

French financial transaction tax on equity securities

Latest developments and practical implications for the market

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On 31st July 2012, the French Parliament voted the Second Amended Finance Bill for 2012 (“Loi de Finances rectificative”) and amended the financial transaction tax (FTT) originally introduced in French tax system by the First Amended Finance Bill for 2012.

The Second Amended Finance Bill shall be published shortly.

The FTT is effective since 1st August 2012.

This is an updated version of our alert issued on 28 June 2012.



France introduced a financial transaction tax as part of the First Amended Finance Bill for 2012 dated 14 March 2012.

The financial transaction tax is actually composed of three different taxes:

- a tax on the acquisition of equity securities;
- a tax on high frequency trading; and
- a tax on naked sovereign credit default swaps (CDS).

This communication focuses on the first one, i.e., the equity securities tax (“FTT”).

As set out in the First Amended Finance Bill for 2012, the FTT is effective as from 1st August 2012.

Our alert (i) summarizes the latest developments / information in respect of the FTT (including, in particular, further clarifications following the publishing of final administrative guidelines on 3 August 2012) and (ii) highlights practical issues for further consideration.

Latest developments – highlights

- I. *Final guidance in relation to FTT has been published by the French tax authorities on 3 August 2012*

New!

The final Guidelines in respect of the 3 financial transaction taxes and in respect of registration duties have been published

The final guidelines (“**Final Guidelines**”) have been released on 3 August 2012 and cover the three taxes, i.e., the tax on equity, the high frequency trading tax and the tax on CDS.

Guidelines in respect of the French registration duties have been published on Monday 6 August 2012.

New!

Decrees

Decrees have been published, including:

- a list of the French listed companies within the scope of the tax (14 July 2012); and
- the obligations of the parties liable to the tax, notably with regard to information to be provided to the central securities depository, Euroclear France (7 August 2012).

New!

Euroclear France and professional organizations publications

Euroclear France, the AMAFI (“*Association Française des Marchés Financiers*”) as well as the AFTI (“*Association Française des Professionnels des Titres*”) have issued updated indicative guidelines in order to set up best practice charts for the different parties.

II. Details in relation to the scope of the FTT

A. Securities in scope

The FTT applies to transactions consisting in acquiring equity securities (“*titres de capital*”) or similar securities within the meaning of the article L. 212-1 A of the French Monetary and Financial Code (“*Code Monétaire et Financier*”).

This also includes instruments giving access to capital or to voting rights in the company and includes securities issued under foreign law.

Only securities issued by French companies were in the scope of the tax.

New!

(i) “*ADR amendment*” effective as from December 1, 2012

The Second Amended Finance Bill for 2012 has extended, effective as from 1st December 2012, the scope of the FTT to securities representing French eligible securities issued by a company regardless of the location of the head office of the company issuing these securities.

Therefore, the acquisition of ADRs or EDRs should fall within the scope of the tax as from 1st December 2012.

Final Guidelines: position of the tax authorities

Depository certificates are considered by the tax authorities only as an “example” of the ad hoc financial vehicles/hybrid vehicles that may be put at the disposal of investor to avoid FTT (no.3).

✎ **The wording of the extension raises the issue of whether other investment vehicles or instruments may be included for FTT purposes as from December 2012.**

(ii) *Convertible bonds, subscription bonds and preferential subscription rights issued by a French Company*

New!

Final Guidelines: position of the tax authorities

Instruments giving access to capital or to voting rights in the company are in the scope. This includes the following instruments:

- bonds convertible into shares (OCA)
- bonds redeemable into shares (ORA)
- bonds convertible into new or existing shares (OCEANE)
- bonds exchangeable into shares (OEA)
- bonds with share subscription warrants attached (OBSA)
- bonds with share redeemable share subscription warrants attached (OBSAR)
- bonds with redeemable share subscription or acquisition warrants attached (OBSAAR)
- bonds redeemable into new or existing shares or bonds redeemable in new shares or in cash (ORANE)
- bonds redeemable in cash or into new or existing shares (ORNANE)

The Final Guidelines also states that subscription bonds (BSA, BSAR, BSAAR) as well as preferential subscription rights (DPS) are in the scope of the FTT (no. 4).

(iii) *Exchanged Traded Funds (ETF) and financial contracts (options, futures, warrants)*

New!

