



## INTERSOL 2013

# Contaminated Lands: What legal and tax optimization to choose ?

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# Contaminated lands : what optimization to choose ?



## Introducing

- 250 000 contaminated lands registered in France
- 4 186 potentially polluted for which Government authorities consider that remedial actions has to be carried out
- Most territories concerned : Nord Pas-de-Calais, Lorraine, Alsace, IDF, Vallée du Rhône
- Brownfields: what interest and what purpose ?

# Contaminated lands : what optimization to choose ?



## Introducing

- A contaminated land is :
  - First of all: the liability of the former « operator » after decommissioning the site
  - Is an opportunity for real estate actors (investors, property developers, private/public planners, ...) who are searching for land resources
  - Has a negative value which must be taken into account and considered as a financial stake in the course of the sale/acquisition transactions

# Contaminated lands : what optimization to choose ?



## Introducing

- In the 1990's : first legal official guidelines (*circulaires*) about the management of contaminated lands in France + complete inventory with BRGM (knowledge on existing contaminated lands treated or not)
- 2007 : former technical tools (ESR/EDR) are deleted. Clarification has been done with a new approach depending on the risk. This is confirmed by new guidelines dated 8th February 2007 - new tools (IEM, “plan de gestion”)
- However, legal approach is complex in France, mixing technical guidelines and many layers in legal regulations

# Contaminated lands : what optimization to choose ?



## Key issues

- I. Reminder of contaminated lands legal foundations
- II. Good practices to reinforce the security of the deals
- III. Tax optimization

# I. Legal foundations of contaminated lands regulations



## 1. Key notions

- **”Pollution”**: a relative notion with a relative meaning, no legal definition (see Guidelines of 8th February 2007)
  - The “true pollution” can not exist without a risk for human health and environment (individual approach)
- **Risk of human health damage**: assessed through the equation “source / vehicle / target”
  - Ways of exposures and contact time period are analyzed
- **Use**: technical meaning vs legal and contractual meanings
- **Decontamination**: from myth to reality

# I. Legal foundations of contaminated lands regulations



## 2. State of regulations: combination of rules focusing on collective / public interests

- Several legal obligation involving actions from local/national the government authorities
- What purpose ?
  - protecting environment, human health, natural resources, etc. and not to regulate private relations (except obligation of information : L514-20 Code env. extended with L125-7. See below)
- What consequences for private interests ?
  - ✓ breach of legal rules can raise civil liabilities (1382 of French Civil Code)
  - ✓ specific agreements must be considered as a compensation

# I. Legal foundations of contaminated lands regulations



## 3. Legal basis of the obligation of remediation works

- Under Classified Installations for the Protection of the Environment (ICPE) : the former operator is required to carry out remedial actions at the end of the business (or during the business eventually)
  - Under waste law: obligation of the waste producer / waste holder to manage, treat and eliminate excavated soils and materials
    - “*land (in situ) including unexcavated contaminated soil and buildings permanently connected with land*” do not fall under the scope of waste law
- ➡
- possibility of valorization on-site and off-site
  - be careful of the liability of “careless” land owner



# I. Legal foundations of contaminated lands regulations



- Under environmental liability law with regard to the prevention and remedying of environmental damage: obligation, for the economic operators, to prevent/remediate of environment damage risks with introduction of materials in the soils or sub-soils, waters and groundwater (“big” damages)
- Under water resource law : obligation of the responsible person or, if defecting, the land owner to inform the government authorities and to carry out remedial actions

# I. Legal foundations of contaminated lands regulations



- Under Town Planning regulations:
  - Urban planning scale : local authorities (town) has the responsibility to integrate in their planning documents (SCOT, PLU et *cartes communales*) all the conditions ensuring compatibility between every kind of pollutions and uses of lands
  - Operating scale (building or developing authorizations) : the mayor has the possibility to restrain or forbid occupations and activities with fragile populations
- Under technical guidelines: risk approach, Guidelines of 8th February 2007 (official guidelines of contaminated lands management)

# I. Legal foundations of contaminated lands regulations



## 4. Identification of the liabilities: the hard way about clarifying situations ?

- Depending on the legal basis, the “obligation of decontamination” concerns a large scope of persons who are liable
  
- Practical difficulties:
  - The multiplicity of former operators and activities,
  - Works / moving soils,
  - Insolvency or disappearing of the responsible,
  - Scientific proof of a direct link between activities / former operators / pollutions,
  - limits of the decontamination obligation (time and content)

# I. Legal foundations of contaminated lands regulations



## 5. Contract: the only way to deal with the gaps in the law

- Articulation between legal obligations and purchase/acquisition agreement
- Prevention of the risk of one's liability being called in respect of clean-up of sites
- Two key elements to be included:
  - ✓ agreements are not binding on government authorities (*Préfet* and *DREAL*)
  - ✓ whatever the form of the contract (deed of sale/real estate, real estate lease-back, LBO, reps & warranties, services agreement, ...): the rule of the game is the agreement itself taking into account the role of each actor (former operator, seller, ...)

