



FRANCE



FRANCE

INTERNATIONAL DEVELOPMENTS

1. WHAT ARE RECENT TAX DEVELOPMENTS IN YOUR COUNTRY WHICH ARE RELEVANT FOR M&A DEALS AND PRIVATE EQUITY?

❖ Progressive reduction of the Corporate income tax (CIT) rate

The French CIT rate should decrease progressively from 33.33% to 25% by 2022 (Finance Law for 2018, article 84). This measure is laid down as follows:

- In 2018, CIT rate is set at 28% until €500,000 of tax profit and 33.33% beyond
- In 2019, CIT rate would be 28% until €500,000 of tax profit and 31% beyond
- The standard CIT rate would be 28% in 2020, 26.5% in 2021 and 25% in 2022

❖ Removal of the 3% tax on dividends distributions

Under article 235 ter ZCA of the French Tax Code (FTC), distributions made by French companies were subject to a 3% contribution in some circumstances. The 3% distribution tax was found to be contrary to the Parent-Subsidiary Directive (ECJ, 17 May 2017, 635/16) and to the French constitutional principle of equality before the law (CC, 6 October 2017, 660 QPC). As a result, the tax is repealed for dividend distributions paid out from 1 January 2018 (Finance Law for 2018, article 38). Litigation to get a refund of this contribution is still possible for contributions paid in 2016 and 2017.

❖ Creation of 2 exceptional and temporary contributions to assist in financing the removal of the 3% distribution tax

The Parliament has approved an exceptional contribution on profits in order to finance the reimbursement of the 3% distribution tax refund claims filed by taxpayers (First amended Finance Law for 2017, article 1st). The contributions apply only once, for fiscal years ending between 31 December 2017 and 30 December 2018.

- The first contribution of 15% calculated on the CIT applies to companies with an annual turnover of at least €1 billion bringing the effective rate to 39.43% (including the social contribution of 3.3% of article 235 ter ZC of the FTC)
- The second contribution of 15% calculated on the CIT also applies to companies with an annual turnover of at least €3 billion bringing the effective rate to 44.43% (including the social contribution of 3.3% of article 235 ter ZC of the FTC)

❖ Facilitation of the reorganisation regime

The Court of Justice of the European Union and French Supreme administrative court ruled out in 2017 that the pre-approval which was required by the French tax authorities was contrary to the freedom of establishment (ECJ, 8 March 2017, Euro Park, C-14/16). In order to comply with these decisions, the Parliament has abolished the tax ruling procedure for cross-border restructuring operations set out in article 210 C of the FTC as of 1 January 2018 (Second amended Finance Law for 2017, article 23). The neutrality regime for mergers, contributions of businesses, spin-offs may apply when a contribution is made to a company located in a country that has signed a treaty with France including a mutual administrative assistance provision provided the transferred assets are recorded in the balance sheet of a French permanent establishment of the foreign company. A new specific tax return will now have to be completed in the context of the reorganisation.

Furthermore, the scope of restructuring operations eligible for the neutral merger tax regime has also been extended (Second amended Finance Law for 2017, article 23). A contribution of shares reinforcing an existing controlling situation will now be assimilated to a contribution of a complete and autonomous branch of activity eligible to the neutrality regime for mergers. Please note that the commitment to hold shares for a three-year



period provided for the contributing company under the neutrality regime for mergers has also been abolished. Nevertheless, in practice, the shares should have to be held for more than two years to benefit from the participation exemption regime.

2. WHAT IS THE GENERAL APPROACH OF YOUR JURISDICTION REGARDING THE IMPLEMENTATION OF OECD BEPS ACTIONS (ACTION PLANS 6 AND 15 SPECIFICALLY) AND, IF APPLICABLE, THE AMENDMENTS TO THE EU PARENT-SUBSIDIARY DIRECTIVE AND ANTI-TAX AVOIDANCE DIRECTIVES?

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 included in French law by the amended Finance Law for 2015 which provides that 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.

Besides, since French legislation already provides for exit tax, CFC rule, or hybrid mismatches rules in compliance with ATAD, European Commission announced that France met the requirements to postpone the whole harmonisation of French legislation until 1 January 2024 at the latest.

