The Section 481 Film/TV Tax Credit

**32%**

*of eligible expenditure*

**90%**

*of tax credit may be paid up-front*

In January 2015 the Irish government introduced dramatic changes to Ireland's film/television tax incentive, Section 481 of the Taxes Consolidation Act 1997 (**Section 481**). Section 481 had previously operated as tax break for private investors who subscribed for shares in a single-purpose film or television production company. The tax break was effectively "shared" between the private investors and the film production company, thus producing a negotiated net benefit for each production.

Following a cost benefit analysis by the Irish government, a decision was made to overhaul Section 481 in order to eliminate from the process both private investors and the associated fundraisers and advisors. Section 481 has now been converted into a tax credit payable in cash to a "producer company".

Some key features of the new tax credit are as follows:

- The tax credit has an enhanced value equal to 32% of the eligible expenditure on the film or television programme. (This compares with a typical net benefit of approximately 28% under the old incentive.) If eligible expenditure as a proportion of the total production budget is greater than 80% the tax credit is capped at 32% of 80%.
- The tax credit is available for feature films, television drama, animation and creative documentaries.
- Under the new tax credit the costs of all individuals (irrespective of residency or nationality) represent eligible expenditure in respect of their time working in Ireland. This means that expenditure on US cast and other non-EU personnel now attracts the Section 481 tax credit.
- Simultaneously with the introduction of the new tax credit the government introduced a withholding tax on payments to non-EU/EEA artists (which principally means actors and voice over artists) for work done in Ireland. The withholding tax also applies to artists using loan-out companies. The rate of the withholding tax is 20%, but expenses incurred by the artist (such as manager's and agent's fees, travel expenses etc) are deductible for this purpose.
- The tax credit is made available to a "producer company" which meets certain criteria. Those criteria include a requirement that the company's tax affairs (and those of a range of related parties) are in order. For practical purposes the producer company must have been trading for a period of approximately 21 months prior to making an application.
- After a successful application by a producer company for a certificate under Section 481, the tax credit is payable to the producer company in repayment of a notional overpayment of corporation tax.
- The producer company must incorporate and own a single-purpose "qualifying company" to which it must pay an amount not less than the amount of the tax credit. The qualifying company must incur all of the eligible expenditure on the project.
- An unusual feature of the new tax credit is the fact that 90% of the tax credit may be paid up-front (i.e. before the relevant expenditure is incurred) provided that certain conditions are met. The remaining 10% is payable on submission of a compliance report following completion of the film/TV programme.
- Alternatively the producer company can wait until completion of the production before claiming 100% of the tax credit.
- In certain circumstances the entitlement to the tax credit may be withdrawn. In the event of a claw-back of the tax credit the directors of the producer company and the qualifying company respectively, as well as significant shareholders in the producer company, are liable.

A number of these features are addressed in more detail below, as are some practical notes on the operation of the new tax credit.

## Who is entitled to the tax credit?

The applicant for a tax credit must be a "producer company" which (among other things):

- is resident in Ireland or in another EEA state and carries on business in Ireland through a branch or agency
- carries on the trade of producing films for cinema exhibition or broadcast (including internet broadcast) on a commercial basis
- is not a broadcaster or connected to a broadcaster or a member of a group whose business consists wholly or mainly of transmitting films via the internet
- is tax-compliant

A producer company is not required to hold the copyright or any exploitation rights in the project. It must hold 100% of the shares in a separate "qualifying company", and the qualifying company must actually incur all of the eligible expenditure on the film or programme. Thus the producer company does not incur eligible expenditure itself, but it must pay to the qualifying company an amount not less than the amount of the tax credit.