# I. Legal foundations of contaminated lands regulations



## 6. The new information of the third parties

- Project of decree about the obligation of information of third parties about a risk of soil pollution

As a reminder, the Grenelle 2 Act of 12 July 2010:

**Art. L125-6 Code env.:**

*« L'Etat rend publiques les informations dont il dispose sur les risques de pollution des sols. Ces informations sont prises en compte dans les documents d'urbanisme lors de leur élaboration et de leur révision ».*

**Art. L125-7, alinéa 1<sup>er</sup> Code env.:**

*« Sauf dans les cas où trouve à s'appliquer l'article L514-20, lorsque les informations rendues publiques en application de l'article L125-6 font état d'un risque de pollution des sols affectant un terrain faisant l'objet d'une transaction, le vendeur ou le bailleur du terrain est tenu d'en informer par écrit l'acquéreur ou le locataire. Il communique les informations rendues publiques par l'Etat, en application du même article L125-6. L'acte de vente ou de location atteste de l'accomplissement de cette formalité ».*

# I. Legal foundations of contaminated lands regulations



## Principles of the draft decree:

- ❑ definition of the risk of soil pollution: site which is likely to be contaminated in relation of former activities and chemical materials that could have an effect (direct or not) on human health and environment, *inter alia* in case of modification of the use of lands
- ❑ requirements of the prefect who will define areas of « **information zones** » (where no risk could be excluded) and « **monitoring zones** » (where binding rules must be followed en the framework of the polluted soils management)

# I. Legal foundations of contaminated lands regulations



- ❑ the prefect requirements inside the “monitoring zone” areas become town planning regulations that must be applied as such rules (documents enclosed to the “*Plan local d’urbanisme*”)
- ❑ Information available on Internet at least on 31 December of 2013 (for “monitoring zones”) and 31 December of 2016 (for “information zones”)
- ❑ the “ERNT” contains such information

# I. Legal foundations of contaminated lands regulations



## □ Miscellaneous

### ➤ A new chapter in the French Environment Code:

in case of modification of the use of lands, remedial action must be carried out to guarantee the compatibility with the future use to protect the human health and environmental

→ **will become a legal rule**

### ➤ in case of works inside a « monitoring zone » : the authorization file would include a certificate of a specialized company in the pollution sector (guarantee that developer has respected the contaminated land guidelines)



# I. Legal foundations of contaminated lands regulations



## 6. Financial guarantees (L516-1 of French Env. Code)

As a reminder

**Decree n° 2012-633 of 3 May 2012**

The scope of financial guarantees is extended to new activities (Act of Ministry of 31 May 2012)

## II. Good practices to reinforce security of the deals



### Key steps :

1. **Inform and be informed** : costly action but necessary
2. **Organize the bases of the negotiation**: identify the project/future use of the site
3. **Searching for financial optimization**: one of the goal of the *modus operandi* of the remediation works
4. **Do not forget the peripheral issues**: relics of industrial activities within the sub-soils, groundwater, etc.
5. **Use restrictions (easements)**: public or private easements are performing solutions and sometimes necessary when decontamination is not possible for all uses

## II. Good practices to reinforce security of the deals



### Illustrations

1. **For the former operator:** the objectives are to comply with legal obligations and to limit his liability in the course of remediation of contaminated lands
  - ❖ Decontamination operations can be carried out by a third party (agreement about the execution of the legal obligations: *modus operandi* for remediation works) like a property developer or a planner
  - ❖ The former operator stay the single interlocutor of the government authorities
  - ❖ The limitation of the liability of operators: what is he able to do and how ?

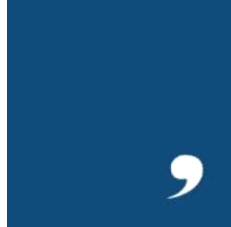
## II. Good practices to reinforce security of the deals



2. **Property developers** : the objectives are to acquire the property and to comply the land with the future use / project of development including additional costs and providing a *modus operandi* of remediation works

- There are many stages in the course of the sale
  - ❖ Preliminary studies/technico-economic feasibility ?
  - ❖ What is the legal regime of the land ?
- Doing a first balance assessment
  - ❖ Could additional costs relating to pollution be appreciate with reliability ?
  - ❖ Is the project feasible ?
- The *modus operandi*

## II. Good practices to reinforce security of the deals



Possible contracts charts:

- ❖ **Remediation works are carried out by the former operator and/or the seller:** the vendor has the obligation to deliver the land for the correct use but the construction works suppose additional costs
- ❖ **Remediation works are carried out by the property developer:** the price is decreased or the cost of remediation works with reimbursed by the seller and/or the former operator

