2020 draft French budget includes ATAD II and corporate tax rate provisions

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In brief

The French government on September 27 released its draft budget for fiscal year 2020 ('the draft budget'). The draft budget includes corporate tax measures designed to transpose into French law Articles 9, 9 bis, and 9 ter of EU anti-tax-avoidance directive 2016/1164 dated July 12, 2016 (ATAD I) as modified by EU directive 2017/952 dated May 29, 2017 (ATAD II). The document also includes other EU-compliant measures and proposes to postpone, for large companies, the scheduled reduction of the corporate income tax rate.

The French Parliament will now review, debate, and amend the entire draft budget. This legislative phase will last several weeks before Parliament votes on and enacts a final budget. If enacted as proposed, most of the measures will apply for tax years beginning on or after January 1, 2020, and could affect multinational enterprises (MNEs) with French operations or subsidiaries. Note: The draft budget contains other tax proposals that are not covered in this Insight.

In detail

ATAD II, including hybrid mismatches with third countries

ATAD I and II Directives were introduced as part of the 2015 OECD Base Erosion and Profit Shifting (BEPS) report, Action 2, on neutralizing the effects of hybrid mismatch arrangements.

The draft budget proposes to transpose ATAD II into French law under new Articles 205 B, C, and D of the French Tax Code - essentially focusing on double deductions and deduction without inclusion situations that would apply not only between EU Member States, but also in situations involving third countries.

Applicability

- The proposed new articles provide that hybrid mismatches could result from:
- Payment under a financial instrument giving rise to a deductible expense in the residence country of the payor without inclusion in the taxable income in the residence country of the beneficiary, where the mismatch outcome is attributable to the differences in the tax characterization of the instrument or the underlying payment.
- Expense deduction in the residence country of the payor without inclusion in the taxable results in the residence country of the hybrid entity, when such outcome results from differences in the laws in the residency country of the hybrid entity governing the allocation of that payment to the hybrid entity and the laws of the residency country of any person with a participation in such hybrid entity.
- Payment made to an entity with one or several permanent establishments with expense deduction in the residence country of the payor without inclusion in the taxable results of such entity as a result of differences in the residence country laws of a head office and its permanent establishment, or between two or more permanent establishments of the same entity pursuant to the laws of the countries in which such entity performs its activities.
- Expense deduction in the residency country of the payor of a payment made to a permanent establishment without inclusion in the taxable income in the country of the permanent establishment under the laws of such country as not treated as a permanent establishment (i.e. disregarded permanent establishment).
- Expense deduction in the residence country of a hybrid entity (payor) without inclusion in the taxable results of the beneficiary as a result of the laws of the residence country of the beneficiary treating such payment as not includible (i.e. disregarded payment).
- Expense deduction in the country of a permanent establishment without inclusion in the taxable income of the beneficiary with respect to a deemed payment between a permanent establishment and its head office or between two or more permanent establishments, as a result of the laws of the residence country of beneficiary treating such payment as not includible. (i.e. deemed branch payment).
- Double deductions resulting from payments giving rise to a deduction of the same payment, expenses, or losses in the residence country of the payor and in another country. In the case of a payment by a hybrid entity or a permanent establishment, the residence country of the payor is the one where the hybrid entity or the permanent establishment is established or situated.

Associated entities

The draft budget provides that the rules would apply between ‘associated entities’ as defined under French law with two main direct and indirect thresholds (25% and 50% of voting rights, share capital, or rights to profits) and would apply depending on the type of hybrid mismatch at stake (e.g., 50% for reverse hybrids). It also includes a provision covering persons acting jointly with another person in order to be considered an associated entity.

Inclusion

The draft budget provides that a payment is deemed included in the residency country of the beneficiary if it does not give rise to an exemption, a tax rate reduction, or a credit or a tax refund (other than a withholding tax) and such inclusion occurred during a tax year that began within 24 months following the end of the tax year during which the expense gave rise to deduction.

It also provides that when a payment gives rise to a deduction without inclusion, the deduction should be denied at the level of the French payor. Or, as a secondary rule, if a deduction arose at the level of a foreign payor, the payment should be included in the taxable income of the French payee. A similar provision addresses situations resulting in double deductions (with a corresponding safe-harbor covering double inclusion situations).

