

Correspondant organique de :

Legipass

8, rue Auber - 75009 PARIS

www.legipass.com

Finn Larsen Advokatfirma

Algade 43, 1 - 4000 Roskilde -Danemark

www.advokat-firma.dk

Horizons China Corporate advisory

1801 Lippo Plaza, 222, Huaihai Middle Road

Huangpu, SHANGAI PR China 200021

www.horizons-advisory.com

Nice, February 9th 2016

Object : Implementation of the French exit tax

CONTEXT

The fight against tax evasion processes, and in particular when they result in the relocation of the most important incomes and patrimonies, is one of the objectives of the legislator. The French exit tax, put in place to try to slow French tax relocations, is a very technical mechanism on both substantive and declarative aspects, but also on the modalities of the suspension of payment and events leading to tax relief or refund.

We are going to present the implementation of this scheme, in a synthetic and practical way, through concrete examples concerning relocation in the EU in Iceland or Norway, the articulation of exit tax and deferrals, and relocation outside the EU.

COMMENTS

1. Relocation in the EU, Iceland or Norway

A taxpayer who transfers his fiscal domicile on year N must submit on N+1 a declaration n° 2042, accompanied if necessary by its exhibits (No. 2042-C and No. 2042 NR in particular) and form No. 2074-ETD, to the personal income tax service ("*Service des impôts des particuliers*") on which his tax domicile depended before the transfer.

- **For the period between January 1 and the day of departure of year N:** the taxpayer declares on the form No. 2042 the amount of his worldwide income, excluding income acquired before his departure but not available to him.
- **For the period after the transfer of domicile:** pursuant to the provisions of Article 167 of the French Tax Code, the taxpayer declares the amount of his French source income taxable in France by application of the applicable tax treaty (exhibit No. 2042 NR). Information is given on the terms of return ("*declaration*") in Information Document No. 2041 E - Persons domiciled outside France - Income tax 2015.

Cabinet BRAHIN Société d'Exercice Libérale à Responsabilité Limitée inscrite au Barreau de NICE

E-mail: info@brahin-avocats.com

www.Brahin-avocats.com

- **For the exit tax, the taxpayer must declare on Form n° 2074-ETD:**

- Unrealized capital gains, receivables of additional price and capital gains in deferral (*“plus-values en report”*) that became taxable in accordance with Article 167 bis of the French General Tax Code (GTC);
- The amount of tax attributable to such capital gains and receivables and the items required for its calculation;
- The date of the transfer of his tax domicile outside France;
- The address of his new fiscal residence.

- **The following years, and throughout the period of residence abroad**, the taxpayer who intends to benefit from the suspension of payment must subscribe annually for 15 years forms 2042, 2042-C and 2074 -ETS precising the amount of initial capital gains and receivables, the amount of capital gains carried forward and the amount of tax that is deferred of payment (*“sursis de paiement”*).

These returns are to be filed with the tax department of non-resident individuals. Failure to comply with these obligations or the inaccuracy of the data which must be included in it shall make the amount of the deferred tax payable. However, if the taxpayer regularizes his situation within 30 days of receiving the official notice (*“mise en demeure”*) from the Administration, the deferment is maintained.

- **In the event of an event terminating the deferment**, the taxpayer must file Forms 2042, 2042-C and 2074-ETS in the year following the expiry of the deferment of payment in the deadline for the submission of the overall declaration. He shall declare on form No. 2074-ETS the nature and date of the event terminating the suspension, the amount of the unrealized capital gains concerned and the calculation of the tax that has become due. In the event of a disposal for valuable consideration of the securities, if a depreciation is recognized, it may be offset against the gain realized on the transfer of the tax domicile.

- **At the expiration of the 15-year period**, the taxpayer declares the nature and date of the event that justifies the request for automatic relief from tax deferred payments or the refund of tax paid upon the departure of France.

- **In the case of a new transfer of residence**: the taxpayer must inform the tax office of non-resident individuals of any transfer of the tax domicile after his initial transfer with the address of the new domicile in the two months following this new transfer. In the event of the second transfer of fiscal domicile taking place outside the EU, Iceland or Norway, suspension of full payment of rights shall cease. The taxpayer must therefore pay the tax that became payable on his transfer, except if he claims the benefit of the deferment of payment on option.