Parties will distinguish:

- Works usually took over by property developers for the project of buildings: earthmoving excavation works, demolition, evacuation of relics in sub-soils, ...)
- Remediation works (deleting all risks for human health and environment) took over by the former operator: property developer could/will participate

## II. Good practices to reinforce security of the deals



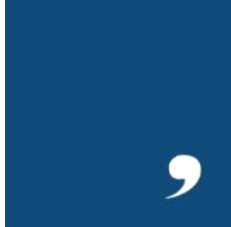
3. **Private and public planners:** the objectives are selling building rights, making the land viable and suitable (provide necessary infrastructure and utilities) with specifications, and avoid all risk or damage for the human health
- The planners are working on larger scales than property developers: they have often insufficient information at the beginning of the ZAC
  - *Modus operandi* with several steps to be included in the course of the execution of the ZAC: how to do so ?
  - Planners is a real estate professional

## II. Good practices to reinforce security of the deals



4. **Corporate mergers & acquisition** : the objectives are to transfer the environmental risks and to limit decreasing of the price
  - Share deal vs Asset deal: what is the difference under the environmental risks ?
  - Transferring the liabilities and the financial risk of remediation works : compensation with reps and warranties
  - Draw up a “baseline report” to establish a state of the soil and groundwater
  - Jurisdiction: common judge or arbitration ?

# III. Tax optimization

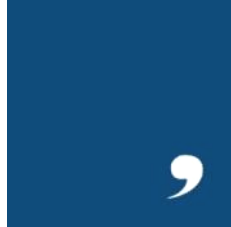


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# Tax news - tax losses (1/2)

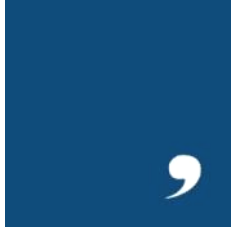


- Summary of the applicable rules as year-end 2012:

Tax losses carry-over	
Fiscal year ending as from 31 Dec 2012	
<b>Loss carry-forward</b>	Indefinite in time, but the loss carry-forward can only offset 50 % of income exceeding 1 m€ *
<b>Loss carry-back</b>	A loss carry-back can only offset income from precedent fiscal year, up to a maximum amount of 1 m€
<b>Restrictions</b>	"Stop loss rules" in case of change of activity Specific limitation for Tax consolidated group (limitation of the use of pre-consolidation losses)

*\* Waiver of debts granted to a French company subject to an insolvency procedure may be added to the 1 m€ franchise*

# Tax news - tax losses (2/2)



- Restricted conditions to be granted a transfer of tax losses in case of restructurations:

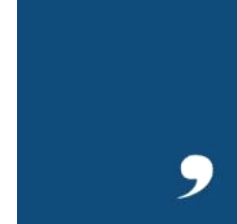
"Stop loss rules" in case of change of activity		
Cases	Definition	Exception
<b>Interruption of activity</b>	i) <b>EITHER</b> disappearance of the production resources needed for the pursuit of activity for more than 12 months	i) " <i>Force majeure</i> " or conditional advance ruling (non tax-driven motives)
	ii) <b>OR</b> same disappearance followed by a disposal of the majority of the company's shares	ii) No exception possible
<b>Significant change of activity</b>	Event triggering, during the fiscal year of the addition or the following fiscal year:	
i) <u>Addition of a new activity</u>	i) <u>An increase of more than 50% of:</u> - <b>EITHER</b> the company's turnover; - <b>OR</b> the average number of employees and the value of the company's fixed assets	i) and ii) upon advance ruling when such action is essential for the continuing of the prior business activity that generated the tax losses and for maintaining employees in their job.
ii) <u>Termination / transfer of an activity</u>	ii) <u>A decrease of more than 50% of :</u> - <b>EITHER</b> the company's turnover; - <b>OR</b> the average number of employees and the value of the company's fixed assets	

# Tax news - financial debt waiver



- Creation of a non-deductibility principle of all financial debt waiver
  - ✓ The deductibility of the financial debt waiver is restricted to businesses in difficulty, i.e., in an insolvency procedure (or in so-called « *sauvegarde* » or « *conciliation* » procedures).
  - ✓ Other financial debt waivers are not deductible anymore.
  - ✓ The financial debt waiver remains taxable at the beneficiary's level.
  - ✓ Commercial debt waivers granted in normal conditions remain deductible.
  
