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Finance Act Amends Taxation of Stock Options

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COUNTRY DIGEST

Finance Act Amends Taxation of Stock Options

France's new 2013 Finance Act (Law 2012-1509) has completely amended the tax and social contribution regimes for stock options and restricted stock units (RSUs). (Prior coverage of the Finance Act: *Tax Notes Int'l*, Feb. 4, 2013, p. 438.)

For shares granted after September 28, 2012, the acquisition gains realized on the exercise of stock options/RSUs are taxed as compensation at progressive individual income tax rates of up to 45 percent (this new 45 percent tax rate applies to net taxable income exceeding €150,000 earned in 2012). Taxation is still deferred until the sale of the shares, however.

For employees, the new regime means that acquisition gains could be subject to the maximum progressive tax and social contributions amounting, in aggregate, to approximately 61 percent, not including the existing surtax (of 3 percent or 4 percent) that may be applicable to high earners.

The French Constitutional Court struck down a provision that would have increased the employee contribution to 17.5 percent, or to 22.5 percent if the required holding period from the grant date (four years for stock options and two years for RSUs after the two-year vesting period) was not met.

New Regime for Stock Options

The four-year minimum holding period between the grant date and the sale date, as established by the tax rules, no longer applies.

The acquisition gains realized by employees at the vesting of RSUs are taxed as salary at the progressive individual income tax rates. Taxation occurs at the time the shares are sold.

Acquisition gains are also subject to the 8.2 percent supplementary social security contribution (CSG) and the 0.5 percent social contribution (CRDS) applicable to compensation income. (Acquisition gains previously were subject to the combined 15.5 percent social contributions on investment income.) The CSG becomes partially deductible (5.1 percent) from the taxable income in the year after payment of the tax.

Thus, such gains remain exempt from the other ordinary social contributions, but remain subject to specific employer and employee contributions (30 percent and 10 percent, respectively).

The French employer must report to URSSAF (Unions de Recouvrement des Cotisations de Sécurité Sociale et d'Allocations Familiales, meaning organizations for the payment of social security and family benefit contributions) the identity of the employees to which shares have been granted during the previous calendar year and the number and value of shares granted to each employee (even for shares granted by foreign companies to French employees). If the employer fails to do so, it will be liable for both employee and employer social insurance contributions at rates of up to 23 percent and 46 percent, respectively, in addition to the employer-paid social tax due on the grant date.

Capital gains derived from the sale of the shares, which were taxable at a flat rate of 24 percent in 2012, now are taxable under the progressive income tax rates. They may benefit, however, from a specific allowance, based on the amount of time the shares were held, of up to 40 percent (20 percent for shares held between two and four years, 30 percent for shares held between four and six years, and 40 percent after six years). Capital losses can be set off against acquisition gains.

Like acquisition gains, capital gains are also subject to the CSG and CRDS applicable to compensation income. (Such gains previously were subject to the combined 15.5 percent social contributions on investment income.) The CSG becomes partially deductible (5.1 percent) from the taxable income in the year after payment of the tax.

Although for acquisition gains, the new tax and social contribution regime applies only to shares granted after September 28, 2012, the new rules will also apply to stock award plans existing before September 28, 2012, if the shares related to those plans are granted after September 28, 2012. Therefore, the previous regime and the new regime could be in force contiguously, with their application depending on the grant date of the shares.

New Regime for RSUs

The acquisition gains realized by employees at the vesting of RSUs are taxed as salary at the progressive individual income tax rates. Taxation occurs at the time the shares are sold.

The two-year minimum holding period under the tax rules no longer applies. However, the separate four-year holding period established under commercial law still applies (corresponding to a two-year vesting period followed by a two-year holding period).

As with the new regime for stock options, acquisition gains are also subject to the CSG and CRDS applicable to compensation income and the CSG becomes partially deductible (5.1 percent) from the taxable income in the year after payment of the tax.

The gains are exempt from the other ordinary social contributions but remain subject to the specific employer and employee contributions (30 percent and 10 percent, respectively).

As with the stock option regime, the French employer must report to URSSAF the identity of the employees to which shares have been granted during the previous calendar year and the number and value of shares granted to each employee (even for shares granted by foreign companies to French employees). If the employer fails to do so, it will be liable for both employee and employer social insurance contributions at rates of up to 23 percent and 46 percent, respectively, in addition to the employer-paid social tax due on the grant date.

Again, capital gains on the sale of shares are subject to the progressive individual income tax rates. However, they can benefit from a specific allowance, based on the amount of time the shares have been held, of up to 40 percent.

The capital gains are also subject to the CSG and CRDS applicable to compensation income but the CSG becomes partially deductible (5.1 percent) from the taxable income in the year after payment of the tax.

Capital losses can be offset against the acquisition gains.

The tax and social contribution regimes for stock options and RSUs granted before September 28, 2012, are outlined below.

Stock Options Granted Before 9/28/12

The acquisition gains realized on the exercise of stock option benefit from a flat tax of 30 percent (of 41 percent above €152,500) when a four-year minimum holding period between the grant date and the sale date is met. The rate drops to 18 percent (or 30 percent above €152,500) when an additional two-year holding period is followed. Taxpayers can choose to have the gain taxed as salary at the progressive individual income tax rates.

Taxation occurs at the time of the sale of the shares. When the four-year minimum holding period is not fulfilled, the gains are taxed under the compensation regime at progressive individual income tax rates.

Acquisition gains are also subject to the 15.5 percent combined social contributions applicable to investment income and to the employer contribution of 30 percent (for shares granted after July 11, 2012) and 14 percent (for shares granted before), and also to the employee contribution of 10 percent.

Social contributions applicable to compensation income do not apply if the four-year minimum holding period between the grant date and the sale date is met.

Capital gains are subject to the progressive individual income tax rates but can benefit from a specific allowance, based on the amount of time the shares have been held, of up to 40 percent.

Capital gains are also subject to the CSG and the CRDS applicable to compensation income. The CSG becomes partially deductible (5.1 percent) from the taxable income in the year after payment of the tax.

Capital losses can be set off against acquisition gains.

RSUs Granted Before 9/28/12

The acquisition gains realized by employees at the vesting of RSUs are subject to a flat tax of 30 percent if the employees meet a four-year minimum holding period (a two-year holding period established under commercial law and an additional two-year holding period in the tax rules). Taxpayers can choose to have the gain taxed as salary at the progressive individual income tax rates.

Taxation occurs at the time of the sale of the shares. When the tax rules' two-year minimum holding period is not fulfilled, the gain must be taxed under the compensation regime at the progressive individual income tax rates.

Social contributions applicable to compensation income do not apply to acquisition gains if the minimum holding period is fulfilled.

The French employer must report to URSSAF the identity of the employees to which RSUs have been granted irrevocably during the previous calendar year and the number and value of shares granted to each employee.

If these two conditions (holding period and notification to URSSAF) are not met, the employer is liable for both employee and employer social insurance contributions at rates of up to 23 percent and 46 percent, respectively, in addition to the employer-paid social tax.

Such gain is subject to the combined 15.5 percent social contributions applicable to investment income, and to the employer contribution of 30 percent (for shares granted after July 11, 2012) or 14 percent (for shares granted before that date), and also the employee contribution of 10 percent.

Capital gains on the sale of the shares are subject to the progressive individual income tax rates. They can, however, benefit from a specific allowance, based on the amount of time the shares have been held, of up to 40 percent.

Capital gains are also subject to the CSG and the CRDS applicable to compensation income. The CSG becomes partially deductible (5.1 percent) from the taxable income in the year after payment of the tax.

Capital loss can be offset against the acquisition gains. ◆

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