales. R300 000 accrues to A as gross income in 2023 and, assuming the detailed requirements of section 12O are met, A will obtain an exemption for the amount of R300 000. The amount of the increase ($R300\,000 \times 5\%$) will not qualify for the exemption as it is not derived from the exploitation rights of the film.

A is entitled to claim the exemption as principal photography commenced before 1 January 2022.

* In context income refers to the amount that is received by or accrues to A; it does not refer to the definition of “income” in section 1(1).

Example 4 – Acquisition of exploitation rights before and after completion date

Facts:

A, a film distributor, acquired distribution rights in 2 films, X and Y, that entitled A to receive 10% of the proceeds from the sales of each film. The rights in film X were acquired after the date that principal photography commenced but before the completion date and the rights in film Y were acquired after the completion date of the film. The rights acquired in film X also entitled A to receive R100 000 in pre-sales from film X.

The films were both completed in 2021. Each film generated R2 million of sales income.

Result:

Film X

A will not obtain an exemption for the pre-sales receipt or accrual of R100 000. The amount was received from the right of use of the film but does not meet the requirement of being wholly dependent on the profit and losses in respect of the film.

A also earns income* of R200 000 ($R2\,000\,000 \times 10\%$) from the distribution rights related to film sales. Assuming the detailed requirements of section 12O are met, A will obtain an exemption for the receipt or accrual of R200 000 as the exploitation rights were acquired after the date of principal photography but before the completion date.

Film Y

A earns income* of R200 000 ($R2\,000\,000 \times 10\%$) from the distribution rights related to film sales. However, A will not obtain an exemption for the receipt or accrual of R200 000 as the exploitation rights (in the form of distribution rights) were acquired after the completion date and the requirements of section 12O have not been met (see **2.3**).

* In context income refers to the amount that is received by or accrues to A; it does not refer to the definition of “income” in section 1(1).

2.1.3 Film

The term “film” is defined in section 12O(1) as –

- (a) a feature film;
- (b) a documentary or documentary series; or
- (c) an animation,

conforming to the requirements stipulated by the Department of Trade and Industry in the Programme Guidelines for the South African Film and Television Production and Co-production Incentive.

The DTIC⁹ Programme Guidelines¹⁰ set out the requirements listed below for feature films, documentaries and animations.¹¹

A feature film is a film –

- including animation, commonly screened as the main attraction in commercial cinemas;
- with a duration of no less than 80 minutes, or in the case of a large format (IMAX) film, no less than 45 minutes; and
- that is shot and processed to commercial theatrical release standards for cinema exhibition or television broadcast, direct-to-video or DVD.

A documentary or documentary series is –

- a non-fictional informative or educational programme or series recording real people or events that may involve some dramatisation;
- with a duration of no less than 60 minutes in length, or in the case of a large format (IMAX) film, no less than 45 minutes;
- that is shot and processed to commercial theatrical release standards for cinema exhibition, television broadcast, direct-to-video or DVD; and
- in the case of a documentary series, is limited to 26 episodes.

An animation is –

- a sequence of frames that, when played in order at sufficient speed, presents a smoothly moving image for broadcast, projection, new media and network use in an entertainment, educational, informative or instructive manner; and
- can be hand-drawn images (2D animation), digitised video, computer-generated images (3D and flash animation), live action objects or a combination of these sources.

2.2 The NFVF has approved the film as a local production or co-production

The NFVF's mandate is to develop and promote the South African film and video industry. In pursuance of this mandate, the NFVF introduced the South African Film Criteria,¹² the objective of which is to set qualifying criteria for what constitutes a South African film based on a point system. Generally the same criteria apply to local productions as well as official co-productions although the points awarded to different criteria may vary.

The NFVF must have approved a film as a local production or as a co-production in order for the film to potentially qualify for relief under section 12O(2)(a), that is, before principal photography has commenced.

⁹ The Department of Trade, Industry and Competition (DTIC) was established after the merger of the Department of Trade and Industry (DTI) and the Economic Development Department.

¹⁰ Issued July 2018. See Annexure F: Qualifying Formats Detailed Description. See the DTIC website at www.thedtic.gov.za for the DTIC Programme Guidelines and any amendments to the guidelines.

¹¹ The DTIC Programme Guidelines also refer to tele-movies, television drama series and mini-series, and digital content and video gaming, which are not included in the definition of a "film" under section 12O.

¹² Applicants can contact the NFVF for details on the South African Film Criteria and weightings awarded for local productions and official co-productions; see www.nfvf.co.za for contact details.

The information in **2.2.1** and **2.2.2** is based on a high level understanding of the NFVF requirements, however the requirements and processes are subject to change and interested parties should consult the National Film and Video Foundation directly for the latest information in this regard.