- ➔ *The financing of companies in difficulty will have to be reviewed, especially within groups. The financing may occur through the financing of operational activities.*

# Tax news - Deductibility of the capital loss on the sale of shares of a company that benefited from a contribution in kind



- Is it required to proceed to an evaluation of the shares of a loss-making subsidiary before conducting a contribution in kind ?
- ✓ In the past, when the net asset value of the subsidiary was negative, a contribution in kind was more tax-optimal than a debt waiver should the parent company had the project to sell the subsidiary on a short-term basis (the contribution was not taxable at the subsidiary's level and the parent company could deduct the short-term capital loss.
- ✓ Concerning sales occurring starting on July 19th 2012, the short-term capital loss will not fully be deductible. The part of the capital loss corresponding to the difference between the book value of the received contributions (i.e. the nominal value of the shares) and their fair market value at their emission date.
- ✓ *Example : A Parent company A proceeds to a contribution in kind of 200.000€ to its subsidiary B which has a negative net worth of 150.000€ prior to the contribution in kind. The shares received by A are booked for 200.000 in the accounts of A. A sells the shares in B the year following the contribution in kind for 40.000 € and generates an accounting capital loss of 160.000 € (i.e. 40.000 - 200.000 €). This capital loss was prior to the tax reform of 2012 entirely deductible: it is now deductible only up to 150.000 € (i.e. the difference between the book value of the shares - 200.000 € - and their fair market value at their emission date - 50.000 €).*

# Tax news - Interest deduction limitation rules



- ✓ A general interest deduction limitation rule applies when the remuneration of shareholders's current accounts is higher than a rate published by the government.
- ✓ A specific thin cap rules applies between associated companies.
- ✓ Starting in 2013, a general interest limitation deduction applies. Applicable in FY 2013, the new limitation provides that 85% of the net financial expenses (with an application threshold of 3m€) will not be deductible. This rate of 85% will be lowered to 75% in 2014.
- ➔ Industrial companies at the end of life of their industrial establishments may easily be subject to the application of thin cap rules

# Scenarios



- ❖ Scenario 1: « *Dismantlement of an industrial establishment* »
  
- ❖ Scenario 2: « *Conversion of an industrial brownfield into residential units* »