When a deductible payment offsets another hybrid payment, directly or indirectly, through a transaction or a series of transactions between associated entities of a taxpayer or through a structured transaction, the deduction on such first payment is denied unless the residency country of one of these entities involved in the transaction neutralizes the impact of such hybrid transaction (if partially neutralized, the deduction then would be partially allowed).

Where a hybrid transfer results in withholding tax relief on a payment derived from a financial instrument transferred to several parties involved in the transfer, the relief would be pro-rated based on the net taxable income related to such payment.

Dual residency

Where dual residency in France and another country gives rise to double deduction of a taxpayer's payments, expenses, or losses, the deduction would be denied in France unless (i) the income is dual inclusion income (although the draft law is unclear in that respect); or (ii) the other country is a EU Member State that denies the deduction and the tax treaty between France and the other Member State considers that the taxpayer is tax resident in France.

Reverse hybrids

The draft budget includes provisions relating to reverse hybrid entities constituted or established in France. Under the proposed draft, France would opt for an exception to apply this provision with respect to collective investment vehicles.

Elimination of current anti-hybrid rules on interest payment*s*

As a result of the transposition into French law of ATAD II, the current French 'anti-hybrid/subject-to-tax' rules applicable to interest (under Article 212, I-b of the French Tax Code) would be eliminated.

These proposed draft budget provisions would apply to tax years beginning on or after January 1, 2020, with the exception of the reverse hybrid provisions, which would apply to tax years beginning on or after January 1, 2022.

Postponement of the corporate income tax rate reduction

The draft budget proposes to postpone, with respect to large companies only, the French corporate income tax rate reduction originally enacted as part of the 2018 French budget. For tax years beginning on or after January 1, 2020 and until December 31, 2020, French companies with revenues exceeding EUR 250M would not benefit from the general 28% reduced corporate tax rate but would be subject to a 31% rate for the portion of taxable income exceeding EUR 500,000 (28% below such threshold).

For tax years beginning on or after January 1, 2021 and until December 31, 2021, French companies with revenues exceeding EUR 250M would be subject to a 27.5% rate. No changes would apply with respect to the scheduled rate reduction to 25% for tax years beginning on or after January 1, 2022. For companies with revenues not exceeding EUR 250M, the scheduled corporate tax rate reductions would remain unchanged.

Adjustment of certain withholding tax and levy rates to the French corporate tax rate

The draft budget proposes to align or clarify certain withholding tax and levy rate alignments - in particular, the 30% withholding tax rate provided for by article 187 of the French Tax Code, article 182B, 244 bis, 244 bis A&B of the French Tax Code - with the French corporate tax rate reductions scheduled over the next few years.

These provisions would apply to triggering events occurring on or after March 6, 2019 and, for withholding taxes under article 119 bis of the French Tax Code, would apply on or after January 1, 2020.

Other proposed EU-compliant measures

Amendments in compliance with the EU Freedom of Establishment

Following the French Administrative Supreme Court decision dated July 10, 2019 (Societe Cofinimmo #412581), the draft budget proposes to amend article 115 quinquies of the French Tax Code (i.e., withholding tax provision on deemed distributed profits realized in France by foreign companies).

The proposed amendment provides that an EU or European Economic Area (EEA) company would be entitled to a withholding tax refund when the amounts subject to French withholding tax have not been divested out of France. The proposed measure would apply to tax years beginning on or after January 1, 2020

Amendments in compliance with EU Free Movement of Capital

Following an ECJ decision dated November 22, 2018 (C-575/17 Sofina SA, Rebelco SA and Sidro SA) regarding French dividend withholding tax application to loss-making Belgian companies, the draft budget proposes the following main changes to French legislation:

- For loss-making foreign companies under a compulsory liquidation procedure (or comparable) or in a dire financial situation with impossibility to recover, a withholding tax exemption would be granted not only to dividends, but also to withholding tax and levies on certain interest, payments, services, real estate gains, and non-resident capital gains (articles 119 bis, 182 A&B, 224 bis, bis A, and bis B of the French Tax Code).
- Only a temporary refund will be granted for loss-making foreign companies in a situation to recover financially, until the foreign company becomes profitable and subject to filing and compliance obligations with the French Tax Authorities by the foreign beneficiary.

