Fiscalimmo News
News & Insights
For Real Estate Tax

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Tax news for the end of 2015

Now, at the beginning of the year, we thought it would be helpful to highlight some of the major events over the past year concerning real estate taxation.

Obviously, ours is a subjective choice, but we hope that this newsletter will provide you with information that is relevant to your activity.

1/ Taxation of real estate transactions: a double blow that may well affect values

As of 1 January 2016, the taxation of real estate transactions in the Paris region is being significantly increased for many assets, with offices and commercial premises located in Paris particularly affected (an increase of 26%, i.e. from 5.09% to 6.41%).

Creation of a tax in addition to the taxes on transfers for valuable consideration on disposals of premises for professional use in the Ile-de-France (IDF) region

Article 50 of the amended Finance Law for 2015 created a tax for the IDF region in addition to the registration duties (*taxe de publicité foncière, TPF*) on transfers for valuable consideration of premises for used for office, commercial or storage purposes completed over 5 years previously.

This increase in the taxation of real estate transactions was justified by the desire to compensate for the loss of receipts in the IDF region arising from the reform of the charge on the creation of offices, commercial businesses and warehouses (see below).

The tax is charged at a rate of 0.6% and applies to transactions and transfers concluded as from 1 January 2016. No transitional measures are planned.

Transfers of residential premises and premises completed within the last 5 years are not affected.

The drafting of the text means that uncertainties remain as regards operations involving transfers for valuable consideration at the reduced tax rate, such as “sale and lease-back” operations (article 1594 F *quinquies*, H, of the French Tax Code (FTC)) and acquisitions with an undertaking to resell under article 1115 of the Code. Such operations would appear to fall under this new tax.

Thus, as of 1 January 2016, transfers subject to this additional charge will face an overall tax rate of around 6.41%.

The tax breaks down as follows:

- Departmental levy: 4.5%
- Communal levy: 1.2%
- Assessment and recovery charges: 2.37% of the departmental levy
- New tax: 0.6%

Increase of the registration duties applicable to Paris

As regards the departmental levy, since 1 March 2014 departmental councils have been permitted to charge a rate of 4.5% instead of 3.8%. Whereas, as of 1 June 2015, Paris was one of the rare departments to have maintained the rate of 3.8%, in November 2015 the Paris City Council voted for a rise in the transfer taxes.

◊**As from 1 January 2016 the rate of transfer taxes in Paris is now 4.5%.**

		IDF	Rest of France
New property (all uses)	Vendor subject to tax	0.715%	0.715%
Property completed over 5 years previously	Premised used for office, commercial or storage purposes	6.41%	5.81 or 5.09%
	Premises used for residential purposes	5.81%	5.81 or 5.09%
	Special acquisition method at reduced rate (sale and lease-back, purchase-resale)	1.32%	0.715%

**Rate applicable to those departments that still charge the departmental levy at 3.8%: Indre, Isère, Mayenne, Morbihan, Martinique and Mayotte.*

2/ Levy on creation of offices, commercial and storage premises in IDF ("RCBCE"): impact of the reform

Prior to the amended Finance Law of 2015, the levy on creating office, commercial and storage premises (*redevance pour création de bureaux, commerces et entrepôts,* RCBCE) did not achieve its desired aim of a territorial distribution promoting businesses and tertiary employment. Under the Prime Minister's directions issued at the Greater Paris inter-ministerial committee of April 2015, the reform of the RCBCE aims to strengthen project dynamics and contribute more to both territorial rebalancing and the development of mixed projects combining dwellings and employment. With this in mind a new division was implemented (except for warehousing facilities) and rates revised to assist territorial rebalancing (reduced rates for offices in zones 2 and 3, limited increase in zone 1).

In some cases of change of circumscription, a transitional mechanism applies between 2016 and 2018 (mechanism partly taking up the previous transitional mechanism).

Summary table of rates per square metre (2016)

	1st zone: Paris and Hauts-de-Seine	2nd zone: municipalities in Greater Paris metropolis	3rd zone: municipalities in Paris conurbation	4th zone: other municipalities in IDF region
Office premises	€400	€90	€50	€0
Commercial premises	€129	€80	€32	€0
Storage premises	€14	€14	€14	€14

Rates before reform (2015)

	1st zone: Paris and Hauts-de-Seine	2nd zone: municipalities in Paris conurbation	3rd zone: other municipalities in IDF region
Office premises	€368.95	€229.52	€92.24
Commercial premises	€128.71	€80.44	€32.18
Storage premises	€13.95	€13.95	€13.95

The provisions regarding the base of the levy (which is henceforth deemed a tax), its field of application and exemptions remain overall unchanged. Nonetheless, if there's no town-planning permit, the operative event is the beginning of the construction or the change of use.

It should be noted that the tax is now capped at a maximum (it may not exceed 30% of the portion of the cost of the operation ascribable to the acquisition and improvement of the construction surface).

◊**In conclusion**, except for office buildings in zones 2 & 3, this reform does not really reduce the rate of the tax compared to the previous situation and once again risks causing uncertainty, in particular as regards the functioning of the “cap” mechanism.

The limitation period that was of 2 years added to the on-going year in presence of a town-planning permit has been raised to 6 years in every case (this period used to apply only when there was no permit).

3/ Disposal of real estate: application of article 257 bis FTC

Summary:
Article 257 *bis* of the FTC (implementing a European directive) aims to simplify the application of VAT to certain transfers of a “business” (transfers of all or part of the totality of assets) that would generate turnover liable to VAT. The article may in certain cases apply to sales of real estate. However, while its desired aim of simplification has merit, its application to real estate sales is not so simple in practice, as it is not obvious when its conditions of application will be met. While the French Tax Authority, FTA, regularly makes written statements in this respect aimed at safeguarding transactions, it very seldom publishes them, meaning that a certain vagueness continues to affect the regime: precedents are thus of great importance in this matter.