Final Guidelines: position of the tax authorities

The Final Guidelines confirm the position taken orally by the tax authorities, i.e. that FCP and SICAV shares including ETF as well as financial contracts (options, futures, warrants) do not qualify as equity securities within the meaning of the article L. 212-1 A of the French Monetary and Financial Code.

ETF units and financial contracts should not fall within the scope of the FTT provided that they cannot be considered as securities representing French eligible securities (as from December 1, 2012)

B. Taxable transactions, i.e. transactions resulting in a transfer of ownership of the eligible securities for consideration

The FTT only applies to transactions giving rise to a transfer of ownership within the meaning of Article L.211-17 of the French Monetary and Financial Code for consideration.

New!

Final Guidelines: position of the tax authorities

The tax authorities have specified that a transaction falls within the scope of the FTT should a consideration be received, regardless of the amount of such consideration (no. 11).

↳ **As a general principle, in most cases, the tax is assessed on the price paid or stipulated in the parties' arrangement, depending on the transaction at stake, and not on the fair market value of the securities.**

Intra-day transactions and deferred settlement services (Service de Règlement Différé - SRD) transactions

From a French legal standpoint, the transfer of ownership of listed securities occurs on the date of settlement of the transaction, i.e. on the date on which the securities are credited on the securities account of the purchaser.

With regard to intra-day transactions and transactions processed under the deferred settlement services ("*Service de Règlement Différé*" - SRD), this principle also applies, i.e. the transfer of ownership occurs on the settlement date as defined above.

Final Guidelines: position of the tax authorities

As a consequence of the application of the transfer of ownership principle, the tax has to be assessed on the basis of the net buying position with regard to intra-day transactions (no. 12 and seq).

The Final Guidelines also confirm that in respect of SRD trades, the tax has to be assessed on the basis of the net buying position at the end of the month (no. 13).

⚡ It is therefore crucial to be in position to verify whether a net buying position has been effectively settled and to modify as the case may be the amount of the tax due based on the instruments actually settled (see point VIII below).

C. Derivatives and Collateral

Final Guidelines: position of the tax authorities

The Final Guidelines confirm that transactions relating to derivatives are included within the scope of the FTT, but only to the extent that they are physically settled and upon settlement (no. 10).

The Final Guidelines also state that the acquisition of eligible securities realized in the context of a collateral arrangement governed by Article L.211-38 of the French Monetary and Financial Code does not constitute a taxable acquisition, even when the securities are transferred following the exercise of the guarantee (e.g. following a default from the borrower) (no. 14).

D. List of French listed companies with a market capitalization above €1bn issuing the securities to be published each year

Companies in scope for 2012

New!

A decree (“arrête”) providing a list of the companies (109 companies) in scope in relation to the transactions realised until 31 December 2012 has been published on 14 July 2012¹.

Only the name of the companies have been disclosed and not the ISIN codes. This potentially creates operational difficulties since a given company may have several ISIN codes. We understand that certain financial data providers have provided a list of ISIN Codes

Companies in scope for years 2013 and onwards

New!

Second Amended Finance Bill for 2012: amendment

Considering practical constraints and to enable the accountable parties to adapt their systems, the Second Amended Finance Bill for 2012 provides that the above assessment of the market capitalization will be done as at 1st December of the year preceding the one during which the transfer occurs (instead of 1st January – the Final Guidelines did not reflect this change in their paragraphs n°1 and n°19).

This provision will apply to transactions performed as from 1st January 2013.

List of the companies in scope to be updated in certain circumstances

¹ The list could be found on the following website :
<http://www.legifrance.gouv.fr/affichTexte.do?cidTexte=JORFTEXT000026178804&dateTexte=&oldAction=rechJO&categorieLien=id>

Final Guidelines: position of the tax authorities

The Final Guidelines confirm that the list of the companies in the scope will have to be updated in some circumstances by the parties involved (e.g. transfer of the head office of an eligible company out of France, transfer into France of the head office of an eligible company) (no. 16).

Conversely, changes of the market capitalization during the year have no impact (no. 19).

III. Market Maker and Other Exemptions

New!

Final Guidelines: position of the tax authorities

The Final Guidelines importantly specify that the exemptions may be granted to any non resident operator which carries out its activities or transactions under similar legal and regulatory provisions (no. 20).

A. Market maker

The objective of the “market maker exemption” is two-fold: avoiding (i) a cascading effect and (ii) any impact on the market liquidity. The exemption is therefore expected to be granted to transactions where the aim is to satisfy clients’ needs and to discourage speculative transactions.

