

Overview

France imposes personal income tax on individuals resident in France in respect of their worldwide income and on non-residents in respect of French-source income. France has a territorial tax system with regard to corporate tax, which applies on profits allocable to a French business and on French-source income.

The French Tax Code also imposes a withholding tax on dividends distributed to non-residents and on certain interest payments, rents, royalties or management fees sourced in France. France has an extensive double tax treaty network that may reduce or eliminate French withholding tax on certain types of income.

As a signatory to the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI), France has agreed to adopt the minimum standards (principal purpose test and dispute resolution) as well as certain optional provisions. The ratification process has been completed and the convention became effective on January 1, 2019.

In addition to income tax, a turnover tax (VAT) is levied at the national level on goods and services supplied in France. Transfers of real estate properties and businesses may also incur transfer taxes.

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Legal system

France operates under a civil law legal system. French law is characterized by its division into two branches: public law and private law. Private law regulates disputes between private individuals, such as in civil, social and commercial cases. Private law litigation is settled in judicial courts, while litigation between private individuals and the state administrations is settled before administrative courts.

Taxation authorities

The tax system in France is administered by the Public Finance Department, which administers local taxes and/or sales tax for a number of local communities. The Public Finance Department is also in charge of auditing individual and corporate taxpayers.

Business vehicles

A non-resident may either establish a French business vehicle to carry on business in France or operate directly through a foreign entity (with or without a French permanent establishment). French business vehicles include corporations (limited liability) and partnerships (unlimited liability).

Partnerships

A partnership is generally treated as transparent for French tax purposes. The tax basis is determined by the partnership's net profits, but the tax is levied at the partner level based on their proportional share in the partnership profits. Subject to certain conditions, a partnership may opt for being subject to corporate tax. The liability of partners in a partnership is unlimited. There are no minimum share capital requirements for a partnership. Depending on its nature, a partnership may carry out a civil or commercial activity.

Corporations

Limited liability companies (SARL)

Limited liability companies (société à responsabilité limitée) are generally used for small and medium businesses. This corporate form is one of the most widely used in France due to the absence of minimum share capital requirements. SARLs can be created by one or more shareholders, and the shareholders are not liable for the SARL's debts.

Generally, SARLs are subject to corporate tax. However, if the SARL is formed by members of the same family, shareholders may opt to be personally subject to income tax on their share of the net profits of the SARL.

Joint stock companies (SA)

Joint stock companies (société anonyme) are generally used for larger businesses. SAs are the only French companies that can be listed. The minimum share capital to create an SA is €37,000. Non-listed SAs must have at least two shareholders and listed SAs must have at least seven shareholders. Shareholders of an SA are not liable for the corporation's debts. SAs are also subject to corporate tax.

Simplified joint-stock companies (SAS)

This company form (société par actions simplifiée) is widely used in France due to its flexibility. The rules around organization and operation are determined by the shareholders at the time of creation. SASes cannot be listed, but they can be created by only one shareholder, and they have no minimum share capital requirement. SASes are subject to the corporate tax. Subject to conditions, they may opt to be tax transparent.

Foreign corporations

A foreign corporation may be subject to French corporation tax on profits derived from a business carried on in France. A foreign corporation is said to be carrying on a business in France if it has a permanent establishment, a dependent agent or a 'complete commercial cycle' in France.

Where the foreign corporation is resident in a country with which France has a double-tax treaty, the foreign corporation will generally be exempt from French taxation on its business profits, unless it carries out its activity in France through a permanent establishment.

Financing a corporate subsidiary

Contributions for shares

Where an equity investment is made into a French corporation in exchange for shares, the amount of the investment is added to the corporation's stated capital account. Contributions in cash upon incorporation of a company are in principal exempt from stamp duty.

Debt financing

Withholding tax implications

French corporations are permitted to borrow funds from related or unrelated third parties without tax implications (subject to the limitations below). Furthermore, there are no French tax implications on the repayment of the principal amount of such debt. Interest payments made by a French resident corporation to a nonresident lender are exempt from withholding tax, unless such payments are made in a noncooperative jurisdiction¹, in which case a 75% withholding tax applies.

Limitations to interest tax deductibility

French tax law provides for two sets of rules that restrict the tax deductibility of financial expenses. The first restriction relates to financial expenses incurred under related-party loans, and the second provides for a general deduction limitation.

In the case of related-party loans, there is a maximum interest rate limitation. The tax deduction of interest expenses paid to direct and indirect shareholders is in principle limited by reference to a maximum fiscal interest rate provided for by the French Tax Code, which is currently approximately 1.31%, unless the relevant lending shareholder(s) qualifies as a related party to the borrowing entity, in which case a higher rate may be applied if it can be justified that it is a market rate.