The Second Amended Finance Law for 2017 has already introduced the general anti-abuse provision derived from ATAD with respect to the application of Corporate income tax neutrality to a reorganisation when the main purpose or of the main purposes of the operation is fraud or tax.

On 17 January 2018, the French Council of Ministers approved the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS (MLI).

GENERAL

3. WHAT ARE THE MAIN DIFFERENCES BETWEEN AN ACQUISITION OF SHARES AND 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 Simplifiées (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 question 6 below).

In asset deals, only assets are transferred – any NOLs remain with the target company provided that such sale does not qualify as a change of activity (see question 6). 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 in 2019).



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 AMORTISATION OF GOODWILL AND SIMILAR INTANGIBLE ASSETS 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 n° 2015-06 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 value 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.

6. FROM A TAX PERSPECTIVE, THE DEPRECIATION OF A BUSINESS ASSET IS NOT ALLOWED. THEREFORE, EXTRA-ACCOUNTING ADJUSTMENTS WILL BE NECESSARY. WHAT ARE THE LIMITATIONS ON THE DEDUCTIBILITY OF INTEREST EXPENSE? ARE THERE SPECIAL INTEREST LIMITATIONS IN THE CASES OF ACQUISITION OF SHARES AND ASSETS?

There are several rules that relate to the deductibility of interest on borrowings. Some modifications are contemplated to introduce the ATAD deductibility provisions based on the EBITDA.

❖ 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. 1.67% for the full year closed on 31 December 2017). 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 a 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 European Union or European Economic Area (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 either in France or since 1 January 2018 in European Union or European Economic Area 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

It should be noted that the new safe harbor provision regarding the case of the controlling entity established in the EU or in European Economic Area has been introduced by the Finance Law for 2018.

❖ **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 COMMON STRATEGIES TO PUSH-DOWN DEBT ON ACQUISITIONS?

The most straightforward solutions to push-down debt consist in 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).

Therefore, the strategy in a debt push-down could consist in 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 4.13%).

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 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 THERE ANY TAX INCENTIVES FOR EQUITY FINANCING?

There are no specific tax incentives for equity financing.

9. ARE LOSSES OF A TARGET COMPANY AVAILABLE AFTER AN ACQUISITION IS MADE? ARE THERE ANY RESTRICTIONS ON THE USE OF SUCH LOSSES?

❖ On a stand-alone basis

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, it being specified losses are not available unless the target company changes its activity.

An addition of business activity can characterise a change in activity where, during the fiscal year of the change 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 may also characterise a change in activity if there is a decrease of more than 50% of the previous criteria.

However, if the target company, which owns losses, is merged into another company, the losses can be transferred to the merging company only if a ruling 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).

❖ On a group basis

In principle, all the tax losses born within the tax consolidated group remain at the level of the head of the group when the said tax group vanishes. These tax losses are then only offset-able by the former head of the group against its own profits.

However, the former head of the tax group may elect for the enlarged basis imputation mechanism (i.e., "*imputation des déficits fiscaux sur une base élargie*") which allows the offset of the previous collective tax losses carried-forward and generated by the companies of the former tax group against the taxable profits realised by such companies and members of the new tax group.

It should be underlined that the significant change in the activity of a subsidiary member of a tax consolidated group does not trigger any vanishing of the carried-forward tax losses it transmitted to the tax consolidated group. The only tax losses which would be definitively lost are those eventually generated by this subsidiary before its entry in the tax consolidated group.

10. ARE THERE ANY ITEMS THAT SHOULD BE INCLUDED IN THE SCOPE OF A TAX DUE DILIGENCE THAT ARE VERY SPECIFIC TO YOUR COUNTRY?

