International Tax

France Tax Alert

19 November 2015

Amended finance bill for 2015 addresses EU issues

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The amended finance bill for 2015, released by the French government on 13 November 2015, includes several measures to bring France's participation exemption for inbound dividends and its withholding tax exemption for outbound dividends distributed to EU companies in line with EU rules (i.e. recent decisions of the Court of Justice of the European Union (CJEU), decisions of the European Commission and the amendments to the EU parent-subsidiary directive (PSD)).

The bill now must be discussed by the French Parliament (both the national assembly and the senate), with a final vote expected by the end of December.

Current rules

Dividends received by a French parent company currently are 95% exempt from corporate tax, provided the French parent holds at least 5% of the share capital of the French or foreign distributing entity for more than two years. The remaining 5% of the dividends, which is deemed to represent costs and expenses associated with the distribution, is taxed at the standard 33.33% corporate tax rate (a 3.3% social surcharge applies to large companies, as well as a 10.7% temporary surtax for financial years ending on or before 30 December 2016, resulting in an effective corporate tax rate ranging from 34.43% to 38%). The 95% exemption does not apply to dividends received from companies located in a country on the list of noncooperative states and territories (NCST), i.e. France's "black list."

As provided under the PSD, dividends distributed by a French company to an EU company that is subject to corporate income tax in its state of residence and that holds at least 10% of the French distributing entity for more than two years are exempt from French withholding tax. (It should be noted that, pursuant to the CJEU's 2006 decision in the *Denkavit* case, the exemption is applied more broadly to dividends paid to an EU parent company that holds only 5% of the capital of the French distributing entity for more than two years if the recipient is unable to offset the corresponding tax credit in its state of residence against the local tax due on the dividends. Although the French tax authorities have implemented the *Denkavit* decision, they have done so only under an administrative statement of practice; it has not yet been incorporated into French domestic tax law.)

If an exemption does not apply, dividends paid to nonresident companies are subject to a 30% French withholding tax, subject to the provisions of an applicable tax treaty. In most cases, this withholding tax complies with EU law, since, if the recipient were a French company, it would be subject to corporate tax at the standard rate (i.e. French companies are not treated more favorably than other EU companies). However, on 28 March 2014, the European Commission formally notified the French tax authorities that it considers the withholding tax to be a restriction on the free movement of capital in cases where the recipient is in a tax loss position and undergoing a liquidation procedure. Under those circumstances, if the recipient were a French company, the distribution received would not be subject to corporate tax; the amount received would reduce the amount of tax losses in the current year (the losses could not be carried forward due to the liquidation process).

Changes proposed under amended finance bill

The amended finance bill for 2015 would make changes to all of the above rules.

Domestic participation exemption for dividends received by a French parent company

- The domestic participation exemption would be extended to apply to the bare ownership of shares (i.e. ownership without usufruct).
- Provisions regarding certain distributions that do not qualify for the domestic participation exemption, which were eliminated in 2014 following a decision of the French constitutional court, would be reinstated (for prior coverage, see the *World Tax Advisor* article dated 23 January 2015). The French tax code previously included provisions that excluded from the participation exemption dividends derived from profits of a subsidiary that related to certain activities that were not subject to the French corporate tax or an equivalent foreign tax (which meant that dividends paid by a real estate investment company (SIIC) were excluded from the participation exemption regime). The constitutional court struck this exclusion down. The reinstatement of these provisions under the amended finance law would apply to fiscal years ending as from 31 December 2015, so there would be no time period during which the exclusions would not apply.
- A provision would be introduced to allow the participation exemption to apply to dividends received from companies located in a NCST, provided the French company could demonstrate that the distributing entity carries on real activities and that the location of the entity does not aim at, or result in, the entity benefiting from a favorable tax regime in the NCST.
- A general anti-avoidance rule (GAAR) would be introduced to transpose the amended PSD into French law. The GAAR requires EU member states to refrain from granting the benefits of the PSD if one of the main purposes of an arrangement is to obtain a tax advantage that would defeat the object or purpose of the PSD, and the arrangement is not genuine. As a result of the GAAR, the 95% exemption on dividends received by French companies would be denied in such cases. This rule would apply to fiscal years ending on or after 1 January 2016.

Withholding tax exemption for dividends paid to EU companies

- The domestic withholding tax exemption would be extended to companies located in the European Economic Area and to bare owners of shares.

- The extension of the withholding tax exemption outlined in the *Denkavit* decision would be codified in the French tax code.
- The existing anti-abuse provision would be revised to transpose the amended PSD into French domestic law. Thus, the exemption from withholding tax would not apply to dividends distributed under an arrangement that has a main purpose of benefiting from the withholding tax exemption and that defeats the object or the purpose of the exemption regime, if the arrangement is not genuine based on all relevant facts and circumstances. This rule would apply to fiscal years ending on or after 1 January 2016.

New withholding tax exemption for dividends paid to certain EU/non-EU companies

A new domestic withholding tax exemption would be added to the tax code for dividends paid to certain nonresident EU or non-EU companies (other than collective investment funds).

To bring French law in line with EU rules, a new exemption from the 30% withholding tax would apply where the recipient of the dividends meets the following requirements:

- It is located in the EU or in a non-EU country that has signed an administrative assistance agreement with France;
- It is in a tax loss position; and
- It is under a liquidation procedure on the date of the distribution.

If enacted, this exemption would apply to distributions made as from 1 January 2016. It should be noted that this new exemption would be useful only in cases where the participation exemption for outbound dividends to EU companies (described above) does not apply. Thus, it mainly would be relevant for distributions to EU companies holding less than 5% of the distributing entity, or distributions to non-EU companies located in a country that has signed an administrative assistance agreement with France.