In two rulings of November 2015 (CE 23-11-2015 nos. 375054 and 375055), the Conseil d'Etat confirmed that a building assigned to rental activity may constitute a totality of assets, whether total or partial, within the meaning of article 257 bis of the FTC, even where a financial lease exists.

A brief summary of the facts is essential for a better understanding of the impact of the Conseil d'Etat’s decision.

A French SCI (real estate Investment Company) rented commercial premises under a financial lease. It sublet the buildings to an enterprise that carried on its business there. Soon after having bought the commercial fittings from the occupier, the SCI acquired the building by exercising its option to buy under the property lease.

On the same day, the SCI resold the building and the fittings to a third party, with the occupier remaining

as tenant. The parties opted to subject neither the exercise of the option nor the subsequent disposal to VAT.

The FTA did not dispute the non-taxation of the disposal, but demanded repayment of a proportion of the VAT deducted upon acquisition of the commercial fittings, which had been posted as a fixed asset by the SCI.

While the administrative court first instance of Strasbourg ruled in favour of the taxpayer, the administrative court of appeal of Nancy overruled this decision and, in two judgments of 21 November 2013, confirmed the settlement demanded by the FTA.

The Conseil d'Etat overturned this view, holding that exemption from VAT "*applies to all transfers of businesses or of an autonomous part of an enterprise where the beneficial owner of the transfer intends to carry on the business or the part of the enterprise transferred in this way rather than simply liquidating the activity concerned immediately*".

In its decision the Conseil d'Etat of State implicitly confirms two points as regards the general scope of article 257 bis of the FTC.

As mentioned above, a property used for rental activity may well constitute a totality of assets (whether total or partial) pursuant to article 257 bis FTC.

In addition, if the conditions for the application of this article are met, it will not only make neutral those operations that would have been taxed (the article removes the tax charge) but will also make neutral those that would have been exempt. In this case, article 257 bis will exempt the person making the disposal from any repayment of VAT previously deducted.

◊**The application of article 257 bis FTC is thus "doubly" possible where the option to buy is exercised followed by an immediate resale of the property.**

4/ Property dealers – the problem of VAT "carry"

According to the tax authorities:

- a company buying a property completed over 5 years ago and posting it as stock may only deduct the VAT on the acquisition if such real estate asset is resold subject to VAT. Such option must be exercised at the time of resale. Only at this point may the property dealer "recover" the VAT paid on acquisition;
- this position remains unchanged even if the property is rented out with the VAT option exercised pending its resale.

The result is that the property dealer has to "carry" the VAT paid on acquisition while at the same time having to collect VAT on the rents from the property during the entire period it is held. As regards the VAT charged on building maintenance works or costs, the FTA intends to make use of a complex exegesis work to link these works or costs either to the rental activity (in which case VAT is deductible) or to the future resale (in which case VAT is only deductible at the time of such resale on the same grounds as VAT on acquisition).

This position, taken during 2014, meant that the tax administration has:

- made numerous tax adjustments for operations where it had previously refunded VAT on acquisition;
- refused to refund such VAT for acquisitions made since the end of 2014.

◊**We must await the decision of the courts on whether or not the FTA's position complies with the VAT directive. An initial case law can be expected in 2016.**

5/ Fourth amendment to Franco-Luxembourg tax convention: an effective application delayed to January 2017

At their sitting on 16 December 2015 the French senate definitively adopted the proposed law authorising approval of the amendment. This single article is aimed at ending the situation whereby capital gains realised by Luxembourg companies on shares in real estate companies holding assets located in France were entirely exempted from tax on account of the contradictory interpretation of the convention by the two countries. This amendment, the result of lengthy negotiations between the two states, now mitigates such total freedom from taxation. As regards its entry into force, Albéric de Montgolfier, general rapporteur of the finance commission, has stated that disposals that were previously totally exempt from taxation may now only be taxed by France as of 1 January 2017. In practical terms, this means that capital gains realised by a Luxembourg company on disposals of shares in a company that mainly owns real estate assets located in France will, for one more year, only be taxable in Luxembourg, where such gains may be exempt.

6/ VAT: management of regulated real estate funds is exempt from VAT

In its ruling of 9 December 2015 (case C - 595/13), the European Court of Justice (ECJ) confirmed that the management of certain real estate investment funds is exempt from VAT.

To qualify for exemption, such funds must have identical characteristics to undertakings for collective investment in transferable securities (UCITS) and carry out the same transactions or, at least, display features that are sufficiently comparable for them to be regarded as being in competition with such undertakings (consideration 39). In particular, the member state concerned must have subjected such companies to specific official monitoring. In addition, to be exempt, the management services must be specific to the activity of the fund. Such exempt management operations will thus include activities related to the acquisition and disposal of real estate assets and to administration and accounting tasks, even where these are provided by a third party.

In practice, the point in question is whether fees invoiced to SCPIs [real estate investment trusts] (especially OPCIs [*pooled real estate investment vehicles*]) by management companies will be exempt from VAT. This question mainly affects OPCIs that only hold real estate assets through subsidiaries, rather than directly (the most widespread situation). With no turnover liable to VAT, the OPCI cannot deduct the VAT invoiced to it. The non-application of VAT to management costs will thus reduce the overall cost to the OPCI by 20%.

However, this VAT exemption has a corollary, namely that the management company is now subject to payroll tax and may not reclaim VAT on its own outgoings.

Since French law permits management companies to opt for payment of VAT on their management services, which must be carefully analysed – in particular together with clients, where necessary – in order to determine the best overall path to choose (whether services should or should not be subject to VAT, i.e. opting for the application of VAT to management services).

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