France

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General

1. What are recent tax developments in your country which are relevant for M&A deals?

- Horizontal tax consolidation

Following the decisions by the Court of Justice of the European Union (CJEU) (regarding the Dutch tax consolidation regime, which is similar to the French one) and by a French court (regarding the French regime), which ruled that the French tax provisions which prohibit the tax consolidation of French subsidiaries controlled by the same EU parent company violate the freedom of establishment, the second Amended Finance Bill for 2014 extended the situation in which companies can set up a tax consolidated group in France. Indeed, it is now possible, subject to conditions, to set up “horizontal” tax groups in France, i.e. to consolidate, for tax purposes, French subsidiaries controlled by a foreign EU parent company if the following conditions are met:

- all companies are subject to corporate income tax (or similar income tax) under the standard regime;
- the French companies are directly or indirectly held at more than 95% by the same EU parent company;
- the EU parent company is not held at more than 95% by another EU company subject to corporate income tax (or similar income tax);
- all companies members of the so-called “horizontal” tax group have the same opening and closing date.

These new provisions came into force for financial years closed on or after 31 December 2014.

From a practical standpoint, the enlargement of cases where a tax group may be created between French companies may also help avoiding some post-acquisition relocation of shares, especially in cases of build-up.

- About French tax consolidation rules

On 2 September 2015, the CJEU ruled that the French tax consolidation rules as regards the tax treatment of dividends distributed between companies that are member of the same tax group violate the freedom of establishment and the rules make it less attractive for companies with EU subsidiaries to exercise that freedom because they would be deterred from settings up subsidiaries in other Member States (CJEU, 02/09/2015, aff. C-386/14, Steria).

The French tax consolidation regime has been amended to bring French law into compliance with European law (amending the finance law for 2015). The new regime applies from fiscal years beginning from 1 January 2016.

As a reminder, according to the former regime, the taxation of dividends is limited to a 5% lump sum (parent subsidiary regime). The 5% lump sum was neutralised in case of a dividend distribution carried out between companies members of the same tax consolidated group. Based on these provisions, dividends received by French companies from its EU subsidiaries that would have fulfilled all conditions to become members of a tax consolidated group if they had been incorporated in France, were subject to CIT up to the 5% lump sum without any neutralisation. This difference based on the state of incorporation of the distributing company has been considered as non-compliant with the freedom of establishment.

According to the new regime, the lump sum is reduced from 5% to 1% in the following cases:

- Dividends distributions within a tax consolidated group or/and;
- Dividends distributions received by a company member of a tax consolidation group and paid by another company in the group or by a company located in the EU which is subject to a similar corporate income tax, provided that these companies meet the conditions which would enable it to be a member of the tax consolidated group if the company was located in France.

It should be noted that the 1% lump sum is not neutralised even in the cases where both the distributing and the receiving companies are members of the same tax consolidated group.

However, it should be noted that for dividends received from French companies owned at 95% or more but which is not a member of the tax consolidation group, the lump sum is 5%.

2. What is the general approach of your jurisdiction regarding the implementation of OECD BEPS actions (Action Plan 6 specifically) and, if applicable, the amendments to the EU Parent-Subsidiary Directive?

The 2014 Finance Bill introduced a new anti-hybrid financing measure limiting the deductibility of interests accrued to related party lenders. The right to deduct interest on loans paid between related parties is subject to the following new demonstration: the borrower must be able to prove, upon the tax authorities' request, that, for the current fiscal year, the lender is subject to a corporate income tax on the interest income received which is equal to at least 25% of the corporate income tax that would be due if computed under the French general rules (i.e., 8.33%) without consideration of the effective tax payment by the lender. The new rule is applicable to the fiscal year ending on or after 25 September 2013.

The anti-hybrid rule represents France's first concrete step to give effect to the OECD base erosion and profit shifting (BEPS) project.

