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French Finance Act For 2018 and Amending Finance Acts For 2017: Key tax measures for businesses and individuals

Article By:

Litigation at KL Gates

The first and second French Amending Finance Acts for 2017 and Finance Act for 2018 were enacted on December 2, December 29 and December 31, 2017, respectively (the "**Acts**"). The Acts introduce a progressive reduction of the corporate income tax rate to 25% in 2022. In response to a decision of the French Constitutional Court, the specific 3% contribution on distributed income has been abolished. The Acts also make important changes to the favorable tax regime applicable to restructuring operations.

The key tax measures of the Acts affecting businesses are as follows:

- The corporate income tax rate is progressively reduced to 25% as follows:
    - for financial years commencing on or after January 1, 2019, 28% for profits up to €500,000 and 31% for profits above €500,000 ;
    - 28% for financial years commencing on or after January 1, 2020 ;
    - 26.5% for financial years commencing on or after January 1, 2021 ; and
    - 25% for financial years commencing on or after January 1, 2022.

For financial years commencing on or after January 1, 2018, the corporate income tax rate remains at 28% for profits up to €500,000 and 33.1/3% beyond this limit.

- The specific 3% contribution on distributed income is abolished for distributions made on or after January 1, 2018. On October 6, 2017, the French Constitutional Court ruled that the 3% contribution on distributed income was unconstitutional.
- Following the decision of unconstitutionality regarding the 3% contribution on distributed income (see above), the French government will have to reimburse companies that have borne the 3% contribution. In order to finance such refunds, two exceptional contributions will temporarily apply to large companies with financial years ending between December 31, 2017

and December 30, 2018 as follows:

    - Companies with a turnover exceeding € 1 billion will be subject to an exceptional contribution of 15% of their corporate income tax.
    - Companies with a turnover exceeding € 3 billion will be subject, in addition to the aforementioned contribution, to a second exceptional contribution of 15% of their corporate income tax.

- The rate of the competitiveness and employment tax credit (*crédit d'impôt pour la compétitivité et l'emploi*) is reduced from 7 to 6% for remuneration paid on or after January 1, 2018. This tax credit was created in 2013 and now amounts to 6% of the payroll, excluding salaries above 2.5 times the minimum wage of €1,498 (gross) per month. This tax credit will be abolished from January 1, 2019 and compensated for by a reduction of the rate of the employer's social security contributions.

- Companies whose turnover is not subject to VAT up to at least 90% are subject to the payment of a wage tax (*taxe sur les salaires*). The marginal rate of the wage tax (i.e. 20% on gross salaries exceeding €152,276) is abolished for salaries paid from January 1, 2018, in a move that is aimed at improving the attractiveness of Paris as a major financial centre.

- In accordance with the so-called "*amendement Carrez*" provision, the deduction of interest expenses incurred in France by a company for the purposes of the acquisition of shares is subject to certain restrictions, unless it can be demonstrated that (i) the decisions relating to such shares are actually taken by the French acquiring company or by one of its French affiliates, and (ii) where the group exercises control or influence over the acquired company, such control or influence is actually exercised from France. From now on (i.e. for financial years ending on or after December 31, 2017), companies located in an EU state (or in Iceland, Lichtenstein or Norway) are treated the same as companies established in France for the application of the "*amendement Carrez*" provision. In other words, the "*amendement Carrez*" now only applies when the decisions (or the exercise of the control) are taken from a state that is not a member of the EU or EEA.

Several changes have been made to the favorable tax regime for restructuring operations occurring on or after January 1, 2018

- A general anti-abuse clause applicable to mergers or transactions treated as such has been introduced. Under this clause, the favorable tax regime does not apply to mergers, spin-offs or partial contributions of assets the or a main purpose of which is tax fraud or tax avoidance. However, in order to secure the application of the favorable tax regime to mergers or transactions treated as such, a new tax ruling procedure has been introduced.

- French companies undertaking contributions to foreign entities via a merger, a spin-off or a partial asset contribution no longer have to obtain prior approval from the French tax authorities to benefit from the favorable tax regime. It is nevertheless necessary (i) to file a special post-transaction tax declaration describing the transaction and (ii) to book the contributed assets in a French permanent establishment of the foreign beneficiary entity.

- There is no longer an obligation to hold for at least 3 years the shares received in exchange for the contribution of a complete and autonomous branch of activity under the favorable tax regime.

Changes affecting individuals which may be of interest to businesses:

- The rate of the employer social security contribution owed on the value of free shares at the time of vesting (the “Vesting Gain”) is reduced from 30% to 20%. In addition, the portion of the Vesting Gain not exceeding €300,000 is now taxed at the marginal income tax rate after application of a 50% allowance. The portion of the acquisition gain exceeding this threshold is still treated as a salary. This applies to free shares granted under a shareholder’s decision from January 1, 2018.
  Other changes affecting individuals.

- From January 1, 2018, the French wealth tax (*impôt sur la fortune*) has been abolished and replaced by a real estate wealth tax (*impôt sur la fortune immobilière*). The latter is assessed only on the real estate owned by taxpayers to the extent that the value of the taxpayer’s real estate net assets exceeds € 1.3 million. All other assets are therefore no longer subject to any taxation.

- Also from January 1, 2018, a 30% flat tax (consisting of income tax at a rate of 12.8% and social security contributions at a rate of 17.2%) has been created. The latter element is applicable to income from capital (mainly interest, dividends and capital gains). Foreign individuals also benefit from this reform insofar as the withholding tax on capital gains arising from the sale of (non real estate) shares and dividends is reduced to 12.8% , subject to relief under tax treaties. The tax regime applicable to warrants for shares (*bons de souscription de parts de créateur d’entreprise, or BSPCE*) has been adapted accordingly

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[1]*In practice, following the decision of French Constitutional Court, the 3% contribution on distributed income has not been owed since October 8, 2017.*

[2]*The favorable tax regime was previously subject to a tax ruling procedure before the French Tax Authorities when - inter alia - the restructuring operations involved a foreign company. This ruling procedure was ruled by the CJEU as contrary to the right of freedom of establishment (CJEU, No. C-14/16 Euro Park Services).*

[3]*In principle, no withholding tax applies on interest payments.*

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