S&A Sevestre & Associés

AVOCATS EN DROIT FISCAL

71 avenue Marceau 75116 PARIS
T. 33 (0)1 53 57 90 10
F. 33 (0)1 40 70 09 65
info@sevestre-associes.com

OCTOBER 2021

THE ATTRACTIVENESS OF TAX DRIVERS: BIOTECHS IN FRANCE

> REVIEW OUR WEBINAR <

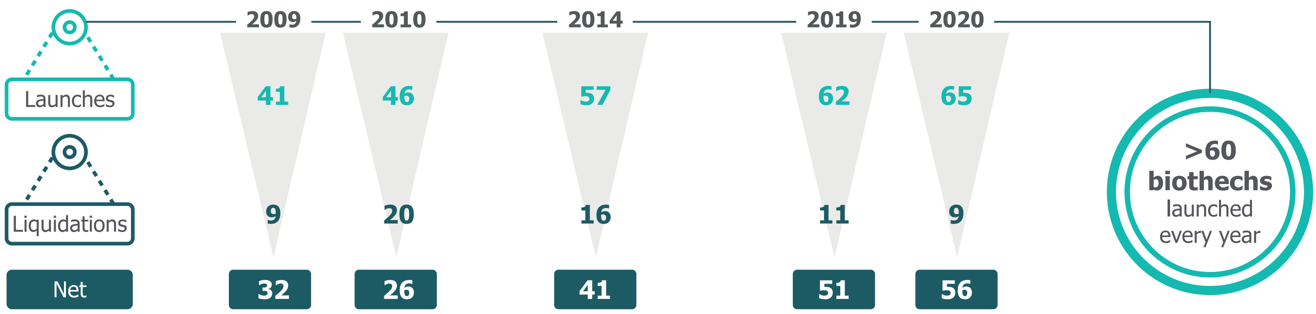
Why is France attractive for Biotech industry ?

- 7 Billion Investment in Biomedical research by 2030
- Status of innovative start-up
- Favourable regime for investors in venture capital
- Reduced rate of taxation for intangibles
- Tax impatriation regime
- Relationship based on trust with FTA (“ESSOC” law)
- Development of tax rulings: tax credit and R&D

1. Tax incentives at the level of the companies

a. Introduction

- Biotech company launches and liquidations



France has an extensive web companies in the health industry (biotechnology, medical devices and diagnostics, eHealth, etc.). The panel of participating companies has almost doubled in 5 years, reaching a total of 405 companies in 2020. The sector has a strong startup dynamic, with around 60 new companies launched yeah year. The number of launches has been on the past ten years (+41%) while the number of liquidations has fallen (-55%).

Source INSEE, verif.com : 2013 France Biotech Panorama

CIR

- **€7.04 billion** of research tax credit (CIR) in 2019
- **26.900 companies** declare €25.5 billion in eligible expenses to the CIR

INNOVATIVE START-UP

- **3,994 companies** benefited from 203 million euros (M€) in exemption, in 2018
- **€1,247 million** in domestic R&D expenditures by Innovative start-up made in 2018

b. Research Tax Credit (RTC)

- **Objective**

- Article 244 quarter B of the French Tax Code (FTC)
- Encourage companies to innovate by promoting the effort dedicated to R&D

- **Tax deduction**

- 30% of the amount of eligible research expenses over a calendar year (or 50% in overseas departments):
  - for a first bracket up to €100M
  - then 5% of the expenses beyond €100M

- **Principle of deduction**

- If sufficient tax: Deduction of the Corporate Tax

- If insufficient tax:
  - Reimbursement by the Administration if status of Community SME status
  - Reimbursement within 3 years if no Community SME status

ATTENTION POINT

- **Annual reporting on form** 2069-A-SD

- **Securing the CIR:**

- The CIR Rescript
- Request on demand

c. Tax credit and R&D (CIR)

- **Beneficiary companies**

▸ **French companies**

- **All companies** under French law
- Subject to **corporate income tax (IS)** or **income tax (IR) &D**

▸ **European companies**

- European companies that have a subsidiary in France (or a legal structure such as a permanent office)
- Only certain resources are to be considered

- **Eligible research expenses**

▸ **3 cumulative conditions**

- Expenses on **research activities defined as such**
- Research activities **located in the EU** or in the EEA zone
- Be an expense **retained for the determination of the taxable result**