On 27 January 2015, the Council adopted an anti-abuse rule about the parent subsidiary regime.

This clause has been transposed in identical format into French law by the amended Finance Act for 2015. Under this amended, the parent subsidiary regime is not applicable " to an arrangement or a series of arrangements which, having been put into place for the main purpose or one of the main purposes of obtaining a tax advantage that defeats the object or purpose of this Directive, are not genuine having regard to all relevant facts and circumstances. An arrangement may comprise more than one step or part. (…) An arrangement or a series of arrangements shall be regarded as not genuine to the extent that they are not put into place for valid commercial reasons which reflect economic reality".

The new clause is applicable for fiscal years as from 1 January 2016.

3. What are the main differences among acquisitions made through a share deal versus an asset deal in your country?

The main difference between share deals and asset deals is that the target company's historical liabilities are transferred when the transaction is structured as a share deal (with a normal three-year statute of limitation, which can in some circumstances be extended to ten years). Asset deals (i.e. straight sales of assets or going concerns) do not result in the transfer of pre-closing liabilities relating to the assets or going concern being transferred (except for the going concern's taxes on assets or activities transferred in the year the transaction occurs, for which the buyer may become jointly liable for a limited period of time).

Asset deals generally trigger a higher tax cost for the buyer. Indeed, acquiring shares of a target company is subject to reduced registration duties, the rate of which depends on the target's corporate form (i.e. for Société Anonyme (SA) or Société par Actions Simplifiés (SAS) – shares, the rate is 0.1% of the sale price). For other company shares, except for real estate companies (see 'special considerations for companies whose main asset is real estate' below) the rate is 3% of the sale price (or of the fair market value, if higher than the price agreed). An allowance is deductible from the basis assessment of registration duty. This allowance is equal to the ratio of the number of shares purchased divided by the total number of shares issued by the acquired company, multiplied by €23,000.

Some operations can be exempted from registration duty, in particular the acquisition of shares between companies forming part of the same group (controlled companies as defined by article L 233-3 of the Trade Code or tax-consolidated group), acquisition of shares further to operations (such as contribution of shares for shares and mergers) carried out under merger neutrality regimes, or acquisition of shares in companies placed under a safeguard procedure or judicial restructuring.

Asset deals, if the assets qualify all together as a going concern, are subject to transfer tax at:

- 0% up to €23,000;
- 3% from €23,000 to €200,000;
- 5% of the sale price exceeding €200,000;
- Or for real estate assets (at a rate of 5.09% plus additional duties).

From a VAT standpoint, both deals should be neutral, provided the assets sold all together form a going concern. It should be noted that VAT implications may arise for sales of isolated assets or real estate assets.

From a corporate income tax standpoint, share deals do not impact the ability of the target company to carry forward Net Operating Losses (NOLs), which remain available in normal circumstances (see section 6 below).

In asset deals, only assets are transferred – any NOLs remain with the target company. In addition, share deals (structured as straight sales) do not allow, in principle, any step-up in basis value and do not impact the target company's amortisation plan of its assets (in terms of duration and depreciation value). But asset deals mechanically imply a step-up in the assets' amortisation basis, which then corresponds to the purchase price paid allocated to each asset. However, in both cases no goodwill may be amortised. It should also be noted that, in the case of an acquisition mainly from treated parties at a price higher than the fair market value, the tax authorities could further challenge the allowance but not the amortisation basis.

Finally, there are other slight differences between share deals and asset deals. For instance, in share deals, the target company's business tax (so-called contribution économique territoriale) liability is not impacted in any way. But asset deals could allow the buyer, subject to certain circumstances, to fall outside the scope of the business tax if the buyer is not the owner of the assets or going concern transferred on 1 January of the year the transaction occurs.

Buy-side

4. What strategies are in place, if any, to step up the value of the tangible and intangible assets in case of share deals?

