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FRANCE

Taxation of real estate income realized in France by non-French tax residents:
European law provides serious grounds for tax refund

- Further to two recent cases, the French Administrative Supreme Court (Conseil d'Etat) ruled that the 33.33% withholding tax on capital gains from French immovable property realized by non-EEA tax residents is incompatible with European law and certain French tax treaty provisions.
- Moreover, social contributions paid in France by non-French tax residents on their real estate income also appear to be unlawful under European law.
- Both situations may lead to a tax refund for non-French tax residents.

33.33% withholding tax on capital gains from French immovable property realized by non-EEA tax residents: a partial refund to be requested.

In a decision dated December 26, 2013, the French Supreme Court ruled that the 33.33% withholding tax on capital gains from French immovable property realized by non-EEA tax residents (article 244 bis A of the French tax code) is incompatible with the principle of freedom of movement of capital within the EU. Indeed, on identical transactions, European Economic Area (EEA) tax residents are only subject to a 19% withholding tax.

In practice, this new case law provides serious arguments to challenge the application of the withholding tax on real estate capital gains realized in France at the rate of 33.33% to individuals fiscally resident outside the EEA, instead of the 19% rate applied to French, EU and EEA tax residents.

In this respect, French procedural rules provide that the filing of a refund claim is only open up to December 31 following the year during which the tax has been withheld. Therefore, claimants who were taxed at 33.33% on transactions carried out in 2013 have until December 31, 2014 to file a claim for refund of the 14.33% difference.

It should be noted that, in another French Administrative Supreme Court case dated November 20, 2013, it has also been ruled that this withholding tax does not comply with the provisions of article 15.4 of the French-Swiss double tax treaty dated September 9, 1966.

However, in this particular case, the argument pertained to the precise wording of the French-Swiss tax treaty. Consequently, such a solution might not be applicable to all situations and attention must be paid to the relevant treaty provisions.

Social contributions paid by non-French tax residents on income from real estate in France: a tax claim worth considering.

Since 2012, non-French tax residents have to pay social contributions on their income related to French immovable property (i.e. on capital gains and property income). Although this tax has been validated by the French Constitutional Court, one can argue that this measure is incompatible with EU rules.

Indeed, as per article 13 of Regulation (EC) n°1408/71 and article 11 of Regulation (EC) n°883/2004, a person is liable to one social security system only. This is the so-called "single applicable legislation" rule.

Subsequently, France cannot subject immovable property income of non-French tax residents to French social contributions without breaching European law.

In this context, the European Commission has recently begun infringement proceedings against France while the European Court of Justice (ECJ) has been asked to give a preliminary ruling on this very point. Since neither procedure will suspend the payment of the

social contributions (currently at 15.5%), non-French tax residents will have to pay it if they realize relevant income.
However, as there are serious grounds to demonstrate that these contributions are not compliant with the aforementioned regulations, taxpayers can apply for refund from the French tax authorities.
For capital gains, refund claims are open up to December 31 following the year during which the social contributions were paid. For property income, the deadline is December 31 of the second year following the year during which the social contributions were paid.
It is worth noting that such social contributions can also be challenged, based on provisions included in certain tax treaties concluded by France. Here again, attention must be paid to the relevant wording of the treaties.

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FRANCE

Tax deductibility of provisions: Accounting treatment trumps tax treatment

- Up until recently, companies that had provisions that met all the criteria for tax deduction could choose whether or not they wanted to deduct said provision.
- The French Administrative Supreme Court issued a decision on December 23, 2013: "Société Foncière du Rond-Point" that puts an end to this practice: if the criteria for a provision to be deducted on a tax level are met, then such a deduction is no longer an option but an obligation.

In French law, the deductibility of provisions follows somewhat different rules depending on whether the deduction is to be made on an accounting or a tax level.

These rules can be briefly summarized:

On an accounting level, a provision must be recorded for a given financial year when a company has a financial obligation to a third party that will probably or certainly generate an outflow of resources without any equivalent retribution on the third party's part. (Article 312-1 of the General Chart of Accounts)

On a tax level, the deduction of provisions requires that a certain number of criteria be concurrently met: the provision must be effectively recorded in the financial statements; it must be allocated in order to face a loss or a tax-deductible expense; a reliable estimate of said loss or expense must, at the time of the tax deduction, be possible; the loss or expense must be probable, and must derive from events that are ongoing at the close of the financial year. (Article 39, 1-5° of the French Tax Code).

To be tax-deductible, the provision must have been recorded on an accounting level beforehand. However, up until now, companies would in a number of cases waive their right to the tax deduction of the accounting provision, even though the criteria allowing such a deduction were met. The reason for such a waiver was mostly that companies want to ward off inevitable discussions during tax audits, as tax auditors often challenge the deductibility criteria; on other occasions, the reason would be optimisation considerations, or the company's wish to avoid a double taxation. Since the carry-forward mechanism of tax deficits has been capped (at 50% of the amount above 1 million euros), deducting the provision could actually generate a deficit that could only partially be offset on the profit generated by the reversal of the provision.