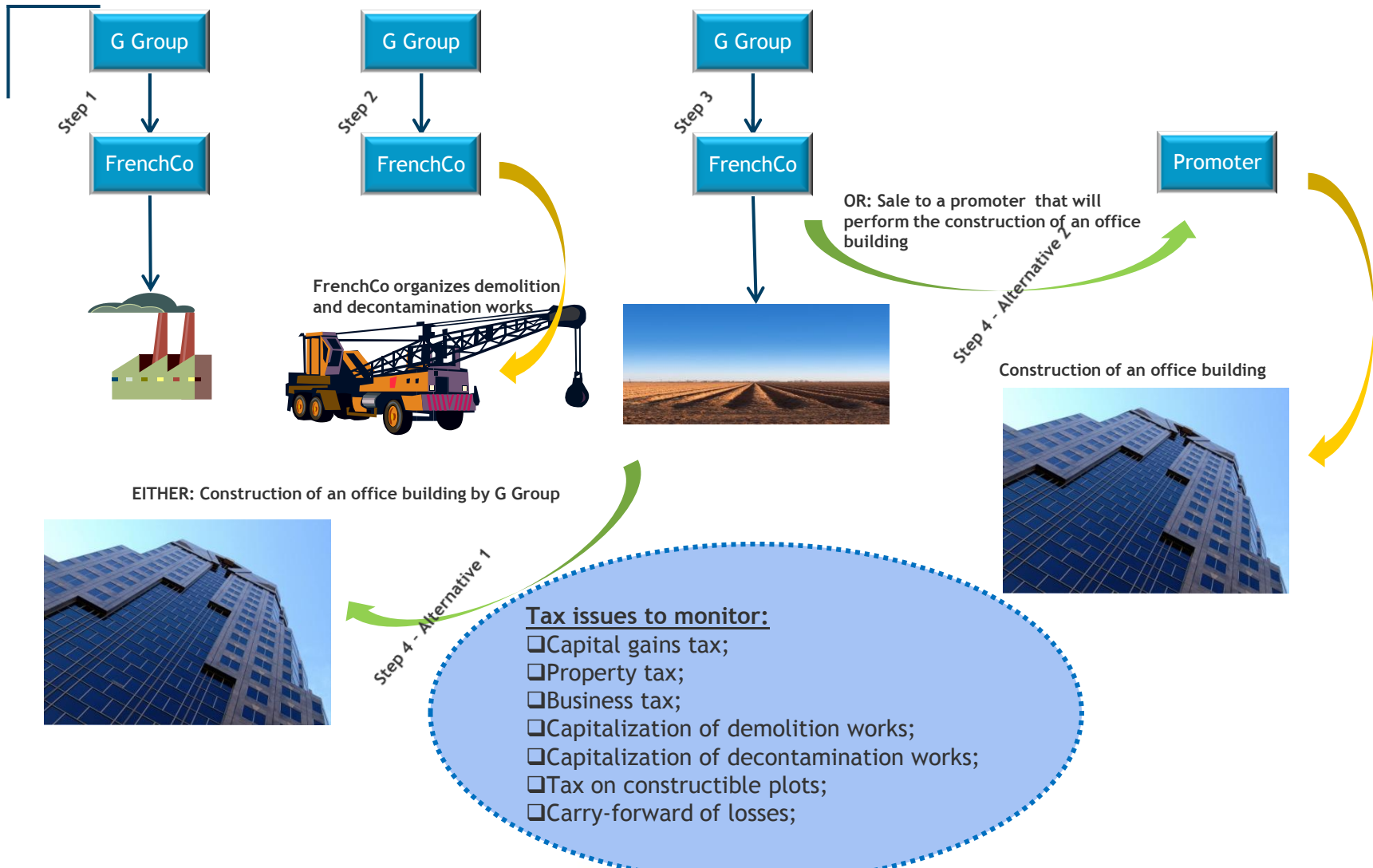
# Scenario 1 - Presentation



## ❖ Scenario 1: « *Dismantlement of an industrial establishment* »

- Company A runs an industrial establishment in its final phase.
- Company A has numerous tax losses.
- Significant dismantlement works have to be performed.
- The plot of land on which the industrial establishment is located is contaminated and will not be used for the construction of housing purposes in the future.
- The industrial establishment is not located within or near an urban zone.

# Scenario 1 - Charts





# Scenario 1 - Issues



## ❖ Tax issues:

- Securing the tax losses generated by the company's industrial establishment;
- Piloting between losses creation and diminution of the taxable capital gain relating to the sale of the building land;
- Deductibility of VAT relating to demolition and decontamination works;
- Qualification of the demolition expenses:
  - Tax-deductible expense;
  - To be comprised in the cost price of the building to be built;
  - To be comprised in the cost price of the building land;
- Optimization of the tax burden regarding local taxes (property tax and business tax);

# Scenario 1- Optimization of the tax losses management



➤ Reminder:

- ❑ The termination of a business's activity generates in theory the definitive loss of the available tax losses;
  - ❑ The activity that generated the losses should not have been subject **to significant changes** during the period following the generation of losses regarding the customers, number of employees, means of exploitation, nature and extent of the activity volume. Also, after the restructuration, the activity should have been pursued during three years without having been subject to significant changes.
- An industrial activity that will be dismantled often generated important tax losses. The transfer of activity to another company through a merger or a contribution in kind will only generate the transfer of the tax losses if the French tax administration (hereinafter "FTA") considers that all legal requirements are met in order for the transfer of the tax losses to occur (Approval procedure - Article 209-II French Tax Code).

# Scenario 1 - Tax optimization of the decontamination financing (1/2)



- ❖ Deductibility of the VAT relating to demolition and decontamination works (Administrative high Court December 30th , n° 319835, 8<sup>e</sup> et 3<sup>e</sup> s.-s., min. c/Sté Rhodia-Chimie):
  - **Principle:** The input VAT relating to a VAT-taxable operation is deductible from the output VAT.
  - The consequence from this principle is that VAT relating to expenses linked with a VAT-taxable activity but that are paid after the termination of a business's activity may, unless the claim is abusive or fraudulent, be reimbursed to a VAT-taxable person if a direct and immediate link exists between these expenses and the activity that was formerly conducted.
  - The person operating an industrial establishment may in theory deduct the VAT linked to demolition and decontamination works.
  - In addition, the sale of shares is a VAT -exempted operation.
  - If a company A operating an industrial establishment is sold by its shareholder B and if it is agreed between the parties that the decontamination works are per agreement taken over by B, two alternatives are possible:
    - ❑ A reinvoices to B the costs of the decontamination services which are conducted by third parties: No VAT is due given that no services are conducted between A and B. In addition, the decontamination operation is linked to a VAT-exempted activity (the sale of shares) given that the decontamination costs were comprised in the acquisition price of subsidiary A;
    - ❑ Third party service providers directly invoice B with VAT: the invoiced VAT is not deductible given that it is not linked with B's activity; A was indeed the company which was legally liable to these works.

# Scenario 1 - Tax optimization of the decontamination financing (2/2)



- ❖ May the transfer of liability of an operating subsidiary to the parent company have an impact on the taxable result?
- It is questionable whether the taking over of the decontamination costs of a company operating an industrial establishment by the parent company is an abnormal act of management (« *acte anormal de gestion* ») (Reminder: this « abnormal act » is non-deductible for tax purposes).
- The last operator of an industrial establishment is legally financially liable for the execution of the decontamination works (Articles L 512-6-1, L-512-7-6 and L-512-12-1 Environment code). In theory, the parent company should not help its subsidiary, given that the obligation to pay the decontamination works lies on the subsidiary.