As a general principle, share deals do not allow any step-up in value of any of the target company's assets. Prior to the sale, however, the target company may consider a global step-up of all its tangibles and financial assets. It should be noted that capital gains are booked as non-available reserves and trigger taxation at the normal corporate income tax rate (of 34.43% globally).

Tax-free restructurings (i.e. merger favourable or merger neutrality regimes allow benefiting from deferred taxation on capital gains on assets transferred by the merged or the contributing company) may also be contemplated. Such operations generally do not offer step-up opportunities when implemented between related parties. However, such operations are performed at fair market value and therefore allow a step-up in basis when implemented between two independent parties (subject to additional conditions).

In parallel, a contribution of an isolated asset (such as real estate property or trademarks under conditions) to the target company prior to the sale is treated for tax purposes as a straight sale and allows a transaction at fair market value. In that case the value of shares of the target company that has benefited from the contribution corresponds to the fair market value of isolated assets contributed. But such an operation triggers capital gains subject to tax at the normal corporate income tax rate and may not benefit from the merger-favourable regime and can imply registration duty exposures.

Operations such as straight sales or contributions of isolated assets within a tax-consolidated group are made at fair market value, while the related taxation is postponed until the end of the tax-consolidated group, the exit of the tax-consolidated group of one of the two companies, or the assets sold to a company that is not a member of the tax-consolidated group (correlatively, amortisation on the re-evaluated value is not possible).

5. What are the particular rules of depreciation of goodwill in your country?

In principle, the amortisation of goodwill is not allowed in France, either in share deals or asset deals. However, in some specific cases, pursuant to the regulation of the ANC dated 23 November 2015, depreciation can be recorded in the case there is any time limit on the use of the business asset (for example: concession).

Moreover, the regulation of the ANC also amended the accounting treatment of a "technical loss" resulting from a merger carried out at the net accounting value (difference, up to the latent capital gain on assets received in the frame of the merger, between (i) the net accounting of the shares held by the absorbing company in the absorbed one; and (ii) the net asset value of the absorbed company). This "technical loss" was in principle recorded in the balance sheet of the absorbing company as a "goodwill" that could not be depreciated either from an accounting or tax standpoint.

Now, from an accounting purpose, if possible, such "technical loss" must be allocated to the underlying assets it relates to and be depreciated following the depreciation rules applicable to said underlying asset.

From a tax perspective, the depreciation of a business asset is not allowed. Therefore, extra-accounting adjustments will be necessary.

6. Are there any limitations to the deductibility of interest on borrowings?

There are several rules that relate to the deductibility of interest on borrowings.

Interest rate limitation

Under the interest rate limitation when interest expenses are paid to a direct shareholder, the annual deductible interest rate is capped at a rate determined by the Tax Administration (e.g. 2.15% for the full year closed on 31 December 2015). However, when interest is paid to a related-party company (whether shareholder or not), the annual tax-deductible interest rate can be higher, provided the borrowing entity may demonstrate, with the provision of a dedicated supporting file, that this rate is at arm's length (i.e. a rate the company could have obtained from third party financial institutions in similar circumstances).

Anti-hybrid legislation

The deduction of loan interest paid by a company subject to corporate income tax to a related company is allowed provided that the lender is subject to tax on profits on the interest received amounting to at least 25% of the tax as determined under French tax rules (i.e. 8.33%) This mechanism was enacted to limit the use of hybrid instruments which take advantage of different legal qualifications of the same flow between two countries and allowing the deduction of the financial interest accrued in France and the exemption of the corresponding interest income received by the lender abroad. This rule is applicable to interest incurred since 25 September 2013, irrespective of the date the loan was granted.

Thin capitalisation rules

The amount of interest paid to related entities which exceeds the highest of the three following thresholds will not be tax deductible on a standalone basis:

- First threshold: amount of interest computed on one and a half times the net equity, i.e., the interest deductibility is limited by the following ratio: "net equity: debt from related parties = 1:1.5";
- Second threshold: 25% of the ordinary income before taxes, amortisation and interest paid to related entities;
- Third threshold: interest received from related parties.

