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COUNTRY DIGEST

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Finance Act Contains Several Notable Corporate Tax Measures

French Finance Minister Pierre Moscovici and Budget Minister Bernard Cazeneuve on September 25 presented to the Council of Ministers the draft budget law for 2014, which will be discussed by the French Parliament over the following weeks. The most notable tax aspects of the draft budget are set out below.

Businesses

Corporation Tax

New Contribution on Gross Operating Profit

This new 1 percent tax on earnings before interest, taxes, depreciation, and amortization (EBITDA) would apply to companies with annual turnover in excess of €50 million.

Deduction of Interest Between Related Companies

The current tax treatment of interest on loans between related companies may allow for the establishment of a tax optimization scheme that in effect creates artificial debt in one of the group companies. The artificial debt can be used to reduce the taxable income of a French subsidiary and to move the profit to a lending entity located in a country where taxes are very low.

To combat those schemes, the government has proposed prohibiting the deduction of loan interest between related companies if the interest received by the lending company (whether a French tax resident or not) is not subject to corporation income tax in an amount that is at least 25 percent of the tax that would be charged under French common law.

Transfer Pricing

A new rule would require French corporate taxpayers to demonstrate that the transfer price set for a restructuring transaction that benefits a related company constitutes normal financial compensation if the transfer reduces the taxpayer's EBITDA by 20 percent or more compared to the average of the past three financial years. Under the proposed regime, the taxpayer would be required to provide evidence of the fair value of the transfer price in a transfer to a related company of functions or risk that the transferring company would no longer carry out itself. The company would have to provide information about the entities involved in those transactions and justify the level of compensation allocated to each of them before and after the transfer of functions or risks. However, this requirement would not apply to the transfer of a sole asset or to the license to use that asset if the assignment or grant is independent of all other transfers of function or risk.

Special Tax on High Compensation Paid by Companies

The taxable basis of this exceptional tax would apply to that part of gross remuneration received by employees and officers (for example, wages, salaries, grants to purchase shares or securities, profit-sharing and incentive bonus schemes, employee saving plans, and so on) in excess of €1 million per year. The rate would be 50 percent and the amount would be capped at 5 percent of the company's turnover.

The new tax would cover salaries earned, awarded, or recognized as expenses of the company in 2013 and 2014.

Other Measures

Several tax measures applying to companies, including the ability to offset tax losses made by a foreign branch or subsidiary of a French small or medium-size enterprise, would be revoked with effect from January 1, 2014.

Individuals

Capital Gains

Capital Gains on Sales of Securities

Currently, income tax on gains from sales of securities and corporate rights by individuals is systematically imposed at progressive rates after applying a discount based on the holding period of the shares sold.

The draft budget law provides for a 50 percent tax allowance for a holding period ranging from two to less than eight years and a 65 percent tax allowance for a holding period of eight years or more.

An even more favorable regime would apply to gains on sales of:

- securities of SMEs created less than 10 years before the acquisition of the securities sold;
- shares of SME owners who are retiring;
- shares of ''innovative companies''; and
- shares transferred to family members.

This specific incentive regime would grant a 50 percent tax allowance for holding periods between one and less than four years; a 65 percent tax allowance for periods between four and eight years; and an 85 percent allowance for holding periods of eight years or more. SME owners who are retiring would also receive an additional fixed allowance of €500,000, which would replace the current exemption.

Real Estate Capital Gains

For building lot sales, the tax allowance for holding periods would end January 1, 2014. For sales of property other than building lots, a full tax exemption of the real estate gain would apply after a holding period of 22 years, and an exemption from social security contributions would apply after a 30-year holding period.

Before the 22-year holding period, there would be a tax reduction of 6 percent for each year of ownership beyond the sixth year and the 21st year and a reduction of 4 percent for the 22nd year of ownership. An exceptional reduction of 25 percent would apply for a period of one year to sales of real estate properties (except building lots) made after September 1, 2013. This reduction would affect the determination of the real estate gain subject to income tax and social security contributions.

Individuals' Savings

A new share savings plan (PEA-PME) would be created to finance SMEs and to benefit households with long-term savings. The new PEA-PME plan would benefit from the same treatment and the same tax benefits as the existing PEA. The ceiling would be set at €75,000.

The ceiling of the PEA would be raised to €150,000 (from €132,000).

Income Tax

A 0.8 percent revaluation of the income bracket limits would apply and the overall ceiling of the dependents' allowance (*quotient familial*) would be lowered from the current €2,000 to €1,500 for each half-share granted for families with children. ◆

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