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Global Tax Alert

French Government releases draft Finance Bill for 2020

Executive summary

On 27 September 2019, the French Government presented the draft Finance Bill for 2020 (the draft Bill). This draft will be discussed by the French Parliament over the following weeks and may be subject to amendments; the final version will be enacted by the end of December 2019.

This Alert summarizes the main direct tax reforms included in this draft that may affect corporations.

Detailed discussion

Modification of the initially proposed French corporate income tax rate decrease for large companies

Following the partial freeze of the French corporate income tax (CIT) rate decrease for companies with revenue equal to, or higher than €250 million, for fiscal years (FYs) opened during calendar year 2019,[1] the draft Bill modifies the initially proposed French CIT rate decrease for these large companies, as follows:

- For FYs starting on or after 1 January 2020, a 28% CIT rate would apply on the first €500,000 of taxable income. Taxable income in excess of €500,000 would be subject to a 31% CIT rate (instead of a 28% CIT rate).

- For FYs starting on or after 1 January 2021, a 27.5% CIT rate would apply (instead of a 26.5% CIT rate).

The initially proposed French CIT rate decrease for companies with revenue lower than €250 million would remain the same as the rates stated by the Finance Bill for 2018,[2] with a 28% CIT rate for FYs starting on or after 1 January 2020 and a 26.5% CIT rate for FYs starting on or after 1 January 2021. For FYs starting on or after 1 January 2022, a 25% CIT rate would apply for all entities.

Finally, the draft Bill specifies that only the rate applicable to companies with revenue lower than €250 million would be taken into account for the payment of withholding taxes or levies for which the rate is determined by reference to the CIT rate. This rule applies to withholding taxes or levies with a triggering event occurring on or after 6 March 2019, or on or after 1 January 2020 for withholding taxes on dividends.

Repeal of the subject-to-tax test applicable to interest expenses

Due to the implementation of the anti-hybrid rules of the European Union (EU) Anti-Tax Avoidance Directives (ATAD 1[3] and ATAD 2[4]) as described in the paragraph below, the draft Bill repeals the existing anti-hybrid rules applicable to interest expenses only. Currently, as per Article 212. I, b of the French Tax Code (FTC), interest accrued by the French borrower must be subject, at the level of the lender, to a minimum taxation of 25% of the French CIT which would have been due, had the lender been established in France.

Such a repeal would apply to FYs starting on or after 1 January 2020.

Implementation of the anti-hybrid rules under the EU ATAD

The draft Bill proposes to literally transpose into French domestic law, the anti-hybrid provisions provided by ATAD 1 and ATAD 2 designed to tackle hybrid instruments as well as hybrid entities.

These directives provide for the transposition into the domestic law of each Member State of the EU, rules to eliminate mismatches in relation to payments as a result of different legal characterization (between Member States of the EU or with third jurisdictions) of an instrument or an entity between two jurisdictions:

- In the case of a double deduction outcome: if the investor jurisdiction is a Member State, that Member State shall deny the deduction; or if the investor jurisdiction is a third country that has not denied the deduction, the Member State that is the payer jurisdiction shall deny the deduction.
- Deduction without inclusion outcome: if the payer jurisdiction is a Member State, that Member State shall deny the deduction; or if the payer jurisdiction is a third country that has not denied the deduction, the Member State that is the payee jurisdiction shall include the payment in its income.

These new rules would apply to FYs starting on or after 1 January 2020, except for those related to reverse hybrids which would apply to FYs starting on or after 1 January 2022.

Adjustment of the research and development (R&D) tax credit

The draft Bill provides for a decrease of the percentage (from 50% to 43%) of staff expenses taken into account as qualifying expenses to assess the lump-sum running costs referred to in Article 244 quarter B, II, c of the FTC. This measure would apply to expenses incurred during FYs starting on or after 1 January 2020.

Refund and deferred payment of withholding taxes and levies borne by foreign entities in a tax loss position

Further to a decision issued by the Court of Justice of the EU,[5] the draft Bill allows foreign entities in a tax loss position to claim a refund of:

- The withholding taxes on dividends provided by article 119 *bis* of the FTC
- The withholding taxes provided by article 182 A *bis* and 182 B of the FTC
- The levies on capital gains upon transfer of real estate shares or assets provided by articles 244 *bis*, 244 *bis* A and 244 *bis* B of the FTC

Regarding the withholding taxes on dividends, the eligible entities would be the foreign entities located in a jurisdiction which: (i) cannot be considered as a non-cooperative within the meaning of article 238-O A of the FTC; and (ii) that has concluded with France an agreement with an administrative assistance clause for the prevention of fraud and tax evasion, as well as an agreement with a mutual assistance clause for tax collection which has a similar scope as the EU directive.

Regarding the other withholding taxes and levies, the eligible entities would be the foreign entities located in an EU Member State, or in another State that is part of the European Economic Area (EEA) agreement which has concluded with France an agreement with an administrative assistance clause for the prevention of fraud and tax evasion, as well as an agreement with a mutual assistance clause for tax collection which has a similar scope as the EU directive.

The foreign entity that would benefit from such a refund, as per these new rules, would have to finally pay the tax when it becomes profitable or if the relevant annual tax compliance requirements are not fulfilled.

Moreover, the draft Bill specifies that said refund would be definitive in the case where the beneficiary foreign entity is in a tax loss position and is subject to a judicial liquidation or an equivalent procedure (as is currently the case for withholding taxes on dividends).[6]

These measures would apply to FYs starting on or after 1 January 2020.

Adjustment of the "branch tax"

Further to a recent decision from the *Conseil d'Etat* (French Administrative Supreme Court),[7] the draft Bill allows entities located in an EU Member State, or in another State that is part of the EEA agreement, which cannot benefit from the current exemption applicable to certain entities located in said States,[8] to avoid or limit the withholding tax provided by article 115 *quinquies* of the FTC if they are able to demonstrate that their profits have not been divested out of France. This measure would apply to FYs starting on or after 1 January 2020.

Endnotes

1. See EY Global Tax Alerts, *French Parliament approves draft bill on partial freeze of corporate income tax rate decrease*, dated 16 July 2019 and *French President signs bill on Digital Services Tax and partial freeze of corporate income tax rate decrease*, dated 25 July 2019.
2. See EY Global Tax Alert, *French Parliament approves Finance Bill for 2018 and second Amending Finance Bill for 2017*, dated 22 December 2017.
3. EU Directive 2016/1164 dated 12 July 2016.
4. EU Directive 2017/952 dated 29 May 2017.
5. CJUE, 22 November 2018, C-575/17, *Sofina SA, Rebelco SA, Sidro SA*.
6. Article 119 *quinquies* of the FTC.
7. CE, 10 July 2019, n° 412581, Sté Cofinimmo.
8. Article 115 *quinquies*, 3 of the FTC.

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