Another typical case scenario is that of intra-group provisions: as they are neutralized, they are not deducted. However, the reversal could be taxable when the company leaves the integrated group.

For provisions that weren't deducted on a tax level, the company would usually reverse said provisions on an accounting level before proceeding to an extra-accounting deduction.

The French Administrative Supreme Court in its December 23, 2013 decision "Société Foncière du Rond-Point" impacted this option. The Supreme Court considered that the reversal, in a subsequent exercise, of a provision that the company decided not to deduct on a tax level although the criteria for such a deduction were met, results in an increase of the net assets of the closing balance sheet(s) of the corresponding financial years. Hence the reversal of the provision will be taxed, even if it wasn't initially deducted.

This jurisprudence brings to light a clear rule: the accounting treatment of a provision trumps its tax treatment. When the criteria for tax deduction are met, companies now have the obligation to deduct the recorded provisions from their tax result. The reversal of the provision will be taxed, whether said provision was deducted on a tax level or not.

Discussions surrounding the tax deductibility of provisions in the framework of tax audits will undoubtedly multiply.

The consequences are particularly stark for provisions related to prescribed financial years that were recorded but not deducted on a tax level: the reversal of such provisions will be taxed with no possibility for companies to remedy the initial absence of deduction.

Recommendations:
As for financial years 2013 and onwards, it is essential to check carefully if the conditions for the fiscal deductibility are met. If so, or even in case of doubt, it might be advisable to deduct the provision.
We would advise also to carefully check the accounting provisions accrued during the years 2011 onwards and not deducted fiscally.
Unless there are strong reasons to defend the non-deductibility, it would make sense to deduct the provision fiscally before the given FY is prescribed.

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GERMANY

Treaty override:
Hope that courts will prohibit it

- Two decisions taken by German Finance Courts now provide taxpayers with the opportunity of contesting the treaty override frequently practised by taxation authorities.
- Although both decisions are not yet final and will thus not be accepted as a decision basis by the taxation authorities, they do offer an approach to avoiding the non-appealability of the tax-increasing assessment notices, with the aim of subsequently being able to claim the protection of a possibly positive final verdict in one of the precedent cases.

Background:

For taxation of cross-border business transactions, national taxation law contains a wealth of regulations that restrict the tax relief provided in the Convention for the Avoidance of Double Taxation (DTC) or relevant EU directives. As a result, Germany claims a right of taxation of taxpayers resident in the Federal Republic of Germany, although it has already waived this right under the provisions of the DTC. This regularly leads to an additional financial burden as a result of de facto double taxation. In practice, this becomes particularly relevant for royalties, dividends or interest which are paid from Germany to a foreign licensor, shareholder or lender. The restrictions or exemptions applying to withholding taxes under EU directives or the DTC are undermined by simple national law. This topic was also treated by the TAG Tax Group at the TAG/TIAG Spring Conference held in Munich in October 2013.

Unlike in other jurisdictions, the acceptability of a treaty override under German law has hitherto been confirmed by the finance courts and by relevant opinions in tax literature.

Current development:

Now two decisions taken by German courts give reason to hope for a change in legal rulings.

For the first time, the Federal Court of Finance *(Bundesfinanzhof)* has seen the treaty override as incompatible with the German Constitution. Since, under German law, only the Federal Constitutional Court *(Bundesverfassungsgericht)* is empowered to establish that a law is unconstitutional, the Federal Court of Finance was not able to pass a verdict. So it passed the case to the Federal Constitutional Court to establish whether the treaty override was in compliance with the Constitution. In another case, the Finance Court of Hamburg decided that a tax provision – irrespective of possibly also being incompatible with the Constitution – is certainly ineffective if it contradicts the rulings of a DTC agreed at a later date. The Court bases its decision on the principle of “lex posterior derogat legi priori”, under which tax-increasing national rulings are overruled by a DTC agreed at a later date.

The specific case before the Finance Court of Hamburg related to a person subject to unlimited taxation in Germany who had participated in an OSCE mission to Azerbaijan. He was paid for his work by the OSCE. Under the DTC between the Federal Republic of Germany and the Republic of Azerbaijan, these earnings should have been exempted from taxation in Germany. Nevertheless the German tax authorities taxed them, basing its decision on a more stringent tax ruling which had come into effect, however, before the DTC was agreed.

Citation of the lex posterior rule – which applies in accordance with German legal principles – allowed the Finance Court of Hamburg to pass a verdict on the treaty override without having to consult the Federal Constitutional Court. In this way, the complainant was saved the lengthy course of proceedings. In view of its citation of the general legal principle of “lex posterior”, the decision taken by the Finance Court of Hamburg may become relevant and is undoubtedly suited to achievement of significance going beyond the actual case in hand.