- **Nature of eligible expenses**

- Depreciation of assets and buildings allocated to research
- Personnel expenses for researchers, research technicians, and additional remuneration of employees who are authors of an invention (and some specific cases)
- Operating expenses, fixed at 75% of depreciation and 43% of personnel expenses (200% for expenses concerning young doctors)
- Outsourced research expenses operated by approved organization (under conditions)
- Certain expenses for standardization of the company's products (for 50% of the amount)
- Technological watch expenses (60 000 € per year maximum) and Patent costs and IP protection

NB : some expenses must be deducted from the calculation base of the CIR

d. Status of the innovative start-up

- **Tax advantages**

- Income tax and corporate income tax exemptions: 50%

- **Total exemption** the first year

- Territorial economic contribution and Property tax: Exemption for 7 years to be checked with the local authorities

Conditions to be qualified as innovative start-up

- Independent SMEs which carry out R&D expenditure amounting to at least 15% of the tax-deductible expenses of a given fiscal year *(list of article 244 quarter B II a to g of the FTC)*
- Possible combination with R&D tax credit
- Not applicable to companies set up in the context of a merger, restructuring, expansion of activities or takeover of such activities

2. Tax drivers for the mobility of the individuals

a. Impatriation

- **Principle**

- **Temporary and partial income tax exemption** garanted to employees and managers:
  - Assignment in France from a foreign company
  - Or direct recruitment by a French company
- No exemption for French social contributions purpose

- **Conditions**

- Not being French tax resident at the recruitment (i.e. during negotiation and signature of the contract)

- Not have been French tax resident at any time during the **5 calendar years preceding the French assignment**

- Becoming French tax resident at the beginning of the assignment (flexible condition for certain situation)

- **Scope of the exemption (1/2): Employment incomes**

- **Part of the remuneration corresponding to the French expatriation *("Prime d'impatriation")***
  - Expatriate premium: provided by the employment contract OR self assessed by the employee up to a lump sum amount amounting 30% of the taxable remuneration (excluding LTI, profit sharing...)
  - Limit: Taxable remuneration =/> usual remuneration received for similar functions in the same company or similar French companies

S&A Sevestre & Associés

AVOCATS EN DROIT FISCAL

OCTOBER 2021

- **Remuneration related to the activity carried out abroad for the company *("Prime d'expatriation")***
  - Premium provided by the employment contract depending on the business trip OR self-assessed by the employee (current method: portion of workdays abroad over total number of workdays)

- **Exemption ceiling *(option to be chosen by the employee)***
  - Option 1: **global ceiling of 50% of the total remuneration** (including exempted premiums)
  - Option 2: **particular ceiling of the remuneration related to the activity carried out abroad only: 20% of the taxable remuneration** (i.e., after deduction of the impatriate premium)

• Scope of the exemption (2/2): Passive incomes receive out of France

- **50% exemption of dividends, interest and capital gains on movable properties**
  - Flat tax of 23.6% instead of 30% (and even 13.9% in case of affiliation of the taxpayer to the social security system of another EU/EEA country than France, or Switzerland)
- **50% exemption of incomes deriving from copyright and industrial property right**

• Duration

- **Exemptions applicable from the year of assignment until the end of the 8th following calendar ones**
- **50% exemption of incomes deriving from copyright and industrial property right**

Example

Situation

- Married couple moving in France without children (secondment of one of the spouses)
- Annual taxable salary: €280,000
- Reference salary in France for similar functions: €200,000
- Workdays abroad: 55 over 220 (25%)

50% exemption of employment incomes

Expatriate premium (lump sum 30%): €84,000 capped at:	▶	€80,000 *(considering the reference salary)*
Remuneration related to business trips abroad:	▶	€50,000 *(€200,000 x 25%)*
Global exemption cap (option):	▶	€140,000 *(50% of the whole taxable salary)*

Tax due by impatriate resident: €29,000 (instead of €66,000 for other French Tax Resident) i.e. a tax saving amounting to circa 56% in this particular case

b. Other favorable measures

• Exemptions for French tax residents seconded abroad not benefiting from the impatriate regime

- **Condition:** activity performed out of France and out of the country of the employer established in EU/EEA

- Full exemption of remuneration paid in consideration of the activity performed outside France

  - E.g.: Particular assignments performed during a minimum of time (international business development of at least 120 / 365 days, construction or industrial site works of at least 183 / 365 days…)