# Scenario 1 - Tax piloting of the demolition works (1/3)



## ❖ Qualifying the demolition works in a tax-intelligent and tax-optimal way:

- The demolition works that aim transforming property into a building land in order to run it for a profitable activity, are comprised in the cost price of the terrain. The demolition costs linked with the transformation into a building land that will be used for the construction of a new building are to be comprised in the cost price of the new building.
- Demolition costs paid in case of abandonment of an industrial site are to be booked as expenses.
- The demolition costs that aim at getting back the property into an building land in order to resale it, the costs are to be booked in sale costs if the demolition is a requirement of the terrain's sale. However, these costs are comprised in the cost price of the terrain from a tax point of view (CE 14 mai 1975, n°93314; BOI-BIC-CHG-60-20-10-20120912 n°20).

# Scenario 1 - Tax piloting of the demolition works (2/3)



## ❖ Qualifying the demolition works in a tax-intelligent and tax-optimal way:

- Demolition costs and the destruction of constructions may reduce the accounting result and increase the amount of tax losses. These losses are however generated in a context where already a significant amount of tax losses already exists.
- The new rules restrict the possibilities to use the tax losses as well as the possibilities to transfer them, in particular when the transferring company was subject to significant changes of activity.
- In order to secure the offsetting of these losses against the taxable result, it may be preferable in certain situation (existence of numerous tax losses) to include the demolition works as well as the residual value of the constructions in the cost price of the terrain from a tax point of view in order to reduce the taxable capital gain on the terrain's sale.

# Scenario 1 - Tax piloting of the demolition works (3/3)



❖ Qualifying the demolition works in a tax-intelligent and tax-optimal way:

➔ Reducing the latent taxable capital gain is in numerous situations to be preferred to the offsetting of tax losses given that it is less subject to the appreciation of the French tax administration.

# Scenario 1 - Property tax (1/2) (“*taxe foncière*”)



- ❖ Keeping the property tax burden under control
  - Reminder: The old “*taxe professionnelle*”, the new business tax replacing it, and the property tax, are taxes that benefit French local authorities.
  - A general tendency: the replacement of the old « *taxe professionnelle*” with the new business tax generated a decrease of revenue for the French local authorities. In order to compensate this loss, the FTA try to collect more revenue using property tax by broadening the meaning of the term « *fixed assets subject to property tax* ».
- ➔ Consequence from this strategy change: The FTA will try to submit every piece of masonry to property tax.
- ➔ In case of reassessment of the rental value of the property, property tax and a part from the business tax will be impacted: this will increase the tax burden of the companies owning their buildings.



# Scenario 1 - Property tax (2/2) (“*taxe foncière*”)



## ❖ Keeping the property tax burden under control

- ➔ *Optimizing the property tax burden may occur through suppression of the destroyed fixed assets that were qualifiable as constructions and to notify the French tax administration with these changes.*
- ➔ *Another method is to claim back the property tax in case of cessation of operation of the property. This procedure however should be piloted very precisely given the very strict legal requirements.*
- ➔ *It is important to obtain the demolition permit of the buildings in order to reduce the book value of the buildings left to be destroyed;*