In addition, third-party loans (including bank debt) which are guaranteed by a "related party" to the borrower are deemed to be related party debt for thin capitalisation purposes (or loans granted by a non-related company, guaranteed by a non-related company itself guaranteed by a related company to the borrower).

Moreover, it should be noted that specific rules apply within a tax-consolidated group. Indeed, subject to limitations, the parent company could be allowed to deduct from the group taxable income all or part of the non-deductible interest as determined on a standalone basis.

Finally, if the accounting consolidated group's debt/equity ratio is higher than the borrowing entity's own debt/equity ratio, the limitation on the deduction of interest paid to related entities will not apply.

The consolidated group is defined as all the French and foreign entities under the control of the same ultimate parent company.

For the purposes of this comparison, only debts owed to third parties are taken into account for computing group's debt/equity ratio, though both debts owed to third parties and related entities are taken into account for the computation of the debt/equity ratio of the borrowing entity.

In any case, if the fraction of non-deductible interest is lower than € 150K, there will be no limitation.

The non-deductible fraction of interest due on the application of the thin capitalisation provision may be carried forward to the following tax year (Y+1) and offset against 25% of the ordinary income before taxes and depreciation of fixed assets. The remaining amount may then be carried forward to the following tax years but with an annual deduction of 5%.

Acquisition of shares not controlled from France (*Carrez* amendment)

The deductibility of financial expenses linked to acquisition of shares qualifying as controlling interest is limited. Financial expenses are only deductible if the purchaser can demonstrate that it (or a company incorporated in France and belonging to the same economic group) actually makes the decisions relating to these shares and that it exercises a control or influence over the acquired company.

If the company fails to provide such evidence, a fraction of the expenses must be added back to its taxable income for the acquisition accounting period and the following eight years.

However the limitation does not apply when:

- The value of shares held by a company is less than €1 million;
- The acquisition has not been financed by a loan;
- The debt ratio of its group is higher or equal to the purchaser's own debt ratio.

Proportional interest deduction restriction "French rabot"

Deduction of financial expenses of companies is now subject to a general limitation. For the accounting period ended as of 31 December 2012 companies have to add-back to their taxable result 25% of their "net financial expenses".

"Net financial expenses" are defined as the difference between the total amount of financial expenses incurred as a consideration for financing granted to the company and the total financial income received by the company in consideration for financing granted by the latter. Rents incurred under a moveable properties rental agreement between related parties or a leasing agreement are included in financial expenses after deduction of the amortisation, financial amortisation of the lessor and all costs invoiced by the lessee.

In a tax consolidated group, this limitation applies at the level of the tax result of the group.

There is no carry-forward mechanism of disallowed interest.

This limitation will not apply if the company's net financial expenses (or net financial expenses of the group for tax consolidation) are lower than €3 million.

Financial expenses related to the acquisition or building of assets within the framework of public utilities' delegation, concession of public engineering and public-private partnership agreements or an administrative long-term lease concluded before 28 December 2012 are all excluded from this mechanism.

7. What are usual strategies to push down the debt on acquisitions?

The most straightforward solutions to push-down debt consist of a dividend distribution up to the target company's distribution capacity or the relocation of assets between the target company and an affiliated company. Both operations would be financed by a loan granted by an affiliated company or third party (e.g. a bank).

As a consequence, the strategy in a debt push-down could consist of the creation of or increase in dividend distribution capacities (based on accounting rules) without triggering tax consequences. Such an outcome may be reached through operations made at fair market value with a limited tax impact, such as the straight sale of shares benefiting from the participation exemption regime (i.e. with an effective tax rate of 3.44%).

