tax notes international
Volume 63, Number 13 ■ September 26, 2011

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Supplementary Budget Bill Focuses On Deficit Reduction

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Reprinted from *Tax Notes Int'l*, September 26, 2011, p. 933

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COUNTRY DIGEST

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Supplementary Budget Bill Focuses on Deficit Reduction

The French Parliament on September 8 passed the Second Supplementary Budget Bill for 2011, which focuses on new tax measures to reduce deficits. Additional tax measures have been proposed in the draft budget law for 2012, which will be presented to the Cabinet on September 28.

New Measures

For Businesses

Tax Losses

Previously, corporate taxpayers could carry forward their tax losses to subsequent financial years without any limitations. There is still no time limit on the carryforward of tax losses, but the deductible amount is now limited to €1 million, plus 60 percent of any taxable profit exceeding €1 million. This limit also applies to the subsidiaries of consolidated tax groups for tax losses accumulated by the subsidiaries before their entry into the group. The fraction of tax losses that cannot be deducted can still be carried forward to subsequent years without any time limit.

Corporate taxpayers also previously could carry back their tax losses for three financial years with no limit on the amount. Now, tax losses can only be carried back to the previous financial year and only up to €1 million.

Both of these new rules apply for years ending as of the date of entry into force of the bill (the day after its publication in the official gazette).

Abolition of Worldwide Consolidated Income Basis System

This system currently allows French companies (subject to the approval of the finance minister) to retain, for a five-year period, all of the profits of their French and foreign subsidiaries and branches (held directly and indirectly) for determining their tax base. The abolition of the system applies for years that ended as of September 6, 2011.

Capital Gains on Securities

The taxation of capital gains on securities is equal to the French corporate income tax on a limited amount corresponding to 10 percent of the capital gain. The 10 percent rate (previously 5 percent) applies for fiscal years beginning on or after January 1, 2011.

Tax on Insurance Contracts

The new supplementary budget bill also increased the tax rate for some health insurance contracts (those known as ''supportive and responsible'' contracts) from 3.5 percent to 7 percent.

In addition the 7 percent rate previously applicable to standard or regular health insurance contracts has been replaced with a standard rate of 9 percent.

These new measures apply to premiums or contributions due as of October 1, 2011.

Tax on Hotels

Hotel operators now are subject to a new 2 percent tax on accommodations priced at €200 or more per night. The tax applies to accommodations that are eligible for the reduced VAT rate of 5.5 percent and for which the VAT is due on or after November 1, 2011.

For Individuals

Social Security Contributions

The rate of social security contributions has been increased by 1.2 percentage points, from 2.2 percent to 3.4 percent. This brings the overall rate of social security contributions to 13.5 percent.

The rate increase applies to indirect income derived on or after January 1, 2011, and to investment products acquired or recorded on or after October 1, 2011.

Real Estate Capital Gains

Until now, the tax on gross capital gains from real estate sales was reduced by 10 percent per year of retention of the real estate beyond the fifth year (with a full exemption after 15 years). Also, a fixed allowance of €1,000 was provided for the gross capital gain, less the 10 percent reduction for the holding period (when applicable).

The capital gain now can be exempted only after 30 years of holding (as opposed to 15) and the tax allowance based on the holding period has been modified as follows:

- no reduction during the first five years of retention;
- a reduction of 2 percent between the sixth and 17th years of retention;
- a reduction of 4 percent between the 18th and 24th years of retention; and
- a reduction of 8 percent beyond the 24th year of retention.

Moreover, the fixed allowance of €1,000 has been abolished. Consequently, the overall tax rate (income tax and social contributions) for real estate capital gains will be 32.5 percent for disposals made on or after October 1, 2011. Notably, capital gains from the sale of a primary home remain exempt.

Provisions of the new bill relating to the computation of the purchase price of the property and the tax allowance apply to capital gains on disposals made on or after February 1, 2012. However, those measures apply from August 25, 2011, for contributions of properties or shares to family real estate investment companies. The provisions concerning the abolition of the fixed allowance of €1,000 will apply the day after the publication of this bill in the official gazette.

Transfer of Shares of Real Estate Investment Companies

Transfers of shares of real estate investment companies that are made abroad will have to be finalized in France with a notarized deed within one month of the transfer. This measure applies from November 1.

The purpose of this provision is to prevent the avoidance of the 5 percent registration fee and the capital gains tax[1] (if any) on sales abroad of shares of real estate investment companies whose assets consist primarily of property located in France.

Tax Proposals

Scellier and Girardin Real Estate Regimes

The draft proposes a limit of 15 percent on the tax reduction, with a new ceiling of €300,000 and a spending cap per square meter in order to avoid a concentration on small units.

Real Estate Capital Gains

Social security contributions would apply to real estate capital gains regardless of the duration of the holding of the property (excluding the primary home).

Taxation of High Incomes

An extraordinary contribution would be assessed at the rate of 3 percent on taxpayers declaring income in excess of an established amount (currently under debate but likely between €250,000 and €500,000 per person, including dividends and capital gains).

Reduced VAT Rate

An intermediate VAT rate between 5.5 percent and 19.6 percent would replace the current reduced rate of 5.5 percent for restaurants and for renovation work on residential dwellings (secondary or primary) that were built more than two years previously.

Tax Loopholes (Niches Fiscales)

Also proposed is a 10 percent reduction of the various tax allowances granted to individuals. The global tax ceiling applicable to tax loopholes would also be reduced. ◆

♦ *Sophie Borenstein, partner, Reed Smith, Paris*

[1]The rate is either 19 percent or 33.33 percent, depending on the tax residence of the seller.

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