- If not: Partial exemption limited to the premium related to assignment abroad

  - Business trips carried out in the interest of the employer only lasting at least 24 hours abroad
  - Depending on the number, duration and location of the trips and capped at 40% of the remuneration

• Flat tax at the rate of 30% applied to dividends, interests and capital gains

- 12,8% of income tax (instead of a potential maximum tax rate of 45%) +17.2% of social contributions (7.5% if the taxpayer is affiliated to the social security system in EU/EEA (except in France) or in a third country)

• Real estate capital gains realized by former French tax residents

- Exemption from capital gains tax realized on the sale of the former main residence in France

  - Sale concluded not later than 31 December of the year following departure from France
  - Real estate not available to third parties since departure from France to another EU country

- Exemption from capital gains tax on the sale of a one Home in France capped at €150,000

  - Taxpayer has been French tax resident on a continuous basis during 2 years at any time before the sale
  - Sale concluded no later than 31 December of the 10th year following the departure from France (or real estate at the taxpayer's disposal since at least 1 January of the year preceding the sale)

• Real estate wealth tax

- **Impatriate** (taxpayers becoming French tax resident without have been so during the **5 preceding years**)
  - **During 5-year following his move-in France:** taxable on his **French properties only** (as a non-resident)
  - **After:** taxable according to his **worldwild properties** (like a French tax resident)

3. Corporate income tax incentives

a. Tax consolidation (vertical / horizontal)

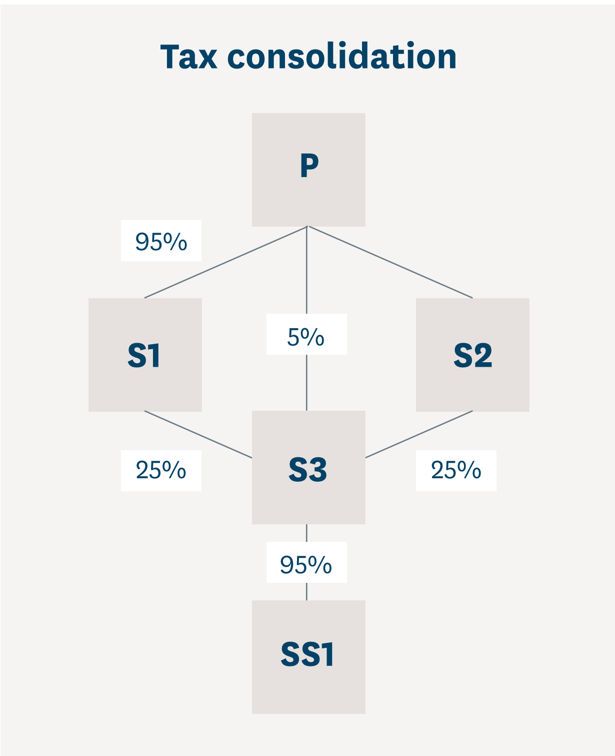
- **Principle -** Article 223 A of the French Tax Code (FTC) **-**

- **Consolidate the results of each company in the group** to be consolidated into a single result, the «overall result”
- Permits the losses of some companies to be balanced against the profits of others
- Applied on the option of the group’s parent company

