Is France a Tax (Credit) Heaven?

The adoption of the Finance Act for 2013 and the third Amending Finance Act for 2012 have been perceived as causes of decline in investments in France. May we prove that it is not so bad with three examples of tax credits that France has to offer?

The New Tax Credit for Encouraging Competitiveness and Employment (CICE)

Effective since 1 January 2013, the CICE is a new tax credit in France designed to foster competitiveness of French businesses. It will enhance investments, innovation, training and employment, and will contribute to reduce labor costs

Scope

It will benefit to all businesses, whether French or foreign provided it is subject to corporate income tax or personal income tax in France, and regardless of their legal status (sole proprietorship, partnership, corporation) and their industry (commercial, manufacturing, services, agriculture).

The CICE will also apply to entities that already benefit from a favorable tax regime (tax-exempt companies such as new firms, innovative start-ups, companies created for taking over a struggling company, located in competitive cluster…).

Statistic shows that it should lower labor costs by 2.6% creating 150 000 jobs by 2018. The Construction industry and the service industry should be the biggest beneficiaries from the CICE.

Conditions and rate

Few conditions apply to the CICE except that the firm must pay salaries to its employees – this excludes self-employed profession such as lawyer, doctor to a certain extent – as the CICE is supposed to finance a € 20 billion annual reduction in labor costs (financed by an increase of the VAT rates) and because the basis of the CICE will be the wages paid during the calendar year provided they do not exceed 2.5 times the French minimum wage (i.e. gross salary below € 3,500 per month).

The rate of the CICE will be 4% in 2013 and 6% for 2014 and subsequent years. It will apply to the gross salary.

What to do with it

As a general rule, the CICE will be offset against income tax whether personal or corporate that is due during the year when the wages are paid. The excess of CICE over the income tax payable will be carried forward and offset against any subsequent income tax liability up to three years. Unused CICE after this 3 years period will be refunded.

Small or medium enterprises (SME) as defined in EU law, (headcount less than 250 employees, annual turnover lower than € 50m, or a total balance sheet lower than € 43m), innovative start-ups or struggling companies may benefit from an immediate refund of the unused part of the CICE.

Finally, CICE receivables may be assigned to banks and other credit institutions (Oséo for instance).

The Research Tax Credit

It is generally admitted that the Government can foster an industry directly via grant and subsidies (e.g. Common Agricultural Policy or CAP) or indirectly through tax incentives such as a tax credit.

The Organisation for Economic Co-operation and Development (OECD) explained that governments support R&D business because it is seen as crucial investment in the long-run growth of economy, it helps maintain jobs especially in times of crisis, it contributes to national competitiveness, and it creates public goods as it generate knowledge spill over (see OECD (2010a), “R&D tax incentives: rationale, design, evaluation”, OECD, Paris.)

According to the OECD, the French Research Tax Credit (CIR) is one of the leading tax incentives in the world. It places France in the 5th place in terms of government funding of business R&D (after the United States, Japan, and Canada, and before the United Kingdom).

The French R&D tax credit benefits to companies subject to corporate income tax in France, and that engaged in R&D. The CIR rate is 30% for eligible expenses less than or equal to 100 million euros and 5% for expenses above this amount.

Only R&D activities defined as fundamental research, applied research, and development research are included in the scope of the R&D tax credit. In these categories, the main types of expenses that can benefit from the tax credit are depreciation of assets dedicated to R&D projects, employees costs (salaries and social contributions), operating expenses dedicated to R&D, research activities subcontracted to other firm even firms located outside of France but in the EU, costs relating to compliance to regulatory affairs.

This tax credit can be combined with a tax incentive affecting revenue from license of patents and other eligible IP rights (the revenue can be taxed at a 24,43% rate, lower than the standard corporate income tax rate of 33,33%.

The CIR is offset against CIT due. The excess portion of the CIR over CIT due can be carried forward for three years and be refunded after this period.

An immediate refund is possible for tax-exempt new firms, innovate start-ups, and corporations that qualify as SME.

The French finance Act for 2013 expanded the scope of the R&D Tax credit to certain innovative expenses.

The Innovation Tax Credit (ITC)

The Finance Act for 2013 creates the innovation tax credit (ITC) on the CIR model.

It applies to companies that meet the EU definition of SMEs (fewer than 250 employees, turnover not exceeding € 50 million or balance sheet total not exceeding € 43 million).

The ITC rate is 20% applicable on eligible expenses (up to € 400 000, hence a maximal ITC of € 80 000).

Eligible expenses are of the same nature as the ones eligible to CIR but also include the design of prototypes or pilot plants for new products. Definitions of prototype and pilot plant are the same as those used in the CIR.

The new product is defined as a tangible or intangible property that meets two cumulative conditions: (i) not be made available on the market and (ii) distinguishable from prior or existing products through enhanced performance on a technical level, eco-design, ergonomics or functionality.

As part of the CIR, it can be offset against CIT due or refunded for SME and certain other companies.

Comment

These tax credits are among a longer list of tax incentives (for instance attractive depreciation rules). Entrepreneurs and business decision-makers should consider these incentives when looking at the best place to develop their business.

Whilst France is not a tax heaven, it is far from being a tax hell. It may just be the right place to do business.

Written by:

Romain Pichot – Partner, Tax
Tel: +33 1 58 44 92 92
rpichot@courtois-lebel.com

Julien Steinberg – Associate, Tax
Tel: +33 1 58 44 92 51
jsteinberg@courtois-lebel.com

COURTOIS LEBEL