

International Tax Systems and Planning Techniques

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B2 France

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B2.1 Introduction

France is in many cases viewed as one of the less attractive among the member states of the EU. The burden of taxation (one of the heaviest in the OECD) and the complexity of administrative formalities are deemed obstacles that do not encourage the setting up of businesses in France.

The French Government has been aware of this matter for a couple of years. In this respect, some measures were taken to encourage the economic growth of enterprises and foreign groups that wish to locate business in France. Among these measures, the Economic Initiative Act (or *Dutreil* Act) was approved on 21 July 2003; it set out a simplification of administrative formalities and registrations required in order to set up a business or incorporate a company. From a tax point of view, this Act provides for a reduction of the burden of taxes on entrepreneurs, such as income tax, wealth tax, death duties, and tax on professional capital gains.

Previously, from a corporate income tax point of view, the 2002 Finance Act carried out the full implementation of the EC Merger Directive regime of 14 June 1990. Firstly, it set out a new definition of the restructurings deemed as mergers from a tax point of view and that are eligible for the favourable tax regime, which is in accordance with the Directive; particularly, the new definition includes the case where a 100% subsidiary is absorbed by its parent company (*confusion de patrimoine* set forth in art 1844-5 of the French Civil Code) and allows, from a practical point of view, partial spin-off followed by the direct allocation of the transferee company's interest to the transferor company's shareholders. The Act has also provided for the application of said regime to cross-border mergers provided that both companies (transferor and transferee) are resident in a country that has entered into a treaty with France for administrative assistance for preventing fraud and tax evasion. Lastly, it must be noted that the rules governing the treatment of losses have been modified in order to facilitate their transfer. Nevertheless, there are still reforms to be made, such as the partial spin-off regime that, under the present rules, induces a double economic taxation of the same capital gains, despite the approach of the aforesaid Merger Directive according to which the restructuring of companies should be tax neutral.

The 2003 Finance Act provided for a new tax regime available to quoted real estate investment companies (called SIIC), as it has existed for some years in Belgium and in the Netherlands. These provisions, provided by art 208C of the French Tax Code, allow quoted real estate investment companies to benefit from an exemption from corporate income tax on profits derived from the rental of their real estate assets or on capital gains pertaining to such assets, provided that they distribute 85 per cent of the said profits and 50 per cent of the said capital gains on a yearly basis. In this respect, it should be noted that the regime, which in other words allows the eligible companies to benefit from tax transparency whereas they are normally subject to corporate tax, would allow foreign real estate investment funds to invest more efficiently in real estate in France, whether directly or indirectly. Furthermore, art 208C does not provide for any limitation on the proportion of the shares that can be held by non-residents (contrary to the Dutch regime that does not apply to companies of which 25 per cent or more of the share capital is held by a company non-resident in the Netherlands) (see **B2.2.4** and **B2.13**).

Recently, a parliamentary amendment to the 2004 Finance Act put an end to a peculiarity of the French tax system that is very detrimental to non-resident companies. According to art 244 bis A of the French Tax Code, capital gains realised by non-resident individuals and companies on the sale of their real estate (or shares held directly or indirectly in real estate legal entities) located in France are subject to a specific taxation that is equal to a third of the amount of the said capital gains (*prélèvement du tiers*, 33.33% levy). Non-resident companies are also subject to corporate income tax if they have a permanent establishment in France. In such a case, the amount of the 33.33% levy can be offset against that of the corporate income tax, but any excess of the 33.33% levy could not be

refunded. Fortunately, the said amendment provides for such refund ending the discrimination that had been introduced by article 244 bis A (see **B2.13.3**).

Additionally, the 2004 Finance Act provides for a deep reform of the taxation of dividends applicable to distributions made as from January 2005. The tax credit on dividends called "*avoir fiscal*" (see **B2.5.1**) and equalisation tax called "*précompte*" that taxpayers subject to corporate income tax have to pay upon certain distributions they made to their shareholders will be replaced by a 50 per cent allowance on the net dividends received by individuals. From a general point of view, the new system will be more understandable and easy to apply, but it will penalise foreign tax residents who will no longer be qualified to obtain, in whole or in part, the refund in cash of the *avoir fiscal* or in certain cases *précompte*, and corporate shareholders that do not satisfy the requirements of the parent/subsidiary regime (for instance, due to the fact that they do not hold 5 per cent of the affiliate) and consequently will be subject to a double economic taxation on the same profits, firstly at the level of the affiliates' tax results and secondly in their own hands.

The 2005 Finance Act provides for an exemption of the taxation of the long-term capital gains derived from the sale of participation shares as from 1 January 2007. Such exemption should allow France to compete with other EU countries, such as the Netherlands and Luxembourg, whose tax system provides for a participation exemption regime. Other long-term capital gains will continue to benefit from the regime reduced rate of 15 per cent.

Such reforms show that the French legislator intends to implement and enforce the EC law as well as the double tax treaties approach. However, this role may be played by the courts. For instance, the French administrative Supreme Court (*Conseil d'Etat*) stated in 2002 that the French Controlled Foreign Companies tax regime was contrary to the French-Swiss double tax treaty. In the same way, the Court of Justice of European Communities (CJCE) ruled that the exit tax applicable to French-resident individuals contravenes the freedom of establishment principle set forth in article 43 of the EC Treaty. The 2005 Finance Act has, therefore, (i) abolished the "exit tax" that was levied on certain hidden capital gains on the date of the transfer of the French individuals outside France and (ii) modified the CFC system set out in art 209B of the French Tax Code to restrict the application field to pure artificial scheme with respect to EU companies.

In some cases, the effect of double tax treaties combined with the interpretation of such by the French and foreign domestic case law results in a double exemption of profits. It is notably the case when a Luxembourg company owns directly real estate in France. In such a case, provided that the Luxembourg company has no permanent establishment in France, income deriving from French real estate, as well as capital gains pertaining to the sale of such real estate, is not subject to corporate income tax, neither in France nor in Luxembourg.

B2.2 Types of commercial enterprise

There are many enterprise forms available to conduct a business in France, and care should be taken as to which is the most suitable in all the circumstances, since the tax treatment may differ greatly. Bearing in mind that French corporate law is not within the scope of this book, only a brief synopsis of the various types of legal entities is listed below.

B2.2.1 Companies

- (i) *Société anonyme* (SA) is the most common form of company, both private and public. It must have a minimum of seven shareholders, who may be resident or non-resident. The minimum capital of an SA is €37,000 authorised and issued, of which at least 25 per cent must be paid up upon incorporation, with the balance of 75 per cent required to be paid up within five years following incorporation. The minimum capital for an SA seeking funds from the public is €225,000. The cost of incorporating an SA with a capital of €37,000 is approximately €2,500 plus professional fees, the process taking at least six weeks (three weeks to obtain registration with the Commercial Court and three weeks to obtain registration with the National Institute of Statistics and Economic Studies (INSEE)). In the event of contribution of *inter alia* a going concern or immovable assets by a shareholder who is not subject to French corporate income tax