7/8 Wilton Terrace, Dublin 2, Ireland

**32%**

*of eligible expenditure*

**90%**

*of tax credit may be paid up-front*

## How is the tax credit calculated?

The tax credit is equal to 32% of the "eligible expenditure" on a project, with the eligible expenditure being limited for this purpose to 80% of the total production budget. Eligible expenditure in this context means (a) expenditure on the employment of individuals on the production of the project in Ireland and (b) expenditure on goods, services and facilities provided in Ireland by a person with a fixed place of business in Ireland. In order for a film or programme to qualify for the tax credit, eligible expenditure must be no less than €125,000 and the total production budget must be no less than €250,000. At the other end of the scale, the eligible expenditure amount upon which the tax credit is calculated for a single project may not exceed €50,000,000.

## How is the tax credit delivered?

The tax credit takes the form of a refund of corporation tax notionally overpaid in respect of the last complete accounting period for which a corporation tax return was made by the producer company prior to the date on which the application for a certificate under Section 481 is made. Upon the issue of a certificate following application to the Revenue Commissioners, the producer company may adjust its corporation tax return for the relevant accounting period in order to crystallise the overpayment of tax and, accordingly, the entitlement to the tax credit.

This delivery mechanism means in practice that a producer company must have been in business for approximately 21 months before it is eligible to make application for a tax credit. Potential applicants who do not own an Irish company that has a sufficient trading history must therefore seek to collaborate with an established producer company (unless they are in a position to to acquire such a company).

## When is the tax credit payable?

Following completion of the project and submission to the Revenue Commissioners of a compliance report and audited accounts in accordance with the Film Regulations 2015, the tax credit is generally payable within 30 days (subject to the provisions of Section 481 and those regulations). However it is possible to accelerate the payment of 90% of the anticipated value of the tax credit in any one of the following scenarios:

- If the Revenue Commissioners are satisfied that the financing contracts are in place and the conditions to the commencement of funding pursuant to those contracts have been satisfied. This may be evidenced by (a) a letter from a law firm representing the producer company confirming the position in relation to financing contracts and (b) a letter from an accountancy firm representing the producer company confirming that it has reviewed the cashflow for consistency with the financing contracts and certifying that the aggregate sums paid to date into to the qualifying company's production account is not less than 68% of the eligible expenditure amount on which the tax credit is based.
- For projects funded by the Irish Film Board (IFB) or the Broadcasting Authority of Ireland (BAI), on written confirmation from IFB or BAI (as applicable) that it has completed its due diligence and agreed to release funding to the producer company.
- If a guarantee, surety bond or similar instrument which secures the advance payment of the tax credit is provided to the Revenue Commissioners.

In summary, a typical "financial close" process must be undertaken in order to secure an advance payment of the tax credit, irrespective of which of the above options is chosen. Once the documentation required for the advance payment has been supplied to the Revenue Commissioners 90% of the tax credit will generally be paid soon (although not less than seven days) afterwards.

## What contractual structure should be used?

The only express requirement of the legislation in terms of contractual structure is that the producer company must contract with the qualifying company and must pay to the latter company an amount not less than the amount of the tax credit. That payment may take the form of a fee or a loan or indeed any other form; the legislation seeks to prevent any potential advantage or disadvantage from accruing to either company in relation to such payment by clarifying that it does not represent taxable income of the qualifying company, nor does it constitute a tax-deductible expense of the producer company.

