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Accountants and Consultants

Subject:

French Tax Authorities Issue Guidelines Regarding Rules for Group Tax Regime

July 2007

International Tax Alert

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Newly issued guidelines by the French tax authorities offer clarification on provisions of the modified 2005 Finance Law and 2006 Finance Law, which express their position on three important points of the French fiscal unity (group tax) regime established under the French Tax Code.

Date/Timing

Effective immediately.

Affecting

All taxpayers doing business in France under the group tax regime.

Summary

The tax deduction of the expenses (including interest) which are incurred in funding the acquisition price of shares acquired when a member of a French tax-consolidated group purchases the shares of another French company that will also become a group member from a shareholder that is not a group member but that controls the group, or from a company that is controlled by the same shareholder, is limited at the group level. This limitation will also apply when the target is not a group member per se, but is merged into a group member or into a company that will later become a group member. For acquisitions taking place during financial years beginning January 2007, the duration of the limitation on the tax deduction is reduced from 14 years to 9 years (the current year and the following 8 years).

The French tax authorities also refined the definition of control, stating that control may be exercised by two or more shareholders if they act jointly to de facto make the decisions in the shareholders' meetings of the company they are controlling.

The guidance also commented on certain intragroup transactions. Intragroup restructuring in many situations should have no immediate impact on the tax status of the group. For instance, the fact that a

company is absorbed by another group member under a simplified merger procedure will not trigger the tax consequences of an exit from the tax group. Further, such internal restructurings will not be treated as an exit from the tax group of either the grantor or the grantee, and therefore will not interrupt the five-year period at the end of which a previously neutralized intra group forgiveness of debt or subsidy may be tax exempt.

In addition to the above, the guidance confirmed the French tax authorities' position that under the parent-subsidiary regime, up to 5 percent of the dividends paid by a group member to another group member during the first tax-consolidated year are taxable at the group level because they related to income earned before entry into the tax-consolidated group.

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