# Scenario 1 - Business tax



## ❖ Keeping the business tax burden under control

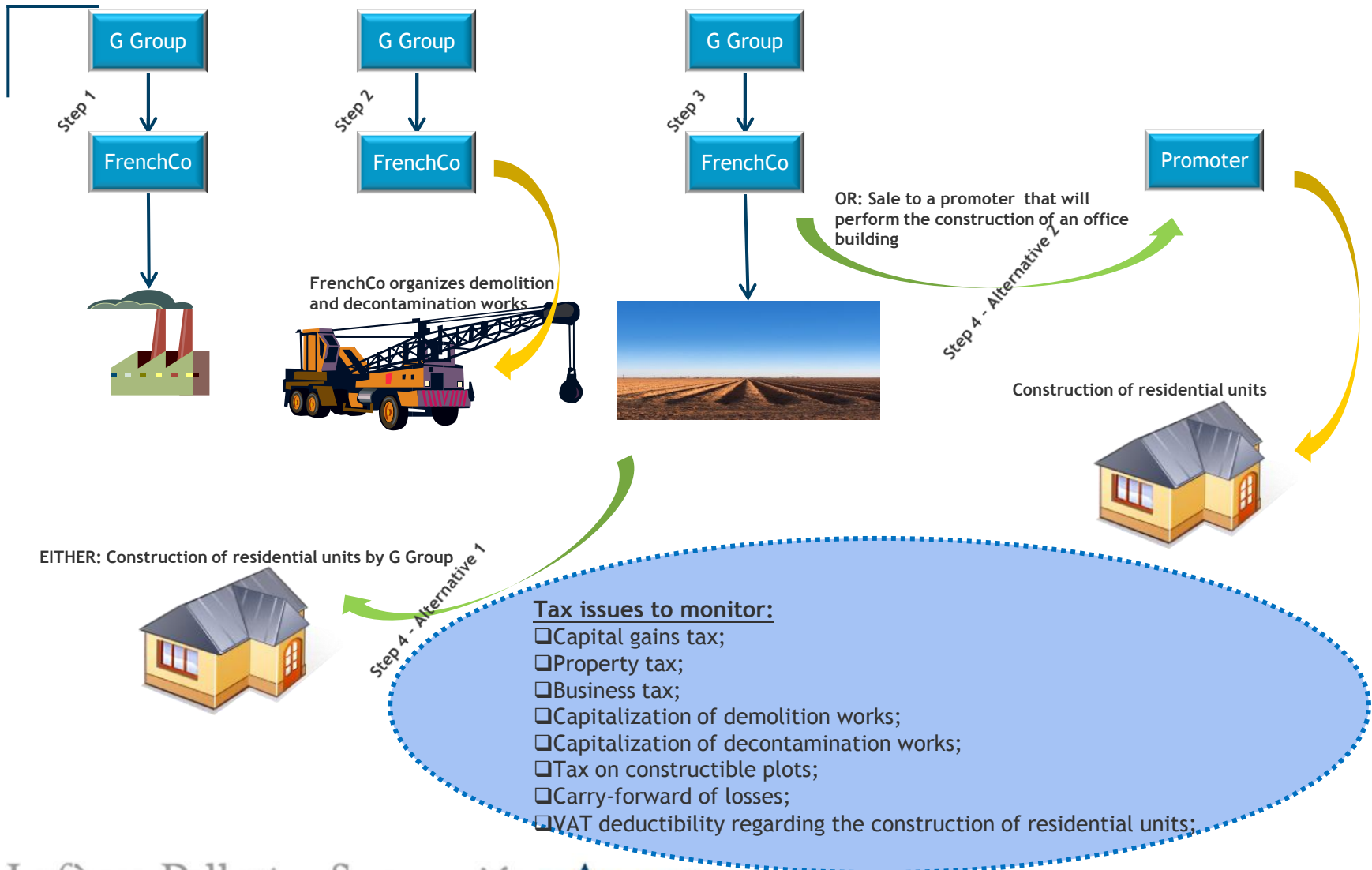
- The business tax is comprised of two different taxes:
  - ❑ The real estate contribution, which is paid by all persons conducting a professional activity, is based on the rental value of the fixed assets subject to property tax that are used by the company;
  - ❑ The company added-value contribution: it is based of the added value generated by the company. It is based on the total sales, deduction made from certain expenses;
- The real estate contribution may be reduced through the reduction of the tax bases used for property tax purposes.
- It is also possible to obtain a real estate contribution reduction in case the activity of the company ceases.
- ➔ It is therefore necessary to pilot the liquidation operation as well as the flow of information sent to the French tax administration in order to facilitate the tax reimbursements.

# Scenario 2 - Presentation

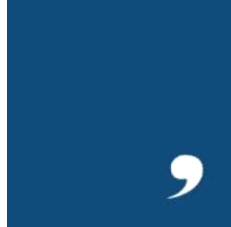


- ❖ Scenario 2: « *Conversion of an industrial brownfield into residential units* »
  - Company B owns a contaminated land located in an urban area.
  - The industrial installations are dismantled.
  - The contaminated land will be used for the construction of buildings that will be used for residential units.

# Scenario 2 - Charts



# Scénario 2 - Issues



## ❖ Tax issues

- Optimization of the tax losses management
- Property tax & Business tax issues
- Tax optimization of the decontamination financing
- Tax piloting of the demolition works
- VAT deductibility
- Optimization of the capital gain taxation in case of the terrain's sale:
  - ❑ Corporate income tax;
  - ❑ Specific tax due on the sale of the terrain that become constructible;
- Optimization of the terrain's sale:
  - ❑ Qualification as « building land » for VAT purposes;
  - ❑ Application of the VAT to the sale and taxation modalities;
  - ❑ Application of the registration duties to the sale and taxation modalities;

## Scenario 2- Optimization of the tax losses management



- ❖ The same tax issues mentioned in scenario 1 apply to scenario 2.

# Scenario 2 - Property tax & Business tax



## ❖ Keeping the business tax burden under control

- The same business tax issues mentioned in scenario 1 apply to scenario 2.

## ❖ Keeping the property tax burden under control

- The same property tax issues mentioned in scenario 1 apply to scenario 2.

## Scenario 2 - Tax optimization of the decontamination financing



- ❖ The same tax issues mentioned in scenario 1 regarding the capitalization of decontamination expenses apply to scenario 2.



# Scenario 2 - Tax piloting of the demolition works



- ❖ The same tax issues mentioned in scenario 1 regarding the capitalization of demolition expenses apply to scenario 2.