2.2.1 Local productions

Application to the NFVF for approval as a local production¹³ must be made in the format prescribed by the NFVF.¹⁴

A film must be awarded at least 70% of the possible points available under the South African Film Criteria¹⁵ by the NFVF in order for the film to be approved as a local production. The South African Film Criteria include a consideration of four main aspects of film production and within those aspects allocates a number of points to different factors. The four main aspects and factors are:

- Key creatives: whether the director, producer, writer, editor, composer, cinematographer or production designer is South African.
- Casting: whether 50% or more of lead actors, second lead actors or supporting actors are South African.
- Technical and craft contribution: whether the art director, wardrobe and makeup artists, sound designer, set designer and constructor, camera assistant or lightning gaffer is South African and whether post production takes place in South Africa.
- HDI:¹⁶ whether the director, writer, editor, composer, cinematographer, sound designer, production designer, lead actor or actress, or second lead actor or actress is HDI and whether 50% of the script is in an official South African language other than English.

2.2.2 Co-productions

Application to the NFVF for approval as a co-production if a film is co-produced under a co-production treaty must be made in the format prescribed by the NFVF.

A co-production is –¹⁷

“a general term covering a variety of production arrangements between two or more production companies undertaking a television, film or other video project”.

A co-production will generally involve both a creative contribution and a financial contribution from the local and foreign co-producers. In limited situations a co-producer’s contribution may be a finance-only contribution. The co-production treaty will determine the type of contributions that a co-producer must make in order for the co-production to fall under the co-production treaty.

¹³ The NFVF refers to a local production as a South African production in the South African film criteria.

¹⁴ Applicants can contact the NFVF for details on the application process.

¹⁵ Contact the NFVF for any updates to the criteria.

¹⁶ HDI broadly means a previously disadvantaged person, including a female or disabled person.

¹⁷ www.nfvf.co.za/co-productions/ [Accessed 14 July 2023].

South Africa has entered into co-production treaties with Canada, Italy, Germany, the United Kingdom, France, New Zealand, Australia, Ireland and Netherlands.¹⁸ Applicants must consider the applicable co-production treaty when applying for approval as the requirements vary per treaty.

The NFVF has a two-stage application process, namely –

- an advance ruling application; and
- a final ruling application.

A co-producer must apply to the NFVF at least 30 days before the commencement of principal photography for an advance ruling. At the end of the production the co-producer must submit an application for a final ruling. The co-producer will be required to submit an application form and relevant supporting documentation for both rulings. The NFVF has prepared a guideline¹⁹ to assist co-producers in making applications. The guideline outlines the application procedure and the submission requirements.

2.3 The income is received by or accrues to an investor

An investor refers to a person who acquired all or some of the exploitation rights of the film. Section 12O makes provision for two types of investors, namely –

- a pre-production investor who acquired the exploitation rights before principal photography commenced; and
- a mid-production investor who acquired the exploitation rights after principal photography commenced but before the completion date of the film.

Mid-production investors will not be eligible for the exemption if the consideration for the exploitation rights was directly or indirectly applied for the benefit of a pre-production investor.²⁰ The use of the consideration to cover production costs, as opposed, for example to being applied for the benefit of a pre-production investor, is a permissible use of the mid-production investor's funds.

The term “principal photography” is not defined in the Act but is considered by the film industry to be when “filming” begins. Principal photography is “the phase of producing a film or television show in which the bulk of shooting takes place, as distinct from pre-production and post-production”.²¹

Example 5 – Pre-production and mid-production investors

Facts:

A and B (who are pre-production investors) own the production rights to produce a local film which is completed in 2021. Principal photography was temporarily stopped in 2019 because of a shortfall of funding. C and D join as mid-production investors (after principal photography commenced but before the completion date) and receive proportionate exploitation rights for providing additional funding for production costs. At the completion date A, B, C and D each held 25% of the exploitation rights.

¹⁸ See www.nfvf.co.za for copies of the co-production treaties.

¹⁹ See the “Guidance Notes on Official Co-productions” on www.nfvf.co.za for detail.

²⁰ Section 12O(2)(b)(ii).

²¹ http://en.wikipedia.org/wiki/Principal_photography [Accessed 14 July 2023].

C sold C's 25% of the exploitation rights to Y for R180 000 one month after the completion date. The film generated income of R1,4 million and A, B, D and Y each received R350 000.

Result:

Assuming the detailed requirements of section 12(O) are met, A, B and D obtain a full exemption on their proportionate income* of R350 000 as the income is earned as a result of exploitation rights held before the completion date. Y's income* of R350 000 is fully taxable because Y acquired the exploitation right from C after the completion date and Y paid C R180 000 for the exploitation rights.

C will obtain an exemption under section 12O for the proceeds of R180 000 accruing from the sale of the exploitation rights to Y.

* In context income refers to the amount that is received by or accrues to A, B, D and Y; it does not refer to the definition of income in section 1(1).

