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France tax alert

Scope of exemption from 3% surtax to be broadened

The French government has decided to maintain the exemption from the 3% surtax for dividends distributed within members of a French tax-consolidated group, and to broaden the scope of the exemption. According to measures included in the amended finance bill for 2016, released on 18 November 2016, the exemption would be extended to distributions made by French subsidiaries to their foreign parent companies, provided a 95% ownership requirement is met, and it would be irrelevant whether the foreign parent is resident within or outside the EU.

Once approved by parliament, the new rule would apply to dividends paid as from 1 January 2017. Dividends paid in 2016 would not benefit from the expanded scope of the exemption.

Background

The 3% surtax, imposed on French entities subject to corporate income tax, is levied on most dividend distributions at the level of the French distributing company. However, profits distributed by a company that is a member of a French tax-consolidated group to another group company are exempt from the surtax, whereas profits distributed by a French tax-consolidated group company to a nongroup company (or vice versa), and distributions made within a non-tax-consolidated group fall outside the scope of the exemption.

France's constitutional court concluded on 30 September 2016 that the exemption from the 3% surtax for tax-consolidated groups does not comply with the equality principle in the French constitution and, therefore, the exemption is unconstitutional (for prior coverage, see the alert dated 5 October 2016). According to the court, the difference in treatment between distributions made within a tax-consolidated group (which may have only French members) and those within a non-tax-consolidated group cannot be justified by the difference in situations or by reason of the public interest. The court ruled that the exemption is to be abolished as from 1 January 2017 unless new legislation is enacted before that date.

As a result of the decision of the constitutional court, the French government had to decide whether to allow the exemption to be abolished, to abolish the surtax itself (and replace it with a new compliant tax) or find an alternative solution. Because the abolition of the exemption would have been costly for French groups, the government has decided to maintain the exemption but to broaden its scope to remove the discriminatory aspect.

According to the amended finance bill for 2016, the new exemption would apply to distributions made by a French subsidiary in the following cases:

- Where a French parent company holds, directly or indirectly, at least 95% of the French distributing company, and the two companies qualify to be members of the same tax-consolidated group (regardless of whether an election is actually made for tax consolidation); and
- Where the distribution is made to a foreign parent company and that foreign parent (i) is subject to a corporate tax similar to the French corporate tax in another EU member state or in a non-EU country that has signed an agreement containing an administrative assistance clause with France (unless the latter country is deemed to be a “noncooperative country” for French tax purposes); and (ii) the foreign parent would be able to meet the requirements for being a member of the same tax-consolidated group as the distributing company had it been established in France, in particular, because the foreign parent holds at least 95% of the distributing company.

To offset the revenue implications of the broader exemption, the government is proposing to require an advance payment of the special social contribution (i.e. the “C3S” contribution) for the largest companies. The C3S currently is paid in the year following the year in which the company recorded the relevant turnover.

Comments

The exemption from the 3% surtax, as well as the surtax itself, have been the subject of considerable controversy. In addition to the above far-reaching decision of the constitutional court, the European Commission has initiated an infringement procedure against the surtax itself and France’s Administrative Supreme Court has referred a case to the Court of Justice of the European Union (CJEU), requesting a preliminary ruling on whether the surtax is in line with the EU parent-subsidiary directive.

The proposed broadening of the scope of the exemption would only remove the element of the surtax that the constitutional court found to be incompatible with the equality principle of the French constitution. The government did not take the opportunity to fully revise the basic premise of the surtax, which may not stand up to the scrutiny of the CJEU (particularly if the CJEU agrees with the recently released opinion of Advocate General Kokott that found the Belgium fairness tax—which involved issues similar to those raised by the French surtax—to be partly incompatible with the parent-subsidiary directive).

The parliament will debate the amended finance law for 2016 beginning the week of 21 November, with final approval expected in mid-December 2016.

Contacts

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