Although it may be underlined that each transaction requires the performance of a tax due diligence on a case-by-case basis, i.e. the review of the tax specificities linked to the activity carried out by the target group, the following items should generally be considered every time a due diligence concerns a French company:



❖ **Losses carry-forward rules**

- General rules

As from 1 January 2004, losses may be carried forward indefinitely. However, it shall be specified the offset-able amount of losses carried forward is limited, i.e. losses carried-forward shall only be fully offset-able against the following year's taxable income up to €1m, and for an amount equal to 50% of the portion of income exceeding 1 million (the remaining 50% of income shall be taxed at the general CIT rate). With respect to carry back, it is limited to one year, capped to €1m. Any excess tax loss is still available for carry forward.

- Change of activity

By way of principle, the cessation of a business activity causes notably the vanishing of the carried-forward tax losses of the company. Moreover, a significant change in the activity carried on by the company as well as the loss of its operating resources may trigger the same consequences (we refer to question 9 for a definition of the "change of activity" under the FTC).

❖ **Specific filing requirements**

French companies are required to file several forms as notably Income from securities and interest returns ("IFU"), and Wages, commissions and fees tax returns ("DAS 2").

In case of a tax audit, failure to fill the above-mentioned forms entails the payment of a fine equal to 50% of the amount which should have been reported.

Capital gains whose taxation has been deferred upon a tax neutral operation must be followed-up by the filling of "54 septies" forms, otherwise a 5% penalty applies on the amount of deferred profits which were not included in the statement.

From 2018, the removal of the formal pre-approval from French tax authorities for international reorganisations has been replaced by the filing of a specific post-declaration of the reorganisation to assess the motivations and consequences of this operation. The failure to comply with this requirement shall result in a fixed fine of €10,000.

❖ **Statute of limitations**

As a general rule, the FTA is entitled to audit a FY until the end of the third calendar year following the closing of the said FY. The FTA is in principle not entitled to conduct a new tax audit in the premises of a company which has already been tax audited in relation to the same tax and for the same FY. Other statutes of limitation are provided by French legislation, e.g. in the event of abuse of law.

However, when the company is in a tax loss position, the FTA is entitled to audit the validity of such losses until the end of the third year following the one during which losses have been offset.


❖ **Specific tax credits**

French legislation provides for certain tax credits whose scope and modalities of application should be focused on, e.g. Research tax credit ("CIR").

❖ **French tax Authorities' practice**

The question of the deduction of financial charges paid for intra-group loans is a new frequent reason for adjustment during tax audits. In practice, the tax authorities consider that when intra-group financing is set up, a company must have a loan offer issued by a bank to justify the normality of the interest rate applied, which is not always the case. For this purpose, the tax Authorities refer to Sections 39, 1-3° and 212 of FTC whereby, in the context of intra-group financing transactions, only interests calculated on the basis of a reference rate applied by credit institutions are deductible (i.e. 1.67% for 2017).

Besides, an emerging practice of French tax authorities consists in challenging the benefit of the tax



consolidation regime based on criteria related to option formalities and alignment exercise periods of member companies.

11. 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 16 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.

Note that in cases of mergers and assimilated operations, Article 816 of the FTC provides for a fixed registration fee of €375, increased to €500 for companies with a capital of at least €225,000.

12. ARE THERE ANY RESTRICTIONS ON THE CORPORATE TAX 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.

13. 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.

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

In principle, the reception of dividends by the acquiring company from its subsidiaries should have no impact on its right to recover input VAT on acquisition costs.

The ECJ (in EUCJ, Beteiligungsgesellschaft Larentia + Minerva mbH & Co KG, C-108/14 & C-109/14, 16 July 2015) and the French Supreme Court (in CE 20 Mai 2016 n°371940, 8e et 3e ch réunies., min c/ SA Groupe Ingénierie Europe Ginger) recently restated the principle that to the extent that the acquiring companies provides management services to each of its subsidiaries, input VAT related to acquisition costs should be fully deductible subject to its VAT taxation ratio.

However, it should be noted that in a recent case law, the French Supreme Court (in CE 23 Janvier 215 n°365520, Sté Lagardère SCA) seems to limit the possibility of a holding company to recover the input VAT on recharged costs if no services are provided (pure holding company).

14. ARE THERE ANY PARTICULAR TAX ISSUES TO CONSIDER IN THE ACQUISITION OF A DOMESTIC COMPANY BY A FOREIGN COMPANY?

We refer to question 20 and question 6 as regards the "Acquisition of shares not controlled from France (Carrez amendment)".