Example 6 – Pre-production and mid-production investors

Facts:

A is a film producer that owns the production rights to produce a local film. Principal photography commenced in 2021 and was completed at the end of 2022.

A initially held all the exploitation rights and was entitled to receive 100% of the proceeds from film sales. However, at the beginning of 2021 B contributed an amount of R200 000 to help fund the expenditure incurred in completing the film and in return received 10% of the exploitation rights which entitled B to receive 10% of the proceeds from film sales.

The film generated R3 million of sales income.

Result:

A earns income* of R2 700 000 ($R3\,000\,000 \times 90\%$) from the exploitation rights related to film sales. A will obtain an exemption for the receipt or accrual of R2,7 million assuming the detailed requirements of section 12(O) are met.

B earns income* of R300 000 ($R3\,000\,000 \times 10\%$) from the exploitation rights related to film sales. B acquired the exploitation rights after principal photography commenced but before the completion date and the proceeds were not paid or applied for A's benefit so B will obtain an exemption for the receipt or accrual of R300 000 assuming the detailed requirements of section 12(O) are met.

B is entitled to claim the exemption as principal photography commenced before 1 January 2022

* In context income refers to the amount that is received by or accrues to A or B; it does not refer to the definition of income in section 1(1).

2.4 To the extent income is received or accrues within a 10-year period after completion

The exemption only applies to the extent that the income is received or accrues within a period of 10 years after the completion date of that film.²² If a taxpayer claims a net loss under section 12O(5)(a), the exemption under section 12O(2) falls away from that point onwards – see 5.²³

3. Persons not allowed the exemption

Despite the fact that a person may have met the requirements considered in 2, an exemption will not be allowed under section 12O if the investor (see 2.3) is a broadcaster or a person that is a connected person²⁴ in relation to a broadcaster.²⁵

For the purpose of section 12O the term “broadcaster” is defined in section 1 of the Broadcasting Act 4 of 1999, as –

any legal or natural person who composes or packages television or radio programme services for reception by the public or sections of the public or subscribers to such a service irrespective of technology used.

4. Reporting requirements

On-going reporting is required in order to measure the economic success of the incentive and to guard against tax avoidance. The NFVF, under section 12O, has been designated as the key point for collecting and submitting information to the Minister of Finance.

In the event that income arising from the exploitation rights of a film is distributed by a person within a period of 10 years commencing from the completion date of the film, any SPCV²⁶ or approved collection account manager (CAM)²⁷ that manages those exploitation rights under a CAM agreement, must provide a report to the NFVF.²⁸ The report must be submitted to the NFVF in the time frame and manner and containing the information as prescribed by the Minister.

The NFVF must provide an annual report to the Minister on all films which the NFVF has approved as local productions or co-productions if any income is received or accrues in respect of that film within a period of 10 years commencing from the completion date of the film and the income is eligible for the exemption under section 12O.²⁹ The report must be provided to the Minister in the time frame and manner and containing the information as prescribed by the Minister.

²² Section 12O(2)(c).

²³ Section 12O(5)(e).

²⁴ Interpretation Note 67 “Connected Persons”.

²⁵ Section 12O(3).

²⁶ It is a requirement of the DTIC incentive (see 6) that an applicant set up a separate SPCV to account for production income and expenditure relating to the film applying for the incentive. It is not a requirement of section 12O that an SPCV must be in place.

²⁷ A CAM is approved by the Minister for the purpose of section 12O by notice in the *Government Gazette*.

²⁸ Section 12O(4)(a).

²⁹ Section 12O(4)(b).

5. Claiming a net loss

Section 12O(5) provides that, notwithstanding section 23(f), a taxpayer may deduct from income an amount in respect of expenditure incurred to acquire exploitation rights in a film.³⁰ The amount of the deduction is equal to the amount of any expenditure incurred to acquire the exploitation rights less any amount received or accrued during *any* year of assessment in respect of that film.³¹ Expenditure incurred to acquire exploitation rights excludes contributions investors make subsequent to acquiring the exploitation right. This arises because even if those subsequent contributions are made in proportion to the exploitation rights held they are not made to acquire the relevant rights as the investor already holds the right. The key question, which must be answered based on the facts of the particular case, is whether the expenditure is being made to acquire the exploitation right. The amount received or accrued includes the amount received from the DTIC incentive (see 6). The deduction is often referred to as a deduction of the net loss.

Taxpayers may claim the net loss during any year of assessment commencing at least two years after the completion date of the film.³²

Any receipts and accruals of income from a taxpayer's exploitation rights in a film in any year of assessment after the year of assessment in which a deduction of a net loss was claimed, will not qualify for an exemption under section 12O(2)³³ (that is, the exemption permanently falls away from that point onwards). In addition, the deduction in section 12O(5)(a) is a once-off deduction and is not available in any year of assessment after the year of assessment in which a deduction of a net loss was first claimed.