2. Articulation of exit tax and tax deferral arrangements

- **Departure after the exchange of securities which resulted in the recognition of a capital gain in deferral (*“en report”*) or deferment (*“en sursis”*).** - The exit tax relates in particular to all capital gains on disposals or exchanges placed under one of the deferment or deferral regimes in years prior to the transfer of the tax domicile.

Thus, the capital gains contributions to a company subject to the corporate tax and controlled by the contributor (GTC, Article 150-0 B ter) must be declared and taxed in respect of the exit tax, except for the benefit of deferment of payment. In this case, a 2074-ETD and lines 1047 and 1048 of Form 2074 should be completed.

Example:

By way of illustration: A taxpayer brings the shares he holds in a company subject to the corporate tax he has created for less than 2 years (A) to a personal holding he holds by 100% (B), then he transfers its tax domicile to Luxembourg with assets valued at € 1 million. The purchase price per share A is assumed to be 1.

- **At the date of the contribution**, the shares held by the taxpayer in company A are each valued at 101. This contribution transaction therefore yields a capital gain on each A share of 100 that can be placed under tax deferral by the taxpayer pursuant to the provisions of Article 150-0 B ter of the CGI.

- **The departure of the taxpayer in Luxembourg immediately after this supply operation** entails questioning the deferral of taxation in respect of the exit tax. Thus, the capital gain per share of 100 placed in deferral becomes taxable when the taxpayer leaves. However, the tax on income and social contributions due on the basis of this surplus value may benefit from the deferment of payment.

The transfer of the tax domicile of the taxpayer outside France also results in the end of the deferment of taxation provided for in Article 150-0 B of the CGI and the recognition of a unrealized capital gain calculated on the basis of the purchase price of the securities whose capital gain had been suspended. A taxpayer whose taxable capital gain is taxable as a result of the transfer of his tax domicile outside France may also benefit from the deferment of automatic payment on account of this capital gain.

It should be noted that the Amending Finance Law for 2016 (Law n° 2016-1918, Dec. 29th 2016) applicable to transfers since January 1st 2016 has specified the procedures for determining the applicable tax rate for the income tax (in application of CGI, Article 150-0 B ter) in order to bring the exit tax rules into line with the rules governing the taxation of capital gains in deferral in domestic law.

However, the income tax rate applicable to capital gains realized since January 1st 2013 is no longer determined according to the rules applicable on the day of the transfer of residence but on the basis of the ones applicable at the date of the contribution of shares: it corresponds to the marginal tax rate at which these capital gains would have been taxed if they had been imposed in the year of contribution in accordance with the provisions of Article 200 A 2b of the GTC.

• **Contribution of securities after relocation.** - In the case of transfers prior to January 1st 2014, the contribution of securities subsequent to the transfer to a company controlled by the contributor within the meaning of Article 150-0 B ter of the GTC constituted an event terminating the deferment.

Henceforth, the deferment of payment provided for by Article 167a of the GTC is not questioned when the contribution of securities subject to exit tax falls within the scope of the tax deferral system of Article 150-0 B ter of the GTC or suspended by Article 150-0 B of the GTC.

In practice :

The taxpayer will report the contribution in the annual follow-up declaration ("*déclaration annuelle de suivi*"). For example, regarding the follow-up status of 2015, for a transfer of residence in 2014, the taxpayer would fill in box 0 of form 2074-ETS3, indicating the characteristics of the contribution operation: date and nature of the transaction, number of securities contributed and received, total value of securities received.

In this case, the transfer of securities is an inter-bank transaction, and the 15-year period at the end of which the exit tax is terminated is continued at the level of securities received at the exchange.

Example:

By way of illustration: The same taxpayer transfers his tax domicile to Luxembourg while he holds securities held in company A for a unit value of 101 and then brings his A's securities to a holding company subject to corporate tax in France that he controls (B) for a value of 151.

- **When leaving France**, the taxpayer must declare unrealized capital gains on securities A (capital gain equal to 100) and assess the income tax and social security contributions due for this capital gain, before automatically obtaining a deferment of payment.

- **After settling in Luxembourg**, the taxpayer contributes its A securities to its holding B. This contribution does not lead to the end of the deferment of payment in France in proportion to the tax due on the securities contributed, i.e. the tax due on the capital gain of 100: this mechanism makes it possible to defer to obligations B the obligations linked to the maintenance of the suspension of payment.