15. CAN THE GROUP REORGANISE AFTER THE ACQUISITION IN A TAX NEUTRAL MANNER THROUGH MERGERS OR A TAX GROUPING?

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 and acquiring companies 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 (relocation after an acquisition).

Mergers, spin-offs or split-offs may benefit from tax neutrality and are generally made within a group at book value (we refer to question 21).

16. ARE THERE ANY PARTICULAR ISSUES TO CONSIDER IN THE CASE OF A TARGET COMPANY THAT HAS SIGNIFICANT REAL ESTATE ASSETS?

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 companies are subject to corporate income tax are taxed at the normal corporate income tax rate.

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



17. IS FISCAL UNITY/TAX GROUPING ALLOWED IN YOUR JURISDICTION AND IF SO, WHAT BENEFITS DOES IT GRANT?

French related companies subject to corporate tax may elect to form a tax-consolidated group provided that some conditions are met (e.g. companies held at more than 95% by the head company). It remains an election and companies should not elect before considering the overall advantages and disadvantages regarding this tax regime.

As far as advantages are concerned, the following main benefits may notably be granted by a French tax group regime:

- ❖ The parent company files a consolidated return, thereby allowing the offset of losses of one group entity against the profits of the other consolidated companies. The parent company then pays CIT based on the tax group result, after certain adjustments are made (e.g. adjustments for intra-group provisions, debt waivers, capital gains realised on asset / share transfers).
- ❖ Regarding intra-group dividend distributions within a tax-consolidated group, further to Steria case law (ECJ Steria, 2 September 2015, aff. C-386/14), two different regimes coexist:
 - Where the parent subsidiary regime is not applicable, intra-group dividends are fully neutralised at the level of the group income as from the second FY of the tax consolidated group.
 - Where the parent subsidiary regime is applicable, a 1% lump-sum amount remains taxable. This provision applies as from the first FY of the tax consolidated group. Please note that the taxation of a 1% lump-sum also applies for dividends paid by European subsidiaries which would satisfy conditions to enter in a French tax consolidated group if they were established in France.
- ❖ Regarding the application of thin capitalisation rules to tax consolidated companies (Section 223 B of the FTC), thin capitalisation rules described under Question 6 apply to each company that is a member of the group taken separately.

Nevertheless, any excess interest recaptured in the individual results shall not be deductible at tax consolidated group level.

Subject to limitations, the parent company shall thus be allowed to deduct excess interest incurred at the level of the tax consolidated companies and to carry forward the remaining amount of excess interest to the following tax years after the annual deduction of 5%.

18. DOES YOUR COUNTRY HAVE ANY SPECIAL TAX STATUS SUCH AS A PATENT BOX FOR COMPANIES THAT HOLD INTANGIBLE ASSETS?

Article 39 terdecies of the FTC provides for a reduced 15% rate of CIT on royalties and capital gains from qualifying intellectual property (IP). French and European patents, patentable inventions and some production processes accessory thereto are deemed as such. However, other IP rights such as trademarks, design rights, software and mere know-how are not included. IP rights only qualify under the regime if they are classified as an asset in the company's statutory accounts. As well as full ownership, the reduced rate may apply to rights received under license and sub-license agreements.

19. DOES YOUR COUNTRY IMPOSE ADVERSE TAX CONSEQUENCES IF OWNERSHIP OF INTANGIBLES IS TRANSFERRED OUT OF THE COUNTRY?

There is no specific adverse rule provided for the transfer of assets outside France.



SELL-SIDE

20. HOW ARE CAPITAL GAINS TAXED IN YOUR COUNTRY? WHAT, IF ANY, GAINS ARISING IN AN M&A CONTEXT ARE ELIGIBLE FOR SPECIAL TREATMENT?

a) Share deal

❖ Capital gains derived by French companies

Capital gains derived from the sale of qualifying participations are only subject to CIT on a 12% lump-sum, resulting in a taxation at the effective rate of 4.13%.

