

Hot Topic

Update on major accounting
and auditing activities



French business tax reform

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Summary

The French Finance Bill for 2010 and the Amended Finance Bill for 2009 were enacted on 31 December 2009. Among other things, the Finance Bill for 2010 includes a provision for a tax on Business Contribution on the Added Value (BCAV). BCAV is a progressive tax that is substantially based on an entity's margin. Because the tax on BCAV is based substantially on an entity's income, we believe the tax on BCAV is subject to ASC Topic 740, *Income Taxes*. As such, the financial statement effects of the change in tax law with respect to BCAV (including deferred tax effects) should be included in continuing operations in the period of enactment of the law (i.e., the fourth quarter for a calendar year end entity).

Summary of tax law change

On 31 December 2009, the French parliament enacted the French Finance Bill for 2010 (the Finance Bill) and the Amended Finance Bill for 2009. [[link to International Tax Alert 2010-25](#); [SCORE no. CM1783](#)] The Finance Bill, among other provisions, repeals, as of 1 January 2010, the local business tax (Taxe Professionnelle) on tangible assets (i.e., real property, equipment and movable

assets) and replaces it with the Territorial Economic Contribution (TEC). The TEC consists of two different taxes: the Business Contribution on Property (BCP) (or Cotisation Fonciere des Entreprises (CFE)), and the Business Contribution on the Added Value (BCAV) (or Cotisation sur la Valeur Ajoutée des Entreprises, (CVAE)).

The BCP is computed based only on the rental value of real property. In a change from the former business tax, the BCP does not tax equipment and movable assets. The tax on industrial buildings is calculated using a reduced rental value.

The BCAV is a progressive tax that can be as high as 1.5% of the added value as defined by the Finance Bill. Generally, added value represents the difference between revenue (or turnover) and expense, as those two components are defined by the Finance Bill.

The Finance Bill defines "turnover"¹ as the total of certain specific revenue items (i.e., sales of goods and services, royalties and license fees). While proceeds from sales

¹ The Finance Bill definition for turnover applies to businesses in general and excludes banks, insurance companies, and certain investment companies, that are subject to specific rules.

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of assets representing normal and usual activities of the business are included in turnover, asset sales that do not meet that definition are not subject to BCAV. In addition to turnover, other specific revenue items are included in added value (i.e., current operating income, operating grants and income from cancellation of financial debt). The expense component of added value includes the cost of raw materials, supplies, equipment and goods for resale, in addition to other defined terms including cost of services, certain taxes and other operating expenses. Depreciation expense for assets other than certain leased or subleased tangible fixed assets is not included in the calculation of added value.

The highest tax rate (1.5%) applies if the turnover of the French taxpayer is higher than €50m. Lower rates apply for taxpayers with turnover below €50m. Additionally, the added value is capped at 80% of turnover, as defined, for taxpayers with turnover that does not exceed €7.6 million and at 85% of turnover, as defined, for taxpayers with turnover that exceeds €7.6 million. The TEC (or the sum of the BCP and BCAV) also is capped at 3% of the added value, as defined. The amount by which the total calculated TEC exceeds the cap may be used to reduce the BCP, but the BCAV is not subject to reduction.

The TEC is deductible from the French corporate income tax (Impôt sur les Sociétés).

Application of income tax accounting

The BCP is considered a tax on property and is considered an operating expense. This component of the TEC is not computed based on income and therefore is not within the scope of ASC Topic 740, *Income Taxes*.

BCAV is calculated based on turnover, as defined, which approximates an entity's margin. As discussed in T5, *Recognition and Measurement*, of our Financial reporting development booklet, *Accounting for Income Taxes*, we believe that similar taxes while based on an entity's margins, are nonetheless a tax based substantially on income and are within the scope of ASC 740. As such, we believe the BCAV is subject to the provisions of ASC 740. Accordingly, the signing into law of the Finance Bill and the Amended Finance Bill of 2009 represents a change in tax law with respect to the tax on BCAV and the corresponding financial statement effect of tax on the BCAV should be recognized in continuing operations in the period the law is enacted (i.e., 31 December 2009), despite an effective date of 1 January 2010.

As previously discussed, depreciation is not generally deductible for purposes of determining the BCAV, and gains on asset sales that are not considered normal and usual activities of the business also are not generally subject to BCAV. As such, the tax base for an asset that is not subject to BCAV is zero. The resulting deferred tax liability should be measured using an effective tax rate of zero as the temporary difference is never subject to BCAV.

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