The Final Guidelines provide for indications concerning the scope of the exemption; certain conditions are still questionable.

New!

Final Guidelines: position of the tax authorities

The Final Guidelines provide that the market maker exemption applies provided that both of the following conditions are fulfilled (no. 24 and seq).

1. Conditions related to the entity

The market making activity must be exercised by an investment firm (“*entreprise d’investissement*”), a credit institution (“*établissement de crédit*”), an entity resident in a foreign country or a local firm member of a trading platform or member of an exchange of a foreign country.

This entity must act as an intermediary and be party to a transaction in a financial instrument within the meaning of Article L.211-1 of the French Monetary and Financial Code.

2. Conditions related to the activity

Three categories of activities are covered, on which the Final Guidelines provide further clarifications.

a) Simultaneously quoting of firm, competitive bid and ask prices of comparable size with the result of ensuring market liquidity on a regular and continuous basis.

This exemption covers the following 2 situations:

- (i) Providing liquidity on a trading platform

- the intermediary must be present on the exchange on a continuous basis or must have a minimal presence on the exchange corresponding to at least - 95% of the time on both the purchase and sale part of the orders book continuously during the trading session (for financial securities) in respect of one day or 80% (for financial agreements) of the time on both the purchase and sale part of the orders book continuously during the trading session (for financial securities) in respect of one month. Specific conditions are also applicable in respect of financial options.
- the intermediary must provide a price that allows the realisation of a number of transactions sufficient to ensure the liquidity of the security; and
- the orders can be clearly identified.

No agreement with the platform is required – contrary to the criteria set forth by the Draft Guidelines.

(ii) Providing liquidity with regard to OTC transactions

The intermediary must fulfil the conditions to qualify as a systematic internaliser (“*internalisateur systématique*”) under French law or prove in certain circumstances that it published or communicated to his clients a firm price (“*prix ferme*”).

b) In the context of its normal activity, executing the orders given by clients or in response to client buy and sell requests

The entity must undertake an activity facilitating the execution of clients’ orders through the interposition of its own account.

The entity must be able to demonstrate a link between a client’s request and the acquisition it has realised for its own account. Consequently, the acquisition of securities (stockpile) by the intermediary as a result of an anticipation of an increasing demand on some securities cannot benefit from the market maker exemption.

c) Hedging of positions related to transactions covered under points a and b above

In order to claim the benefit of the exemption, the accountable party must be able to demonstrate the link between the acquisition/subscription of financial securities/contracts as part of its hedging activity and the market maker activities mentioned in points a) and b) above.

The Final Guidelines state in an example that a market maker on financial contracts (“*contrats financiers*”) acting within the conditions defined under point b) above (i.e. upon the request of the client) is not liable for the tax when it purchases eligible securities to hedge its position.

3. Safeguards

The acquisition of securities by the intermediary as a sole result of an anticipation of an increasing/decreasing demand cannot benefit from the market maker exemption.

Pure arbitrage activities do not fall within the scope of the exemption.

4. Documentation

In order to claim the benefit of the exemption, the accountable party can notably apply the exemption by reference to the mapping of the activities that investment firms and credit institutions must set up to comply with Regulation 97-02 (relating to internal controls in credit institutions and investment firms), subject to certain conditions.

✚ **A detailed mapping of the transactions carried out by each accountable party, which would distinguish the different categories of transactions, will have to be organized and properly documented.**

B. Convertible bonds exemption

New!

Final Guidelines: position of the tax authorities

The Final Guidelines provide that this exemption shall cover the acquisition of the following French and assimilated foreign bonds:

- bonds convertible into shares (OCA)
- bonds redeemable into shares (ORA)
- bonds convertible into new or existing shares (OCEANE)
- bonds exchangeable into shares (OEA)
- bonds with share subscription warrants attached (OBSA)
- bonds with share redeemable share subscription warrants attached (OBSAR)
- bonds with redeemable share subscription or acquisition warrants attached (OBSAAR)
- bonds redeemable into new or existing shares or bonds redeemable in new shares or in cash (ORANE)
- bonds redeemable in cash or into new or existing shares (ORNANE).

According to the French tax authorities, the acquisition of eligible securities following the exchange, the conversion or the subscription of such bonds is subject to tax.

C. Securities financing exemption

Securities financing transactions quoted in point 10 of Article 2 of the Commission Regulation (EC) 1287/2006 dated 10 August 2006 are exempt from the tax.