In addition, reference should be made to the rules governing the taxation of capital gains in Luxembourg in order to determine the tax treatment of the additional capital gain of 50 on A securities at the time of such contribution.

3. Relocation outside the European Union

A taxpayer who transfers his or her tax domicile to a state outside the EU, Iceland and Norway may be granted an optional tax deferment.

In order to exercise this option, he must send form 2074-ETD no later than 30 days before the date of the transfer of his tax domicile outside France, accompanied by a proposal for guarantees in the service of private non-residents individuals, and the appointment of a tax representative established in France authorized to receive communications relating to tax assessment, collection and litigation. The amount of the guarantees must be equal to 30% of the total amount of capital gains and receivables. However, the amount of the guarantees relating to the tax on capital gains deferred in accordance with Article 150-0 B ter of the CGI after 1 January 2013 shall be determined by application of the rate mentioned in Article 200 A 2 ter of the CGI.

Example:

By way of illustration: the same taxpayer decides to transfer his tax domicile to Singapore on 1 March 2017. He will have to offer guarantees for an amount equal to 30 (i.e. 30% of the amount of the capital gain equal to 100) not later than January 30th 2017, in the service of non-resident individuals if he wishes to apply for the deferment of payment. Those guarantees can take the form of a pledge of securities. The amount of guarantees proposed at this stage should not take into account the tax due but only the value of the unrealized capital gain on the transferred assets.

The taxpayer must enter on Form 2074-ETD the amount of the unrealized capital gains, the amount of tax corresponding to these capital gains and the calculation of that tax. In addition, he expressly mentions his intention to benefit from the deferment of payment on option. In this case, the taxpayer must appoint a tax representative in France who undertakes to carry out all the formalities required of him.

The taxpayer must then file the same 2074-ETD declaration that was filed before his departure within the same period as the taxpayers who transfer their residence in the European Economic Area (EEA) i(n N + 1), to the Tax Service of Individuals ("*Service des impôts des particuliers*") on which his domicile

in France depended before his transfer, along with with his income tax declaration n° 2042, stating that it is a "second filing in the case of an optional deferment".

In the month following the receipt of the tax assessment issued in respect of the tax on unrealized capital gains, the taxpayer shall, if necessary, provide additional guarantees for the recovery of the tax, or demands the restitution of the difference between the amount of the guarantees constituted and that of the tax thus calculated.

Example:

By way of illustration: the notice received by the taxpayer in September 2017 may indicate an amount of tax deferred differently from the amount of the guarantees granted by the taxpayer prior to his departure.

- **If the income tax is equal to 17:** if the amount of the tax is less than the proposed guarantees, the taxpayer may claim part of the guarantees offered up to 13 (= 17-30).

- **However, if the tax calculated by the Administration is equal to 40:** the taxpayer will have to constitute a supplement of guarantees for a value of 10 (= 40-30).

In subsequent years, and for the duration of the deferment of payment, the taxpayer will have to file a 2074-ETS return to the Tax Service of non-resident Individuals to track its taxation. It should be noted that each year, different versions of this form are published by the tax authorities, depending on the year of transfer of the taxpayer's fiscal domicile.

However, the creation of guarantees is not required if the taxpayer justifies the transfer for professional reasons and if the State not party to the EEA Agreement has concluded with France an administrative assistance agreement to fight fraud and tax evasion and a mutual assistance agreement on tax collection, with a scope similar to that laid down in Council Directive 2010/24/EU of March 16th 2010 concerning the mutual assistance in the collection of receivables relating to taxes, duties and other measures.

Thus, this requirement is one of the issues involved in the negotiation of new versions of tax treaties. Practitioners have thus regretted the absence of a recovery assistance clause in the new version of the tax treaty concluded between France and Singapore signed on January 15th 2015.

In practice : In the event of a transfer for professional reasons in one of the States complying with this condition, the taxpayer must provide in support of his application for deferment of payment on declaration No 2074-ETD a document attesting his change of professional activity, his location and the date of the start of the activity (form 2074-ETD-NOT, transfers in 2015, III.B).

Once the taxpayer makes a second transfer, which results in a repatriation of his tax residence within the EU or the EEA, the deferment of payment of duty replaces the suspension of payment on option. The taxpayer may therefore request the guarantee-release to the Tax Service of non-resident Individuals.

Nicolas BRAHIN

Avocat au Barreau de Nice

nicolas.brahin@brahin-avocats.com