Despite the above, taxpayers will not be allowed to claim a deduction for the net loss to the extent that the expenditure was funded from a loan, credit or similar financing.³⁴

Example 7 – Net losses and the effect of the DTIC incentive

Facts:

A is a film producer that owns the production rights to produce a local film which was completed on 31 January 2021. A's exploitation rights, which were acquired before 2021, entitled A to 40% of the film proceeds. A incurred R4 million on the acquisition of the exploitation rights. The R4 million was used to fund the production costs of the film and was not applied for the benefit of the previous holder of the rights.

Company A, an SPCV, received funding for the film from the DTIC in the form of the DTIC incentive and paid R500 000 of the grant to A. The film generated proceeds of R6 million of which R2,4 million was allocated to A.

³⁰ Provided the taxpayer has qualified for exemption under section 12O(2) and principal photography commenced before 1 January 2022.

³¹ Section 12O(5)(d) refers to limiting the deduction to the extent that the expenditure incurred exceeds the total amount received or accrued in respect of the exploitation rights. Practically this calculation will always give rise to an amount which is equal to or greater than the amount of the deduction calculated under section 12O(5)(b). Therefore, the amount calculated under section 12O(5)(b) will be the amount of the deduction assuming it is a positive amount and all the other requirements of the section are met.

³² Section 12O(5)(d).

³³ Section 12O(5)(e).

³⁴ Section 12O(5)(c).

A's year of assessment ends on 28 February each year.

Result:

A will obtain an exemption under section 12O(2) on the proceeds of R2,4 million because the income is earned from exploitation rights held before the completion date of the film. The amount of R500 000 from the DTIC incentive is exempt under section 12O(6)(b). The expenditure of R4 million is incurred in the production of exempt income and is not deductible under section 11(a) in the year it is incurred.

A may deduct an amount in respect of the expenditure incurred to acquire the exploitation rights, however the amount may only be deducted in any year of assessment commencing at least 2 years after the completion date of 31 January 2021. This means the first year in which A may claim the deduction is A's 2024 year of assessment. The amount of the deduction is R1,1 million (R4 million expenditure – income of R2,4 million received from the film in the 2024 or an earlier year of assessment – income of R500 000 from the DTIC incentive).

The exemption under section 12O(2) is not available to any income received or accrued from the film concerned in any year of assessment subsequent to the date of the deduction of the net loss. Therefore, any income earned from the film concerned in the 2025 or a later year of assessment will be taxable. In addition, the deduction under section 12O(5)(a) is only available once and may not be claimed in the 2024 year of assessment or any subsequent year of assessment.

Example 8 – Net losses if expenditure is funded by a loan

Facts:

A is a film producer that owns the production rights to produce a local film which was completed on 31 January 2021. A has exploitation rights with an entitlement to 40% of the film proceeds. A incurred R4 million on the acquisition of the exploitation rights, R1 million of which was incurred on loan account. The R4 million was spent on the film and was not applied for the benefit of the previous holder of the rights.

The film generated proceeds of R6 million of which R2,4 million was allocated to A.

A's year of assessment ends on 28 February each year.

At the end of the 2024 year of assessment R400 000 of the R1 million originally incurred on loan account was still outstanding.

Result:

A will obtain a full exemption on the proceeds of R2,4 million under section 12O(2) because the income is earned from exploitation rights held before the completion date of the film in 2021. The expenditure of R4 million is incurred in the production of exempt income and is not deductible under section 11(a) in the year it is incurred.

A may deduct an amount in respect of the expenditure incurred, however the amount may only be deducted in any year of assessment commencing at least 2 years after the completion date of 31 January 2021. This means the first year in which A may claim the deduction is A's 2024 year of assessment. The amount of the deduction is R1,2 million (R3,6 million expenditure because at the time of calculating the net loss R400 000 was still outstanding on loan account – income of R2,4 million received from the film in the 2024 or an earlier year of assessment).

The exemption under section 12O(2) is not available to any income received or accrued from the film concerned in any year of assessment subsequent to the date of the deduction of the net loss. Therefore, any income earned from the film concerned in the 2025 or a later year of assessment will be taxable. In addition, the deduction under section 12O(5)(a) is not available in later years of assessment.

Example 9 – Deduction of a net loss

Facts:

A is a film producer that owns the production rights to produce a local film. Principal photography commenced on 1 June 2020. On 1 January 2021 B contributed an amount of R200 000 to fund the expenditure incurred in completing the film and in return received 10% of the exploitation rights which entitled B to receive 10% of the proceeds from film sales.

In addition, on 1 March 2021 A and B were both required to contribute an additional amount in proportion to A and B's share of the exploitation rights. This contribution was used to fund production costs during 2014. B's additional contribution amounted to R40 000.