Another solution could be a relocation of assets (e.g. shares) held by the target company under the target company's subsidiary. Such an acquisition could be financed by debt. Further to this operation, the target company could distribute the capital gain realised to the holding company. In order to be tax neutral, the relocation of assets other than shares benefiting from the participation exemption regime could be contemplated between companies members of the same tax-consolidated group (see section 2 above and section 9 below).

French tax authorities try to deny the deduction of the interests related to the acquisition of a company if the holding company decides to merge the target company in a short period of time after the acquisition. However, the French tax authorities recently decided to allow the realisation of a quick merger between two holding companies, namely in the case of a secondary leveraged buy-out.

In any case, these schemes have to be analysed in light of French commercial law, which prohibits a company from financing its own acquisition.

8. Are losses of the target company(ies) available after an acquisition is made?

The acquisition of the target company's shares does not have any impact on the amount of the available losses carried forward by the target company. As a general principle, losses carried forward are not available unless the target company changes its activity.

An addition of business activity can characterise a change in activity when, during the fiscal year during which it occurs or the following fiscal year in comparison with the fiscal year preceding the change, there is an increase of more than 50% of:

- The company's turnover;
- The average number of staff and the gross amount of fixed assets.

A surrender or transfer, even partial, of a business activity can also characterise a change in activity if there is a decrease of more than 50% of the previous requirements.

However, if the target company, which owns losses, is merged into another company, the losses can be transferred to the merging company only if an agreement is given by the French Tax Authorities. In particular the activity of the merged company has to be maintained for at least three years. The transfer of tax losses is not allowed if the merged company is a holding company. Attention also has to be paid to the consequences of such merger on the merging entity's right to carry forward its own standalone tax losses further to the merger (i.e. impact on its own activity).

9. Is there any indirect tax on transfer of shares (stamp duty, transfer tax, etc.)?

The acquisition of shares is subject to reduced registration duties. The rate depends on the target company's corporate form. For SA or SAS companies, the rate is 0.1% of the sale price. For other company shares, except for real estate companies (see section 8 below), the rate is 3% of the sale price. An allowance is deductible from the basis of assessment of the registration duty. This allowance is equal to the ratio of number of shares purchased divided by total number of shares issued by the acquired company, multiplied by €23,000.

10. Are there any restrictions on the deductibility of acquisition costs?

Acquisition costs of shares mainly include registration duties, commissions, fees (auditor fees, external appraiser fees, advisor fees) and deed expenses related to the acquisition.

- From an accounting standpoint, these costs may be taken into consideration in the acquisition cost of the shares or deducted for the FY where they have been incurred.
- From a tax standpoint, the costs incurred to acquire shares qualifying as a controlling interest must be incorporated into the acquisition cost of said controlling interest. However, the deduction of acquisition costs may be spread over a 5-year period. In case of acquisition in the course of a fiscal year, the first annuity is computed pro-rata temporarily.

11. Can VAT (if applicable) be recovered on acquisition costs?

As a matter of principle, based on ECJ case law and guidelines issued by the French tax administration, input VAT on acquisition costs may only be recoverable if the acquiring company provides services subject to VAT to its subsidiaries.

Note, however, that in the case where the acquiring companies would receive non-ancillary financial income, its right to recover input VAT could be reduced.

In principle, the fact that the acquiring company would also receive dividends from its subsidiaries should have no impact on its right to recover input VAT on acquisition costs.

However, it should be noted that, despite the provision of the guideline issued by the French tax authorities (that have not been amended to date) and the ECJ case law, recent case law from French Supreme Court may give some arguments to the FTA to try to limit the possibility to deduct 100% of the input VAT in the case where the acquiring company receives dividends from its subsidiaries.

12. Are there any particular issues to consider in the acquisition by foreign companies? (for example non-resident taxation rules/substance rules and tax efficient exit routes)

We refer to question 17.

13. Can the group reorganise after the acquisition in a tax neutral environment through mergers or a tax group?

Under the Charasse amendment, anti-debt push down regulations provide for a partial recapture of the financial expenses borne by a tax consolidated group in case of transactions deemed to qualify as self-purchases.