Qualifying participations must satisfy both of the following conditions:

- They must be qualified as controlling interest (specific class of shares for accounting purposes that enables the shareholder to have a controlling interest) or, be eligible for the dividend participation exemption regime (provided 5% of the voting rights in the subsidiary's capital are held)
- They must have been held for at least two years before their sale

A reduced 15% tax rate applies to the following:

- Capital gains derived from sales of shares in venture mutual funds and venture capital investment companies if these shares have been held for a period of at least five years
- Capital gains realised on patents or patentable rights held for at least two years, unless the disposal takes place between related companies

Capital gains derived from sales of participating interests in companies that are predominantly real estate companies are subject to tax at the standard rate of 33.33%. For listed real estate companies, the rate is reduced to 19%.

❖ Capital gains derived by non-resident companies

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 the standard CIT rate of 33.33% 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).

According to the new French tax guidelines, the foreign seller is allowed to claim, under certain conditions and through the formal process, 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%).

21. IS THERE ANY FISCAL ADVANTAGE IF THE PROCEEDS FROM THE SALE OF SHARES OR ASSETS ARE REINVESTED?

There is no specific advantage to reinvest the proceeds of a sale. 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.

22. ARE THERE ANY LOCAL SUBSTANCE REQUIREMENTS FOR HOLDING 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 operating company, a financial company and a non-operating holding which only manages its shareholding. Consequently, the substance level requirements for non-operating holdings are necessarily limited.

23. ARE THERE ANY SPECIAL TAX CONSIDERATIONS REGARDING MERGERS/SPIN-OFFS?

❖ Accounting principles

As regards the transcription modalities of the transfer, it shall be noted that contributions have to be translated in the beneficiary company's books under the following accounting rules (French GAAP), i.e. at the net book value (usually where the parties involved are under common control, that is, when the merging company controls the merged company or when both of them are under the control of a third party) or at the fair market value (usually where parties involved are non-related parties and where the main shareholder of the merging company keeps the control of the remaining entity).

❖ Tax principles

❖ CIT

❖ Common regime

Under common regime, mergers/spin-offs imply the consequences of enterprise cessation, i.e.:

- Provisions and latent capital gains taxation at CIT
- Registration duties applicable to contributions made to a company (depending on the nature of the contribution)

❖ Specific neutral regime

Under special regime, mergers/spin-offs benefit from favorable provisions as regards CIT and registration duties, provided certain requirements are met, including accounting requirements.

Upon election, Section 210 A of the FTC contains a special system of CIT applicable to the mergers mainly resulting in the deferral of capital gains and provisions taxation (unless provisions are no longer required) at the level of the contributing company.

In order for the merger/spin-off special regime to apply, in addition to the express election for the application of the special regime, the beneficiary company shall comply with several requirements to allow the future taxation of capital gains and provisions which were exempt from tax at the time of the merger/spin-off, e.g. record all the transferred assets for the value they had in the merged company books.

However, if the merger is concluded with retroactive effect from the beginning of the FY, the normal business result would be included in the taxable profits of the beneficiary company.

At the level of the beneficiary company, the capital gains arising from the cancellation of its interest in the contributing company due on a merger are tax exempt.

❖ VAT

VAT exemption is applicable where the transaction qualifies as a transfer of a going concern within the meaning of French and European Union law, such as a transfer of a business. On the transfer of a business, the exemption applies to the disposal, subject to payment, of all the assets constituting the business (i.e. intangible and tangible assets excluding real estate).



❖ Registration duties

Pursuant to Section 816 of the FTC, mergers and assimilated operations benefiting from the merger tax regime of Section 210 A, trigger fixed registration duties amounting to €500 (€375 for companies whose share capital is less than €225k).

Real estate properties transferred in the frame of a merger benefiting from the merger tax regime of Section 210 A are however subject to a real estate publicity fees (contribution de sécurité immobilière) amounting to 0.10% of the value of the properties received (Section 879 of the FTC).

If the real estate property transfer is realised in the frame of winding up, an additional real estate publicity fees of 0.715% (taxe de publicité foncière) will be due on the value of the property received.