The film was completed on the last day of the 2021 year of assessment.

The film was not a success and only generated R1,5 million of sales income in 2022.

B's year of assessment ends on 28 February each year.

Result:

B's income* of R150 000 ($R1\ 500\ 000 \times 10\%$) in 2022 is from the exploitation rights related to film sales. B acquired the exploitation rights after principal photography commenced but before the completion date and the proceeds were not paid or applied for A's benefit so B will obtain an exemption for the receipt or accrual of R150 000 assuming the detailed requirements of section 12(O) are met.

* In context income refers to the amount that is received by or accrues to B; it does not refer to the definition of "income" in section 1(1).

B will meet the requirements for a deduction under section 12O(5)(a) in the 2024 year of assessment which commences 2 years after the completion date. The amount of the deduction under section 12O(5) is R50 000 (expenditure to acquire the exploitation rights R200 000 – R150 000 income from the film). The additional contribution of R40 000 does not qualify for a deduction as it is not expenditure which was incurred to acquire the right. B already owned 10% of the exploitation rights at the date the expenditure was incurred and the additional contribution did not alter this *pro rata* share.

6. Exemption from tax for the DTIC incentive

6.1 Background

The DTIC incentive³⁵ was introduced by the DTIC in 2008. The aim of the DTIC incentive is to support the local film and television industry and to contribute towards employment opportunities in South Africa. The DTIC incentive is in the form of a grant calculated at 35% of qualifying South African production expenditure. An additional 5% of qualifying South African production expenditure is granted for productions hiring at least 30% of Black South African citizens as head of departments and procuring at least 30% of the qualifying South African production expenditure from 51% South African black owned entities which have been operating for at least a period of one year.³⁶ The incentive is capped at a maximum grant of R50 million per qualifying project. The DTIC incentive is administered by the DTIC.

The DTIC incentive is only available to qualifying South African productions and official treaty co-productions³⁷ with a minimum total production budget of R500 000 for documentaries and R2 500 000 for other eligible formats (for example, feature films).

The DTIC incentive specifies that an applicant must be an SPCV which is set up solely for the purpose of producing the film. The SPCV must be incorporated in South Africa and may only qualify for the grant in respect of one film. The SPCV must keep separate accounts to the holding company, if applicable, and must account separately for the production costs and income of the film.³⁸

6.2 Exemption under section 120

Any grant received by or accrued to an SPCV from the state under the DTIC incentive will be exempt from normal tax but subject to the general recoupment provision under section 8(4).³⁹

Section 8(4)(a) specifies that there must be included in a taxpayer's income all amounts allowed to be deducted or set-off in the current or any previous year of assessment under sections 11 to 20, amongst others, that have been recovered or recouped during the current year of assessment. This means that if the grant covers an amount of expenditure for which the taxpayer has claimed a deduction under, for example, section 11(a), an amount equal to the amount of the deduction claimed will be included in income.

³⁵ There is a separate programme for Foreign Film and Television Production.

³⁶ This guide only mentions some of the requirements – see the DTIC Programme Guidelines on www.thedtic.gov.za for information regarding all of the requirements and the application forms.

³⁷ Approved co-productions with Canada, Italy, Germany, the United Kingdom, France, New Zealand, Australia, Ireland and Netherlands.

³⁸ See the DTIC Programme Guidelines on www.thedtic.gov.za for further information and application forms.

³⁹ Section 120(6)(a). See **6.3** for a consideration of the consequences of possible duplication of the exemption under section 120(6)(a) and section 12P(2).

Example 10 – Exemption subject to section 8(4)(a)

Facts:

A is a film producer that owns the production rights to produce a local film. Principal photography commenced in 2020 and was completed on the last day of the 2021 year of assessment.

During the 2020 year of assessment A claimed a deduction under section 11(a) for costs totalling R100 000. A had not obtained approval from the NFVF.

The DTIC awarded A a grant under the DTIC incentive in the 2022 year of assessment. The grant included an amount of R25 000 in relation to costs that A had claimed a deduction for in 2021.

Result:

An amount of R25 000 will be included in income in the 2022 year of assessment as it constitutes a recoupment under section 11(a). The balance of the grant will be exempt under section 12O(6)(a) assuming the details of the amount do not bring it within the ambit of section 8(4)(a).