Practical information:
If a person liable to pay tax in Germany is not granted tax relief under EU directives or the appropriate DTC as a result of a treaty override, an objection to the relevant tax assessment notice must always be lodged within four weeks. This objection must make reference to the proceedings pending at the Federal Constitutional Court relating to whether a treaty override is constitutional (file no. II BvL 1/12). Insofar as the taxpayer can claim tax relief under a DTC or EU directive that is more recent than the more stringent national taxation ruling, such an objection should also always be based on the "lex posterior" decision of the Finance Court of Hamburg (file no. 1 K 87/12).

Since, for obvious reasons, the tax authorities have filed an appeal against the last-mentioned verdict (file no. I R 64/13) and the quoted proceedings at the Federal Constitutional Court have not yet been completed, tax offices will not readily remedy the objection. In such cases, procedural law provides the legal alternative of adjournment of the proceedings, for which the taxpayer should definitely make application.

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MALTA

Individual Investor Program for non EEA persons & Ordinary residence for EEA persons

- A new Individual Investor Program is broadening the right to Maltese citizenship investors.
- Maltese non-resident citizens will benefit from interesting tax advantages.

The IIP is regulated by Legal Notice 47 of 2014, Maltese Citizenship Act (Cap. 188), Individual Investor Program of the Republic of Malta Regulations, 2014.

The following are highlights from this Legal Notice.

This Program shall allow for the granting of citizenship by a certificate of naturalisation to foreign individuals and their families who contribute to the economic development of Malta.

The qualifications and general requirements for a person to be a Main Applicant for citizenship under this Program are the following:

- At least 18 years of age;
- Meet the application requirements;
- Make a contribution;
- Have a residential address in Malta (minimum purchase price of €350,000 or minimum rental value of €16000 per year);
- Provide proof of residence of Malta for a period of at least twelve months preceding the issuance of the naturalisation certificate;
- Commit to investing in Malta;
- Applicant and dependents must all have a global health insurance;

The Program will be managed by a Government Agency called Identity Malta. The number of successful applicants under the Program will be capped at 1,800.

Identity Malta will receive applications from Maltese financial services practitioners to be appointed as Accredited or Approved Agents. Only Accredited or Approved Agents will be authorized to promote the Program and to submit applications on behalf of clients to Identity Malta.

The Main Applicant shall also provide a written statement that he will undertake other such investment in Malta for an amount of €150,000 as identified by Identity Malta and retain such investment for 5 years.

The contribution values are as follows:

- Main Applicant - €650,000
- Spouse - €25,000
- Child under 18 years - €25,000
- Unmarried child 18 to 26 years - €50,000
- Dependent parent or grandparent above 55years - €50,000

A personal interview with an applicant is not mandatory but may be requested.

The Minister shall issue a certificate of naturalisation to all successful applicants within 2 years, but not earlier than 6 months, from the date of an approved application. The applicants can then apply for a Maltese passport after taking an Oath of Allegiance. Passport fees are €500 per passport.

Malta Ordinary Residence

European Economic Area (EEA) or Swiss nationals have the right to reside in a European Country by exercising any of their Treaty rights. These are: work, self-employment, economically self-sufficient individuals, students and family members. Under European law, an EEA or Swiss national does not need to obtain any particular documentation in order to confirm their right of residence in Malta. One can apply for a registration certificate, which would confirm your right of residence in Malta under European law.

Ordinary Residence: An EEA national can reside in Malta if they can prove one of the following:

- employment/self employment;
- economic self-sufficiency; and
- education;

Family members: Family members of an EEA national have the right to join and accompany the applicant in Malta. Family members are defined as the spouse, children or grandchildren of EEA nationals or those of the applicant's spouse, who are under 21 years of age or who are dependent on the applicant and the dependent parents or grandparents of the EEA national or of the applicant's spouse.

Employment/Self-employment: EEA nationals and their family members can accept offers of work and seek employment in Malta, work (whether as an employee or in self-employment) and set up a business.

Economically self-sufficient persons: An EEA national does not necessarily have to work while he is living in Malta. However in order to reside in Malta, he must be able to support himself and his accompanying dependents, without recourse to public funds. The current thresholds are set at a minimum capital of €14,000 or a weekly income of €92.32 or, in the case of a married couple, a capital of €23,300 or a weekly income of €108.63.

Students: An EEA national and his family members, following a recognized course of education in Malta, also have the right of residence in Malta on the condition that they are able to support themselves and accompanying dependents without recourse to public funds.

Permanent residence: Once the EEA national and his/her family members have lived in Malta for a continuous period of five years they are entitled to apply for confirmation of permanent residence on the basis that they still satisfy, at least, one of these conditions.

Taxation on remittance basis: Malta adopts a remittance basis of taxation with respect to (Malta) resident non- domiciled individuals. This means that these individuals are subject to tax in Malta only on income or capital gains arising in Malta and any other source of income that is remitted to Malta. They would therefore not be taxable on foreign source income not remitted to Malta.

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