The Charasse amendment applies:

- When the shares of a company have been purchased by another company from parties who also directly or indirectly control (de jure or de facto) the acquiring company at the time of acquisition;
- Where both the acquired company and acquiring company become members of the same tax-consolidated group after the transaction (including by way of merger).

This rule leads to the non-deductibility of the interest expense within the tax consolidated group up to an amount equal to: Financial expenses x [(acquisition price – amount of contribution in cash)/average group debt].

This reinstatement applies to the acquisition accounting period and the following eight years.

The Charasse amendment no longer applies to cases involving a change in control of the acquiring company. Moreover, the Charasse amendment is no longer triggered when a subsidiary held by a company directly acquired by the investor is immediately sold to a French holding company that elects to set up a tax consolidated group.

Mergers, spin-offs or split-offs may benefit from tax neutrality and are generally made within a group at book value.

14. Is there any particular issue to consider in case of companies of which main assets are real estate?

For capital gains tax purposes a real estate company is a company with assets made up of more than 50% of French real estate assets at the date of the transfer or at the closing date of the last fiscal year. Properties used for the purpose of a commercial activity are not deemed to be real estate assets for capital gain purposes.

For transfer tax purposes a real estate company is a company with assets made up of more than 50% of French real estate at any time of the year preceding the sale.

a. Share deal

Capital gains on the transfer of shares in real estate companies subject to corporate income tax are taxed at the normal corporate income tax rate (i.e. maximum effective rate of 34.43%). The favourable regime of participation exemption (i.e. effective tax rate of 4.13%) does not apply to the transfer of shares in real estate companies.

The acquisition of shares in a real estate company is subject to transfer duties at the rate of 5% of the fair market value of the shares.

b. Asset deal

Capital gains on the transfer of assets in real estate company subject to corporate income tax are taxed at the normal corporate income tax rate.

The acquisition of real estate asset is subject to transfer duties at the rate of 5.09% of the fair market value of the estate asset.

Sell-side

15. How are capital gains taxed in your country? Is there any participation exemption regime available?

a. Share deal

For non-French tax resident companies subject to the provisions of relevant tax treaties having a substantial shareholding provision (e.g. those with Spain, Italy, Hungary, etc.), capital gains on shares held in a French company are subject to tax at a rate of 45% provided the foreign selling entity has held, at any time during the five years preceding the sale, directly or indirectly, more than 25% of the French company's share capital of the French company (section 244 bis-B of the French Tax Code).

In the same situation, French companies may be exempted from paying tax on the capital gains realised upon the sale of stake, except on 12% of the gross amount, provided there was a holding of at least 5% for a two-year period.

According to the new French tax guidelines, the foreign seller is allowed to claim, under certain conditions and through formal claim, for a refund of the paid tax exceeding the effective tax burden.

b. Asset deal

If a French company sells assets, the capital gain is taxable at the normal corporate income tax rate (i.e., maximum effective rate of 34.43%).

16. Is there any fiscal advantage if the proceeds from the sale are reinvested?

There is no specific advantage to reinvesting the proceeds of a sale if the transaction price of the sale of shares is reinvested by the seller company. If the seller is a fund, subject to conditions, no taxation arises at the level of the fund's interest holders as long as no cash is distributed.

17. Are there any local substance requirements for holding/finance companies?

The local substance requirements for holding companies are: minimum staff, offices, location of board meetings, decision power, etc.

However, the substance must be in relation to the activity of the company, i.e. the substance-level requirement is different between an operational company, a financial company and a non-operating holding which purpose is only management of its shareholding. Consequently, the substance level requirements for non-operating holdings are necessarily limited.

Your Taxand contact for further queries is:

France

Denis Andres
T. +33 170388804
E. denis.andres@arsene-taxand.com