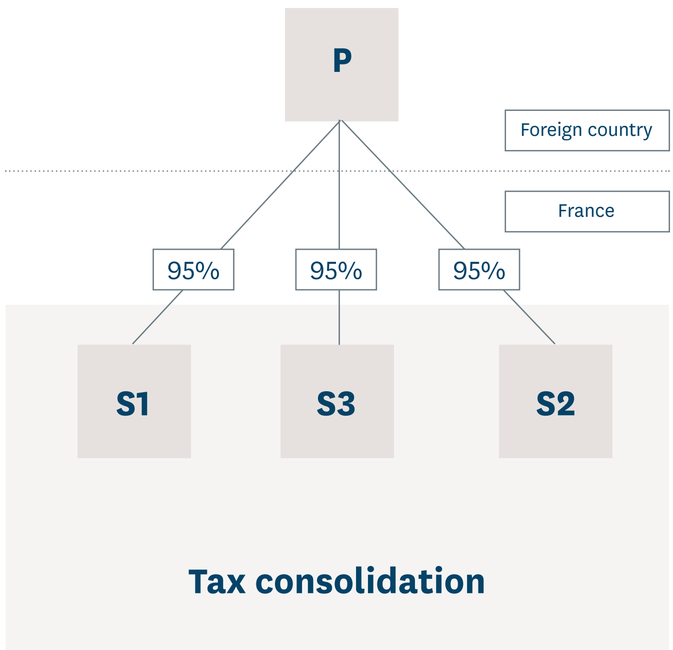
- **Conditions**

- All the companies in the group must **be subject to corporate income tax** at the standard rate (reduced or normal rate) and on the total results of the French operation, regardless of the form and nature of the activity carried out by the companies
- All group companies must **close their financial year on the same date**
- **Subsidiaries must be at least 95% owned**, directly or indirectly, by the parent
- **The parent company must not be more than 95% owned,** directly or indirectly, **by a company subject to corporate income tax** with its registered office in France

Vertical tax consolidation



Horizontal tax consolidation



b. Deduction of financial expenses

- **Principle -** Article 212bis of the French Tax Code (FTC)
  The 2019 Finance Act adapted French kaw to the EU ATAD 1 Directive **-**

- Companies that are not undercapitalized can **deduct their net financial expenses** up to the higher of:
  - **3M€ per tax year,** if necessary reduced to 12 months
  - **30% of income before tax,** interest, depreciation and amortization (Tax Ebitda)
- The capping rule applies **at the level of the tax group** and not at the level of each company in the group
- An **additional deduction** for autonomous companies is introduced, for net financial expenses not deducted after application of the ceiling of 30% of the tax Ebitda or €3 million. The amount of the additional deduction is 75% of the net financial expenses not allowed as a deduction after application of the first ceiling

- **Tax Ebitda**

- **Tax EBITDA** is not identical to accounting EBITDA. A certain number of adjustments, reintegrations and deductions must be made

c. Transfer pricing awareness

- **Definitions**

- "The prices at which an enterprise transfers tangible property, intangible assets, or provides services to associates». OECD

· Transfer prices are the prices at which international intra-group flows are concluded. This also includes transactions for free

- **Obligations**

In France, companies are subject to several documentary or reporting obligations relating to transfer pricing:

- **A transfer pricing declaration** (art. 223 quinquies B of the French General Tax Code) **if:**
  - Turnover before tax or gross assets ≥ **50M€** (and no longer 400M€) ; or
  - Owing (/being owned), directly or indirectly, (in the amount of) more than half of the capital of (/by) such an entity; or
  - Belonging to a group covered by the tax consolidation regime if a member of the group meets one of the above criteria.

- **A transfer pricing documentation** (art. L. 13 AA of the French Tax Code) **if:**
  - Legal entities established in France, and
  - with a turnover excluding taxes or with gross assets in the balance sheet exceeding 400 M€, or holding more than 50%, or being more than 50% held by an entity meeting this criteria.

- **A country-by-country reporting** (art. 223 quinquies C of the French Tax Code)
  - For multinational enterprises with consolidated revenues of at least 750M€

4. Tax opportunities and challenges on Intangibles

- Tax issues in the valuationof intangibles in Biotechs companies -

a. Attractive French taxation regime on intangibles

• **Incentive but complex – Nexus Regime** - Article 238 of the FTC : Option for the taxation at the reduced rate of 10% of the net result of the transfer, concession, sub-concession or capital gains of patents and similar intangible asset

- The modalities of the option concern either : assets, goods or services, family of goods or services *(it must be a fixed asset)*
- It must be an intangible asset listed in article 238 of the FTC, e.g:
  - **Patents, Industrial property titles, Software protected by copyright, plant variety certificate**
- Equivalent foreign titles issued by **a foreign industrial property** office are **eligible**
- Application of the Nexus Ratio, taking into account multiple parameters

b. Valuation framework and challenges (1/2)

Arm's length principle

• **Several valuation methods:**

- **Traditional methods:**
  - Comparable open market price method
  - Resale price method
  - Cost plus method

- **Transactional methods, profit based:**
  - Profit sharing method
  - Transitional net margin method

- **Functional analysis:**

The company examines its place and its economic role within the group and identifies the functions performed, the risks incurred, the tangible and intangible assets used.

Function
Design, R&D, services, provision of intangible assets

Risk
Market risks, after sales service, financial risks,...

Assets and means used
Type, characteristics and means used

- **DAC 6 challenge regarding valuation of intangibles**

Sevestre & Associés

71 avenue Marceau 75116 PARIS
T. 33 (0)1 53 57 90 10
info@sevestre-associes.com
www.sevestre-associes.com