In accordance with the Anti-Tax Avoidance Directive, a French anti-hybrid mechanism applies, which provides that:

- i. The deduction of interest should be denied in France when the interest could have been deducted both in France and in another jurisdiction;
- ii. The deduction of interest should be denied in France when the interest was deductible in France without being taxed in the other jurisdiction;
- iii. The payment received in France should be taxed if, because of its hybrid nature, it was deductible in another jurisdiction and not taxed in France.

The second restriction is a general deduction limitation. Since 2019, there is a general capping mechanism, where the deduction of net financial expenses (NFE) is limited as per the provisions of the European Union Anti-tax Avoidance Directive, as implemented in the French legislation. NFEs are deductible to the extent they do not exceed 30% of the borrower's EBITDA, and are fully deductible if they do not exceed €3 million per financial year.

When companies are defined as "autonomous", they may deduct 75% of the non-deducted NFEs. From an accounting point of view, companies are considered autonomous if they do not belong to a tax-consolidated group, and do not have any associated enterprise or permanent establishment abroad.

NFE is defined as the excess of the financial expenses incurred by the taxpayer over its financial revenues.

The financial expenses and financial income include any interest paid/ received in respect of any type of indebtedness and claims.

In addition to being able to deduct 30% of the borrower's EBITDA, the taxpayer, to the extent it belongs to a consolidated group, may deduct 75% of the non-deducted NFE, if its ratio of own funds to total assets is equal to or higher than the own funds to total assets ratio of the group to which it belongs.

Thin capitalization rules

As an exception to the above rules, a portion of NFEs related to the interest paid to affiliates is deductible only to the extent it does not exceed 10% of the EBITDA, if the taxpayer is thinly capitalized, and is fully deductible if it does not exceed €1 million per financial year.

The taxpayer is deemed to be thinly capitalized if its affiliated debts to own funds ratio exceeds 1.5 to 1. The affiliated

debts corresponding to a group centralized cash management tool are not taken into account.

The taxpayer would be still entitled to the 30% EBITDA deduction if one of the below conditions is met:

- i. The affiliated debts to own funds ratio of the consolidated group to which it belongs is higher than its own ratio
- ii. The taxpayer is a credit institution or is eligible as a specialized financing entity.

Corporate income tax

For companies with a taxable profit equal to or greater than €250 million (this threshold being determined at the level of a tax-consolidated group), the CIT rate is:

- i. 31% for fiscal years starting on or after 1 January 2020, while a CIT rate of 28% is levied on the first €500,000 of taxable profit (already effective for fiscal years beginning January 1, 2019);
- ii. 27.5% for fiscal years starting on or after January 1, 2021.

For companies and tax-consolidated groups with a revenue below €250 million, the CIT rate is:

- i. 28% for fiscal years starting on or after January 1, 2020;
- ii. 26.5% for fiscal years starting on or after January 1, 2021.
- iii. 25% starting in 2022

A reduced rate of 15% applies to small and medium corporations with net taxable profits below €38,120.

In addition to corporation tax, a social surtax of 3.3% applies to taxpayers, where their corporate tax liability of the relevant fiscal year exceeds €763,000. The surtax is assessed on the principal amount of the corporation tax due.

Capital gains

Resident French entities are in principle subject to French corporate tax at the standard rate with respect to capital gains derived from the sale of shares in other companies. However, the disposal of shares that qualify as investment shares and which have been held for at least two years at the time of the sale may be exempt up to 88% of their amount, so that only a 12% fraction of the gain remains subject to corporate tax at the standard rate.

The above does not apply in respect of shares in real estate companies where the company's assets comprise mainly of real estate (other than real estate allocated to a commercial or industrial activity). Capital gains on the disposal of such shares remain subject to corporate tax at the standard rate.

Non-resident entities are also generally taxable on the disposal of "taxable French property," which includes *inter alia*:

- i. Real or immovable property located in France
- ii. Property (including goodwill) used or held by a taxpayer in a business carried out in France
- iii. Inventory forming part of a business in France
- iv. Shares in French real estate companies
- v. Shares in French companies that are subject to corporation tax, where the non-resident entity holds directly or indirectly 25% of the share capital of the relevant entity.

Branch remittance tax

After-tax profits of a French branch of a foreign company are deemed to be distributed to non-residents and are subject to a 28% branch tax. However, since 2020, the branch can prove that the profits made in France stay in France and are not invested elsewhere. The presumption is therefore no longer irrefutable and companies can ask for a refund of the branch remittance tax. This tax may be reduced or eliminated under applicable tax treaties and is not due if the foreign company is located in another European Union (EU) member state or a member state of the European Economic Area.

Computation of taxable income

Taxable base

A taxpayer is subject to tax on its profits from carrying on its business. Profit is generally considered to be its

revenues less its deductible expenditures. Subject to certain conditions (i.e., direct or indirect shareholding of at least 95% of the share capital of the relevant entities), the parent company of a group of companies may consolidate for corporate tax purposes, the net profits and/or losses of all or part of the French companies that are members of the same group. In this case, corporate tax is assessed in the hands of the parent company on the net consolidated result of the group.