❖ Other considerations

❖ Tax losses

The transfer of carried-forward tax losses in case of merger or similar restructuring operation is notably subject to the condition that the activity that originated the tax losses did not suffer any significant change in terms of customers, staff, operating resources, nature and volume of activity, otherwise the transfer would be subject to a ruling granted by the FTA.

❖ Quick merger

French tax authorities try to deny the deduction of interest 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.

❖ Acquisition costs

Where participation shares are transferred to the merging company due to the merger, and provided the merger benefits from the special regime above-mentioned, the absorbing company is allowed to continue to proceed to the amortisation or deduction of the acquisition costs included in the participation securities' cost price (on the time left to amortise).

Where participation shares are cancelled in the merging company's accounts following the merger, the gain or loss realised must be determined on the basis of the tax value of the cancelled shares, i.e., the cost value majored by the acquisition cost related to these shares, and minored by the amortisation or deduction amount already performed.

MANAGEMENT INCENTIVES

24. WHAT ARE THE TAX CONSIDERATIONS IN YOUR JURISDICTION FOR MANAGEMENT INCENTIVES IN CONNECTION WITH SELLING OR BUYING A COMPANY?

❖ New taxation rules for individuals

The gain realised by managers benefiting from management incentives may be taxed differently depending on whether it is qualified by the FTA as a capital gain or as a salary.

Until 1 January 2018, financial income such as dividends, interest, and capital gains on the sale of shares earned by individuals was subject to French annual income tax at progressive rates (up to 45%), exceptional contributions on high income (up to 4%), and to social contributions (15.5% in 2017).



The Finance Law for 2018 introduced a 30% flat tax on financial income (interest, capital gains, carried interest, distributions and similar income), composed of a 12.8% income tax, and 17.2% social contributions (Finance Law for 2018, article 28). The contribution on high income (up to 4%) however remains in place in addition to the 30% (leading to a global rate of 34%).

❖ **Free shares plan**

For free shares issued in relation with free shares plan voted as of 1 January 2018, the following regime applies:

- As regards acquisition gains (the share value is fixed at the vesting date), the portion that does not exceed €300,000 benefits from a global deduction of 50% for the calculation of individual income tax at the progressive rate and remains subject to social contribution of 17.2% whereas the portion exceeding is still treated as salary at the progressive income tax rate.

An employer contribution of 30% also applies at the date of the granting.

- As regards capital gains (difference between the selling price and the acquisition gain), the taxable basis is subject to the 30% flat tax (including 17.2% of social contributions). The tax is due at the time of the sale of the shares.

❖ **Risk in relation with management packages**

The FTA reserves the right to deny the qualification of “capital gain” and requalify in “salary” the gain realised by managers where the latter have not borne a real investor’s risk, i.e. where managers have benefited from a more favorable treatment due to their salaried activity.

- From a tax standpoint, the qualification as employment income will be borne by the manager benefitting from the management plan (individual tax at 45% vs 12.8% for capital gains on top of the 17.8% of social contributions and the potential 4% tax on high level income)
- From a social contribution standpoint, the qualification as employment income can trigger a social contribution burden for the company employing the manager (depending upon the remuneration of each manager but amounting to circa 50% of the income earned by the manager). Indeed, this principle has been provided by a recent case law (Court of Appeal of Paris, 6 July 2017, SAS Groupe Lucien Barriere vs URSSAF – Ile de France 14/02741). Please note that an appeal has been lodged against this decision and we are waiting for the decision of the Supreme Court.

To date, based on case law, the FTA notably pays particular attention to the following key elements:

- the link between the investment realised and the function performed, i.e. whether the management package replaces an element of remuneration of the manager (link with the manager’s salaried activity)
- advantages eventually granted at the entry and at the exit to the managers, i.e. whether the management package constitutes a risky capital investment or not.

For that purpose, it is important to limit the corroborating evidences notably if it is not possible to avoid the good/bad leaver provision in the agreement with the managers. After a review of the contemplated term sheet

of management package plan, we would recommend the following

- An accurate market value of the shares is key
- The management package requires the existence of a capital risk

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