# Scenario 2 - Capital gain (1/2)



## ❖ Optimization of the capital gain taxation in case of the terrain's sale:

- The « 210 E » regime is extinguished since December 31st 2011;
- A new regime has replaced it: A special reduced tax applies on capital gains generated by the transformation of office units into residential units (Article 210 F du CGI).
- This allows to transform a part of the offices into residential units and to optimize the capital gain taxation;

# Scenario 2 - Capital gain (2/2)



## ❖ The capital gain taxation on constructible lands has increased:

### ➤ National tax on the cession of the constructible lands :

- A specific tax applies on the first cession of a constructible land;
- The tax applies if the ratio Sale price/Acquisition price is superior to 10;
- An annual allowance of 10% is provided after the 8th year following the classification as constructible land;
- The tax base, which amounts to the difference between the sale price and the acquisition price and when the sale price is 10 times superior and 30 times inferior to the acquisition price, is taxed at a 5% rate.
- The tax base, which amounts to the difference between the sale price and the acquisition price and when the sale price is over 30 times superior to the acquisition price, is taxed at a 10% rate.
- The tax is due by the seller;

### ➤ « Grenelle II » taxes:

- Two taxes based on a fraction of the capital gain may be instituted by city councils;
- The « Grand Paris » tax was suppressed at the end of 2010;

# Scenario 2 - Asset deal (1/2)



## ❖ Qualification as a building land for VAT purposes

- The sale of a building land:
  - ❑ is subject to VAT and land registration tax (0,71498% of the sale price) if the prior acquisition did generate the deduction of VAT;
  - ❑ is subject to the « *margin VAT* » scheme and to the registration duty of 5,09% if the prior acquisition did not generate the deduction of VAT;
- In both cases, the registration duty may be reduced to 125 € in case of commitment to proceed with the construction of a building on the acquired terrain;

# Scenario 2 - Asset deal (2/2)



## ❖ Sale modalities of a building land - Sale to a promoter or to an investor:

- The company may sell its terrain to a promoter or to an investor :
  - ❑ Only a 125 € registration has to be paid if the promoter commits itself to proceed with the construction of a building on the acquired terrain;
  - ❑ The sale in « VEFA » of the building is subject to VAT and generates land registry duty;
  
- The company may sell the building to a promoter, which generate tax savings:
  - ❑ Only a 125 € registration has to be paid if the promoter commits itself to proceed to a construction;
  - ❑ The real estate promotion contract may not be published. If it were, only the 125 € registration duty should be paid;
  - ❑ The land registration duty, based on the fair market value of the buildings, will not have to be paid;
  
- ➔ The VAT linked with the acquisition of the terrain is generally deductible. The VAT deduction could trigger a high financial burden.

# Scenario 2 - Share deal



- ❖ Increase of the registration duties on real estate companies - widening of the 5%-tax scope:
  - The old registration duty regime provided for the taxation of the acquisition price of a real estate company. The tax amounted to 5% of the acquisition price of the real estate company;
  - What does not change:
    - ❑ The rate: **5%**
    - ❑ The definition of a real estate company: basically, in order to qualify as a real estate company, the balance sheet of the company should be comprised of at least 50% of real estate assets;
  - What changed since January 1st 2012:
    - ❑ The tax base of the 5% registration duty: the tax base is now basically the fair market value of the underlying assets deduction made from certain liabilities linked with the acquisition of the assets;

# Scenario 2 - VAT deductibility



- ❖ The construction of residential units will trigger a VAT deductibility issue at some point of the commercialization of the buildings:
  - The input VAT relating an expense or a fixed asset may be deducted provided this expense or this asset is used for an operation subject to VAT that allows the deduction of the input VAT;
  - When a residential unit is constructed, no VAT deductibility issue arises since:
    - ❑ Either the building will be sold with VAT included;
    - ❑ Either the building will not be sold and a “*self-delivery*” (the building will be deemed to be sold to its builder for VAT purposes) for VAT purposes will occur within approximately two years after the completion of the building (Reminder: the self-delivery is deemed to be a VAT-taxable operation);
  - Specific rules apply when the residential buildings are bought by a buyer-reseller.

# Scenario 2 - International tax optimization



## ❖ Optimization of the capital gain taxation through a structuring in other countries of the European Union:

- Certain tax treaties provide for the taxation of the capital gains on the sale of real estate companies in the country of residence of the seller. That is the case for the tax treaties with Belgium, Luxemburg, Germany;
- This allows to benefit from the participation exemption regime (tax exemption of the capital gains on the sale of participation).

➔ The use of these countries allow for a double exoneration of the capital gains of the sale of real estate companies. However, the abusive or fraudulent nature of the structuring should be watched for.

- It is necessary to watch for possible modifications of tax treaties with the « interesting » countries and to be sure that the participation exemption regime applies. To this regard:
  - ❑ The French-Luxemburgish double tax treaty is currently being renegotiated;
  - ❑ Belgium restricted the use of the « *participation exemption* » regime;





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