Deductions

A taxpayer is generally permitted to deduct its current expenses in computing business income. As a general rule, capital expenses are not deductible. Moreover, the tax deductibility of certain expenses such as financial expenses may be specifically limited by the French tax law.

Ordinary tax losses may be carried forward indefinitely, but may be offset against the taxable profits of a given fiscal year only up to an amount of €1 million, plus 50% of the taxable result in excess of that threshold. Tax losses may be carried back for one year in certain cases, up to €1 million.

Income tax reporting

French resident corporations and non-resident corporations that carry on business in France are required to file an annual corporate tax return. The annual corporate tax return must in principle be filed within three months following the end of the relevant fiscal year (the applicable deadline is four months if the fiscal year corresponds to the calendar year). Installment payments are required in respect of current-year taxes, and interest on any unpaid tax balance up to 0.2% per month of delay.

Cross-border payments

Transfer pricing

France's transfer pricing regime generally conforms to the arm's length principle of the Organisation for Economic Co-operation and Development (OECD). The price set between related parties should be the same as the price that two unrelated arm's length parties would agree to. The French legislation allows the administration to ensure compliance with this principle and to adjust pricing when benefits have been indirectly transferred abroad, either through the increase or decrease of sale prices, or by any other means. Companies exceeding certain thresholds must maintain contemporaneous transfer pricing documentation.

Withholding tax on services fees

Amounts paid by a debtor established in France to a foreign company, in remuneration for certain services rendered or used in France or intellectual property products, are subject to withholding tax in France where the foreign company does not have a permanent professional facility in France. The applicable rate is the standard corporate tax rate and tax is levied on the gross amount paid, excluding VAT. The applicable rate may be increased to 75% for some of the amounts paid to persons established in a non-cooperative jurisdiction (see above).

Payroll taxes

Employers are required to pay, in addition to salary, social security contributions that cover: sickness insurance, maternity insurance, invalidity insurance, death and basic retirement insurance, and employment insurance contributions. Employees also contribute to social security and amounts are collected and remitted by the employer to various organizations. The contributions of both the employer and the employee are calculated on the employee's gross earnings. Contributions amount in average to approximately 40% for employers and to approximately 25% for employees.

Indirect taxes

Value-added tax (VAT)

France follows the EU legislation on value-added tax. The current VAT rate in France is 20% and is imposed on the

final domestic consumption of most goods and services supplied in France. For EU-based companies, VAT is chargeable on most sales and purchases within the EU. VAT is not charged on exports to jurisdictions outside the EU. A reduced rate of 10% is applied to some food products, pharmaceutical products, and domestic passenger transport. A second reduced rate of 5.5% is applied to goods or services considered in the good interests of society, including some food products, school canteens, medical equipment for disabled persons, and some domestic care services. The rate of 0% is applied to intra-community and international transport.

Entities and individuals (including non-residents) that are involved in taxable supplies in France in the course of a commercial activity are required to register for and charge, collect and remit VAT on such supplies. Each registrant that makes taxable supplies is generally entitled to recover any VAT paid on its inputs. Subject to certain exceptions, input VAT incurred by a taxpayer in the course of its commercial activity is generally deductible from its output VAT.

Other taxes

Local economic contribution (CET)

The CET includes two specific taxes. The first is the company property tax (cotisation foncière des entreprises) (CFE), which is based on the rental value of the properties owned by the taxpayer. The second is the contribution on added value (cotisation sur la valeur ajoutée des entreprises) (CVAE), which is levied at a progressive rate ranging between 0% (turnover not exceeding €500,000) and 1.5% (turnover exceeding €50 million).

Land tax

The land tax on built properties applies to taxpayers that own buildings fixed to the ground. New constructions, reconstructions and additional constructions can be exempt from this tax for two years. The rate of the land tax may vary depending on the location of the taxable property, and the tax is assessed on the rental value of the taxable property, as determined by the tax authorities.

Transfer taxes

The sale of real estate property generally gives rise to real estate transfer tax at a maximum rate of 5.8% (plus a 0.1% real estate security contribution), assessed on the sale price. The transfer of a going concern, or operating business, is subject to a 5% transfer tax.

The sale of shares in an SARL or a partnership is subject to a 3% transfer tax, whereas the sale of shares in an SA or SAS is subject to a 0.1% transfer tax. The applicable rate is increased to 5% where the company whose shares are transferred qualifies as a real estate company. For transfer tax purposes, a real estate company is a company whose assets mainly comprise real estate.

A financial transaction tax of 0.3% applies to transactions related to shares of listed companies established in France and having a market capitalization exceeding €1 billion.

1. The list of non-cooperative jurisdictions is established by the French tax authorities and in general, updated each year. Currently, this list includes the following jurisdictions: Aguiila, Bahamas, Fidji, Guam, the American Virgin Islands, BVI, Oman, Panama, Samoa, American Samoa, Seychelles, Trinidad and Tobago, and Vanuatu.↩

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