The exemption will continue to apply should the SPCV pay the amount over to another person pursuant to the exploitation rights in respect of the film. However, the exemption will only apply to the extent that the amount does not exceed any amount that the person contributed to the production of the film.⁴⁰ The “production of the film” refers to the process of making the film and is a process which ends when the film is in a form in which it is regarded as ready for copies to be made and distributed, for presentation to the general public. An amount which is contributed towards the funding of expenditure incurred or to be incurred in producing the film will be taken into account in calculating the amount of the exemption. The facts and circumstances of the particular case will determine whether an amount is incurred in the production of a film. For example, the remuneration paid to the lead actor for being the lead is clearly related to the production of the film and will be taken into account. In contrast, the remuneration paid to part-time employees serving the food and beverages at the film’s launch party will not be taken into account because it does not relate to the production of the film; it relates to the marketing of the film. These examples highlight that in determining if an amount relates to the production of the film, a taxpayer cannot only look at the nature of the expenditure, for example, salary remuneration, but must also look at the purpose and effect of the expenditure.

The following types of expenses will be included in the calculation of the amount of the exemption provided the expenditure is incurred in the production of the film, the determination of which can only be made on a case-by-case basis:

- Any remuneration, salary, legal, accounting or other fee, commission or other amount paid or payable to any person.
- The cost of acquiring the story rights, script, screenplay, copyright or other similar rights.
- Insurance premiums for insurance against injury to or death of persons, or loss of or damage to property.

⁴⁰ Section 12O(6)(b).

- Premiums or commission payable in order to secure a guarantee that the cost of the film will not exceed a specified amount.
- Interest, finance charges and raising fees incurred in connection with the production of the film.
- The cost of acquiring or creating music, sound and other effects which will form part of the film.
- The purchase, hire or construction of sets or of any machinery, implements, utensils or articles for that film.

Any contribution towards any of the following items would be excluded from the calculation of the amount of the exemption because they are not considered to be an amount the person contributed to the production of a film:

- Consideration for exploitation rights which is directly or indirectly paid or applied for the benefit of a previous holder of such rights.
- Any expenditure on the marketing, promotion or soliciting of orders of the film.
- Costs incurred in making copies of the film for sale.

Example 11 – Production-related costs

Facts:

A is a film producer that owns the production rights to produce a local film. Principal photography commenced in 2021 and was completed on the last day of the 2022 year of assessment.

At the beginning of 2022 B paid A R1 million for 10% of the film's exploitation rights. B also contributed R2 million towards expenditure incurred during and related to principal photography (for example, actors and actresses salaries, location fees and hiring of equipment).

In addition, in March 2022 A and B were both required to contribute an additional amount in proportion to A and B's share of the exploitation rights towards post-production costs. B's additional contribution amounted to R500 000 (R300 000 towards the editing of the sound and visual effects and R200 000 towards marketing).

Result:

B's contributions will be considered to be production-related to the extent it was made for the following items:

- a) R2 million used towards actors and actresses salaries, location fees and hiring of equipment; *and*
- b) R300 000 used towards editing the film.

B's contributions will not be considered to be production-related to the extent it was made for the following items –

- i) the acquisition of 10% of the exploitation rights paid directly to A; and
- ii) R200 000 towards marketing the film.

6.3 Exemption under section 12P

Section 12P, which deals with the exemption of amounts received or accrued from government grants,⁴¹ is relevant to a taxpayer who receives or to whom a DTIC incentive accrues.

Section 12P(2) provides that any amount received by or accrued to a person as a beneficiary of a government grant is exempt from normal tax if, amongst others, the government grant is listed in the Eleventh Schedule to the Act. The DTIC incentive falls within the “*Film Production Incentive received or accrued from the Department of Trade and Industry*” category of the Eleventh Schedule to the Act and therefore, the exemption under section 12P will apply to an SPCV who receives or to whom an amount accrues under the DTIC incentive. The SPCV will also have qualified for the exemption in section 12O(6)(a) (see 6.2). An amount can only be exempt from tax once and a taxpayer may not therefore claim a double exemption.

Section 12P(3) to (6) deal with the consequences on the cost, deductions and allowances available to a taxpayer if a government grant contemplated in section 12P(2) is received or accrued for the acquisition, creation or improvement, or the reimbursement for expenditure so incurred, of trading stock, allowance assets or other assets, or for the incurral or reimbursement of expenditure deductible under section 11. The consequences dealt with in section 12P(3) to (6) are relevant in the situation in which a DTIC incentive is received by or accrues to a taxpayer even if the taxpayer claims the exemption under section 12O(6)(a) and not section 12P(2). The reason being that section 12P(2) uses the word “contemplate” which is wider than “applies” or “qualifies” and therefore, provided the grant is considered in section 12P(2), section 12P(3) to (6) will apply. All grants in the Eleventh Schedule to the Act, which includes the DTIC incentive, are contemplated in section 12P(2) and therefore taxpayers who receive or to whom a DTIC incentive accrues must consider the provisions of section 12P(3) to (6).