With respect to withholding taxes and levies under article 119 bis of the French Tax Code, the above provision would apply to foreign entities that are not located or established in non-cooperative states and territories pursuant to French legislation, and in jurisdictions having concluded both a mutual assistance convention regarding the tackling of fraud and tax evasion as well as a mutual assistance convention regarding tax collection with a similar scope to the EU Directive 2010/24 dated March 16, 2010.

With respect to the other types of levies and withholding taxes, the compliance amendments would only apply to foreign entities in EU Member states, or EEA states having concluded a mutual assistance convention regarding the tackling of fraud and tax evasion as well as a mutual assistance convention regarding tax collection, with a similar scope to the EU Directive 2010/24 dated March 16, 2010.

The proposed provisions would apply to tax years beginning on or after January 1, 2020. Situations prior to that date would have to be reviewed and addressed through refund claim procedures.

Transfer of isolated assets within the EU

Pursuant to the French Tax Code, a specific election allows for taxation over five years of built-in gains relating to asset transfers upon a transfer of a company seat or of one of its permanent establishments in another EU Member state, or EEA state having concluded a mutual assistance convention regarding the tackling of fraud and tax evasion as well as a mutual assistance convention regarding tax collection. This provision would be extended to transfers of one or several isolated assets and would apply to tax years beginning on or after January 1, 2020.

Proposed transposition of EU Directive online business VAT regime

EU Directive 2017/2455 was intended to simplify the VAT regime applicable to online businesses in the EU. The draft budget proposes to transpose the EU Directive into French law and includes:

- A minimum single gross revenue threshold of EUR 10,000 over all Member states for intra-EU distance sales of goods. Above this threshold, distance sales would be taxed in the Member state of consumption.
- The existing and so-called 'mini one stop shop' (MOSS) would be extended to such intra-EU distance sales and to services for which VAT is due in another Member state other than the one where the provider is situated (OSS).
- Regarding distance sale of imported goods from third countries or territories to the EU, a new taxation regime would apply for consignments with a value under EUR 150 and an IOSS (“Import One Stop Shop”) would be set up for such transactions.

In order to facilitate the VAT collection process and reduce the administrative burden for sellers, consumers, and tax authorities, online platforms would be liable for the VAT with respect to distance sales of imported goods with a value under EUR 150 or with respect to domestic delivery or intra-EU distance sale of goods through the platform by a seller not established in the EU to a non-taxable person.

Regarding distance sale of imported goods, online platforms would be liable to import VAT in lieu of the person indicated as the real recipient of the goods on the import filings, even above the EUR 150 threshold. The online platforms would need to keep a special register for 10 years for control purposes by the tax authorities.

These proposed provisions would apply from January 1, 2021.

New 'Name and Shame' procedure against non-cooperative online platforms

The draft budget contemplates a new sanction consisting in the publication online of the identity of platform operators that repeatedly failed to comply with their French tax obligations.

In order for the sanction to apply, the platform would need to have first defaulted to certain listed obligations followed by another default within 12 months.

It notably covers:

- VAT for which the platform is jointly liable for not requiring its professional users to be compliant with their VAT obligations.
- A penalty for absence of answer to a request from the French tax authorities under article L.81 al.2 or L.82 AA of the Tax Procedural Code.
- A penalty for default filing obligations regarding income realized by its users through the platform.
- A taxation resulting from an automatic tax assessment procedure regarding VAT on online distance sales of goods realized through the platform.
- A taxation resulting from an automatic tax assessment procedure regarding the French digital tax.

The publication could not last more than one year and would be removed from the website as soon as the amounts due (tax liability or penalties) are paid by the platform. The proposed provisions would apply as from January 1, 2020.

The takeaway

MNEs operating in France should consider the impact of the draft budget with respect to their international flows, structure, and tax obligations. Enactment of such proposed provisions could occur by the end of December 2019.

Let’s talk

For a deeper discussion of how this issue might affect your business, please contact:

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