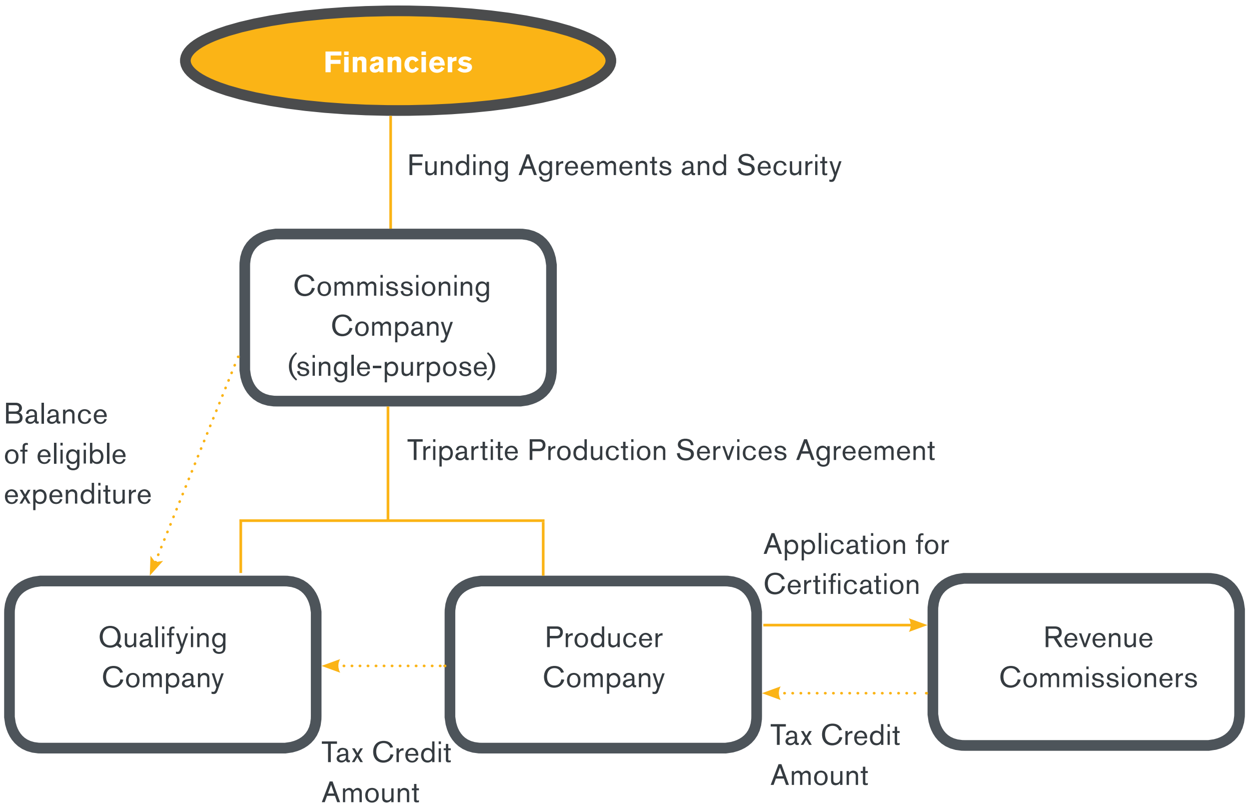
The simplest structure therefore is for an established producer company itself to contract with all co-producers and financiers and for that company in turn to engage the qualifying company under a simple production services agreement, pursuant to which the producer company would agree to pay the qualifying company an amount equal to 100% of the budgeted eligible expenditure.

However some producers may be well advised to incorporate a special purpose commissioning company to contract with the funders and, in turn, with both the producer company and the qualifying company. A number of considerations are relevant in that context, including:

- If the producer company is a producer's principal trading entity, potential financiers of a specific project may be concerned about unknown risks in the company that could affect their project. That is a concern that is likely to be magnified the longer a company has been operating as a producer company and incurring the associated commitments and liabilities.
- If on the other hand all rights and other assets relating to the project are passed directly by the (single purpose) qualifying company to a single purpose commissioning company, the insolvency risk associated with the project is significantly reduced and the chain of title is simplified. It also means that the financiers of the project can contract with (and where applicable take security over) a "clean" company.

The following diagram illustrates how such an alternative financing structure would work in practice. Where the non-Section 481 financing of a project is complex and/or the funders wish to take security over the project assets, this structure is generally preferable to one in which the producer company contracts with all funders.

## Optimal financing structure - in practice




## Conclusion

Although it is still early in the life of the new Section 481 tax credit, to date it has been operating efficiently in practice and the enhanced net benefit is a very welcome boost to the Irish film and television industry.

For further information please contact a member of Philip Lee's media team.

**JONATHAN KELLY**
PARTNER
jkelly@philiplee.ie
+353 1 237 3700

**BRIAN GORMLEY**
PARTNER
bgormley@philiplee.ie
+353 1 237 3700

Please note that the content of this update is for information purposes only and does not constitute legal advice.