
European Tax Newsalert

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French Parliament introduces significant changes to the treatment of losses and capital gains on shares

On September 7 and 8, 2011, the Amended Finance Act for 2011 was passed by the French *Assemblée nationale* and *Senat* after an unusually quick legislative process.

The Amended Finance Act for 2011 is expected to be enacted within 15 days of its submission to the government i.e., by the end of September 2011 (unless a Constitutional review is undertaken).

Amongst other measures passed, the Amended Finance Act for 2011 contains the following two amendments that may significantly impact US and International groups with French operations or subsidiaries:

- A modification to the treatment of tax losses; and
- An amendment to the existing capital gains participation-exemption regime for the disposal of participating shares.



Modification to the treatment of tax losses

Currently, tax losses can generally be carried forward for an unlimited period of time (unless there is a significant change in business). In addition, tax losses can be carried back against the profits of the three preceding tax years of a company, with no limitation on the amount utilized. The new measures will now limit the amount of losses utilized by a company.

The new measures are as follows:

- **Tax loss carryforward**

Under the new provisions, a company may still carry forward its tax losses with no time limitation. However, tax losses carried forward will only be available to offset against EUR 1 million of taxable profits, plus 60% of the current year taxable profits exceeding that amount.

The portion of the tax losses that cannot be offset in a given year can be carried forward and offset against future taxable profits. Accordingly, companies with annual profits of more than EUR 1 million will be subject to tax on 40% of their taxable profits, notwithstanding that they have sufficient tax losses carried forward.

- **Carryback of tax losses**

Under the new provisions, a company will now only be entitled to carry back its tax losses to the fiscal year immediately preceding that in which the losses arose. The new provisions will limit the amount of carried back losses to EUR 1 million. Any unused surplus will be carried forward and available for use pursuant to the new rules.

In addition, a carryback election filing will be required to be made prior to the deadline for submission of the corporate tax return for the loss-making period. This new filing regime is more restrictive than the current regime that allows filing for current and previous fiscal years losses.

- **French tax groups**

The overall tax losses of a French tax group (fiscal unity), as well as pre-entry tax losses of the respective French companies of the group will be attributed, whether carried forward or carried back, in the same manner and within the same limits as those set out above.

The new rules regarding tax loss carryforwards and carrybacks will apply to fiscal years ending after the entry into force of the Amended Finance Act for 2011.

Given that the enactment of the Amended Finance Act for 2011 is expected by the end of September (unless Constitutional review), companies with a fiscal year ending after this date would then be immediately impacted by these new provisions.

Amendments to the French capital gains participation exemption regime

Currently, capital gains arising from the disposal of participating shares held for more than two years are 95% tax exempt. The remaining 5% is subject to French corporate income tax at the maximum corporate income tax rate of 34.43% (i.e., effective tax rate of 1.72%).

Under the new rules, the participation exemption on capital gains will now be reduced to 90%. Consequently, capital gains arising from the disposal of participating shares will be subject to an effective tax rate of 3.44% upon application of the maximum corporate income tax rate of 34.43%.

This new provision will apply to capital gains arising from the disposal of participating shares held for more than two years for fiscal years starting on or after January 1, 2011.

Conclusion

US and international groups with operations or subsidiaries in France should carefully review the potential impacts of these new measures, including impacts on profit sharing and deferred taxed assets.

For more information, please do not hesitate to contact:

Your international tax service team in the U.S.

Guillaume Glon 646-471-8240 g.glon@us.pwc.com

Guillaume Barbier 646-471-5278 g.barbier@us.pwc.com

Sebastien Delenclos 646-471-1971 sebastien.g.delenclos@us.pwc.com

Gilles de Vignemont 646-471-1301 gilles.j.de.vignemont@us.pwc.com

Your international tax service team in France

Renaud Jouffroy +33 1 56-57-42-29 renaud.jouffroy@fr.landwellglobal.com

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