7. Conclusion

Section 12O effectively eliminates income tax on qualifying film receipts and accruals for a 10-year period from the date the film is completed provided principal photography commenced before 1 January 2022. It applies to films that have been approved by the NFVF as a local production or a co-production. The NFVF has introduced a set of qualifying criteria, the South African Film Criteria, that are used to determine whether a film constitutes a local production or a co-production based on a point system. The exemption is limited to investors who acquired the exploitation rights held before the completion date of the film.

Taxpayers may claim a net loss on a film in a year of assessment commencing at least two years after the completion date of the film. The deduction of a net loss also results in a taxpayer being unable to claim the exemption on the particular film going forward.

Section 12O(6) provides that any grant received by or accrued to an SPCV from the state under the DTIC incentive will be exempt from normal tax but subject to the general recoupment provision under section 8(4). In certain cases, if the grant is passed on to an investor, the investor will also qualify for the exemption. A taxpayer who receives or to whom an exempt DTIC incentive accrues must consider the provisions of section 12P(3) to (6) as there are

⁴¹ See Interpretation Note 59 (issue 2) “Tax Treatment of the Receipt or Accrual of Government Grants” for a detailed consideration of section 12P and the Eleventh Schedule.

consequences on the cost, deductions and allowances available to a taxpayer in respect of related expenditure.

Annexure – The law

Section 120 – Exemption in respect of films

120. Exemption in respect of films.—(1) For the purposes of this section—

“**completion date**” means the date on which a qualifying film is for the first time 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;

“**exploitation rights**” means the right to any receipts and accruals in respect of—

- (a) the use of;
- (b) the right of use of; or
- (c) the granting of permission to use,

any film to the extent that those receipts and accruals are wholly dependent on profits and losses in respect of the film;

“**film**” means—

- (a) a feature film;
- (b) a documentary or documentary series; or
- (c) an animation,

conforming to the requirements stipulated by the Department of Trade and Industry in the Programme Guidelines for the South African Film and Television Production and Co-production Incentive;

“**National Film and Video Foundation**” means the National Film and Video Foundation established by the National Film and Video Foundation Act, 1997 (Act No. 73 of 1997); and

“**special purpose corporate vehicle**” means a company responsible for the production of a film as required by the Department of Trade and Industry in terms of the Programme Guidelines for the South African Film and Television Production and Co-production Incentive.

(2) There must be exempt from normal tax the receipts and accruals in respect of income derived from the exploitation rights of a film—

- (a) if the National Film and Video Foundation has approved the film in terms of section 3(c) read with section 4(1) of the National Film and Video Foundation Act, 1997 (Act No. 73 of 1997), as a local production or co-production whereby a film is co-produced in terms of an international co-production agreement between the government of the Republic and the government of another country, which agreement must be subject to the Constitution;
- (b) if income is derived from the exploitation rights of the film—
 - (i) by a person who acquired the exploitation rights in respect of that film prior to the date that the principal photography of that film commenced; or
 - (ii) by a person who acquired the exploitation rights in respect of that film after the date that principal photography of that film commenced but before the completion date of that film if consideration for those exploitation rights was not directly or indirectly paid or applied for the benefit of a person contemplated in subparagraph (i); and
- (c) to the extent that the income is received or accrues within a period of 10 years after the completion date of that film.

(3) No exemption shall be allowed under this section to a person that is a broadcaster as defined in section 1 of the Broadcasting Act, 1999 (Act No. 4 of 1999), or any person that is a connected person in relation to that broadcaster.

- (4) (a) Any—
- (i) special purpose corporate vehicle; or
 - (ii) collection account manager that—
 - (aa) manages exploitation rights under a collection account management agreement; and
 - (bb) is approved by the Minister for the purpose of this section by notice in the *Gazette*,

must provide a report to the National Film and Video Foundation containing such information, within such time and in such manner as is prescribed by the Minister when income arising from exploitation rights of a film is distributed to a person within a period of 10 years commencing from the completion date of the film.

(b) The National Film and Video Foundation must provide a report annually to the Minister in respect of all films approved in terms of subsection (2)(a) containing such information, within such time and in such manner as is prescribed by the Minister for a period of 10 years commencing from the completion date of a film if—

- (i) any income is received or accrues in respect of the film; and
- (ii) the income is eligible for the exemption under subsection (2).

(5) (a) Notwithstanding section 23(f), a taxpayer may deduct from the income of the taxpayer an amount in respect of any expenditure incurred to acquire exploitation rights in respect of a film in accordance with paragraph (b).

(b) The amount of the deduction contemplated in paragraph (a) is equal to the amount of any expenditure incurred as contemplated in that paragraph less any amount received or accrued during any year of assessment in respect of that film.

(c) No deduction may be made under this subsection to the extent that the expenditure was funded from a loan, credit or similar financing.

(d) The deduction contemplated in paragraph (a) may only be made in any year of assessment commencing at least two years after the completion date of the film to the extent that the amount of expenditure incurred exceeds the total amount received by or accrued to that taxpayer in respect of the exploitation rights.

(e) Subsection (2) and paragraph (a) of this subsection cease to apply to any income derived from a film in any year of assessment subsequent to the date of a deduction made under paragraph (a) in respect of that film.

(6) (a) In addition to the exemption under subsection (2), any amount received by or accrued to a special purpose corporate vehicle by way of a grant payable by the State under the South African Film and Television Production and Co-production Incentive administered by the Department of Trade and Industry shall be exempt from normal tax subject to section 8(4).

(b) Where a special purpose corporate vehicle that received a grant contemplated in paragraph (a), or to whom such grant has accrued, pays the whole or any portion of the amount of the grant to another person pursuant to any exploitation rights in respect of that film, the exemption under this paragraph must also apply to the amount received by or accrued to that other person to the extent that the amount does not exceed any amount that the other person contributed to the production of the film.

Section 12P – Exemption of amounts received or accrued in respect of government grants

12P. Exemption of amounts received or accrued in respect of government grants.—(1) For the purposes of this section—

“**allowance asset**” means an asset as defined in paragraph 1 of the Eighth Schedule, other than trading stock, in respect of which a deduction or allowance is allowable in terms of this Act for purposes other than the determination of any capital gain or capital loss;

“**base cost**” means base cost as defined in paragraph 1 of the Eighth Schedule;

“**government grant**” means a grant-in-aid, subsidy or contribution by the government of the Republic in the national, provincial or local sphere.

(2) There must be exempt from normal tax any amount received by or accrued to a person as a beneficiary of a government grant if that government grant—

- (a) is listed in the Eleventh Schedule; or
- (b) is identified by the Minister by notice in the *Gazette* for the purpose of exempting that government grant with effect from a date specified by the Minister in that notice (including any date that precedes the date of that notice), after having regard to—
 - (i) the implications of the exemption for the National Revenue Fund; and
 - (ii) whether the tax implications were taken into account in allocating that grant.

(2A) Notwithstanding subsection (2), there must be exempt from normal tax any amount received by or accrued to or in favour of any person from the Government in the national, provincial or local sphere, where—

- (a) that amount is granted for the performance by that person of its obligations pursuant to a Public Private Partnership; and
- (b) that person is required in terms of that Public Private Partnership to expend an amount at least equal to that amount in respect of any improvements on land or to buildings owned by any sphere of government or over which any sphere of government holds a servitude.

(3) Where during any year of assessment any amount is received by or accrues to a person by way of a government grant as contemplated in subsection (2) or (2A), other than a government grant in kind, for the acquisition, creation or improvement, or as a reimbursement for expenditure incurred in respect of the acquisition, creation or improvement of—

- (a) trading stock—
 - (i) any expenditure incurred in respect of that trading stock allowed as a deduction in terms of section 11 (a); or
 - (ii) any amount taken into account in respect of the value of trading stock as contemplated in section 22 (1) or (2); or
- (b) an allowance asset, the base cost of that allowance asset,

must be reduced to the extent that the amount of that government grant is applied for that purpose.

(4) Where any amount is received by or accrues to a person by way of a government grant as contemplated in subsection (2) or (2A) for the acquisition, creation or improvement of an allowance asset or as a reimbursement for expenditure incurred in respect of that acquisition, creation or improvement, the aggregate amount of the deductions or allowances allowable to that person in respect of that allowance asset may not exceed an amount equal to the aggregate of the expenditure incurred in the acquisition, creation or improvement of that allowance asset, reduced by an amount equal to the sum of—

- (a) the amount of the government grant; and
- (b) the aggregate amount of all deductions and allowances previously allowed to that person in respect of that allowance asset.

(5) Where during any year of assessment any amount is received by or accrues to a person by way of a government grant as contemplated in subsection (2) or (2A), other than a government grant in kind—

- (a) for the purpose of the acquisition, creation or improvement of an asset other than an asset contemplated in subsection (3) or (4); or
- (b) as a reimbursement for expenditure incurred for the acquisition, creation or improvement of an asset other than an asset contemplated in subsection (3) or (4),

the base cost of that asset must be reduced to the extent that the amount of the government grant is applied for that acquisition, creation or improvement.

(6) (a) Where during any year of assessment—

- (i) any amount is received by or accrues to a person by way of a government grant as contemplated in subsection (2) or (2A), other than a government grant in kind; and
- (ii) subsection (3), (4) or (5) does not apply to that amount,

any amount allowed to be deducted from that person's income in terms of section 11 for that year of assessment must be reduced to the extent of the amount of that government grant.

(b) To the extent that the amount received or accrued by way of a government grant exceeds the amount allowed to be deducted as contemplated in paragraph (a), that excess is deemed to be an amount received or accrued in respect of that government grant during the following year of assessment for the purposes of paragraph (a).