Final Guidelines: position of the tax authorities

According to the Final Guidelines, this exemption will cover the following (and similar) transactions:

- Stock lending transactions within the meaning of L.211-22 of the French Monetary and Financial Code
- Sale and repurchase agreements within the meaning of L.211-27 of the French Monetary and Financial Code

- Buy/sell transactions and sell/buy transactions to the extent the ownership of the eligible securities is not definitively transferred

New!

Final Guidelines: position of the tax authorities

Exempted transactions (to the exception of exempted exchangeable and convertible bonds) have in principle to be reported.

However, the Final Guidelines specify that in respect to securities financing transactions, as well as for corporate transactions (corporate action), only transactions carried out as from 1st January 2013 will have to be reported (no. 65).

It may however be argued that stock lending transactions should be outside the scope of the tax as there is no consideration paid (same reasoning as for the French registration duties). Therefore these transactions would not have to be reported at all but it would not be consistent with the reporting mechanism at the level of Euroclear France.

D. Primary market

Acquisition and subscription transactions performed as part of the issuance of equity or assimilated securities are exempt from the FTT under paragraph 2 of article 5 of the Council Directive 2008/7/CE of 12 February 2008 relating to indirect taxes on the pooling of capital.

Final Guidelines: position of the tax authorities

The Final Guidelines state that such primary market exemption also applies to acquisitions made from an Investment Service Provider (ISP) which itself acquires the eligible securities on the primary market in the context of underwriting services (no. 21).

New!

Final Guidelines: position of the tax authorities

The primary market exemption also applies to acquisitions made in the context of a stabilisation procedure as set forth by Regulation EC no. 2273/2003 dated 22 December 2003, to the extent such acquisition is connected with the issuance of securities on the primary market and not on the secondary market (no. 21).

E. Transactions performed by a clearinghouse or central securities depository

Transactions performed by a clearinghouse or securities depository as part of their respective regulated operations are exempted from the FTT.

Final Guidelines: position of the tax authorities

A clearinghouse or central securities depository, which purchases securities for own account with no connection with their regulated activities is not exempted from the FTT (no. 23).

⚡ **As indicated above, this shall also apply to non-French clearing houses or central securities depository to the extent they carry out their activities in a similar manner.**

F. Intra-group, restructuring schemes and employee saving schemes exemptions

1. Some intra-group and restructuring transactions are exempted, under which:

- transactions between companies in the same group within the meaning of article L.233-3 of the French Commercial Code;
- transactions between companies in a French tax consolidated group (article 223 A of the French tax code); and
- transfer of ownership resulting from a merger, a contribution or a spin-off made under the provisions of article 210 A and 210 B of the French Tax Code.

New!

Final Guidelines: position of the tax authorities

The Final Guidelines importantly specify that the exemptions may be granted to any company fulfilling these criteria, irrespective of its place of establishment (no. 31).

2. Under certain conditions, the acquisition of equity securities in the context of employee savings regimes may also be exempted. Foreign employees savings regimes which are similar to those set up under the French legislation might benefit from that exemption.

G. Non-cumulative application of the registration duties and of the FTT

It should be noted that transactions which are effectively taxed under the French FTT, are not subject to registration duties set forth under Article 726 of the FTC. As a consequence if a FTT exemption applies, registration duties should be considered.

↳ **From a practical perspective, accountable parties (i.e. the accountable parties) will have to request the relevant information from their clients in order to apply an exemption. The exempted transactions will have to be recognized in the systems as they will have to be reported.**

IV. Computation of the taxable basis in respect of intra-day transactions and SRD transactions

Final Guidelines: position of the tax authorities

The Final Guidelines clarify the methodology required to compute the taxable basis in the context of intra-day/intra-month positions.

With respect to each single security, the accountable party will have to compute the net buying position by the end of the day (or by the end of the period if processed under the SRD) for the transactions carried out for each of its clients and for its own account.

The computation of the net buying position does not include the exempted transactions or the disposals realized in the course of the exempt activities (primary market, market making etc.). These transactions have therefore to be excluded for the computation of the net buying position.

The accountable party then adds together the net positions in respect of (i) transactions carried out for third parties and (ii) those transactions undertaken on its own account.

The Guidelines include an example of a computation.

V. Tax rate applicable

New!

Second Amended Finance Bill for 2012: amendment

The Second Amended Finance Law for 2012 has doubled the FTT tax rate to **0.2%**.

The bill provides for the application of this rate before the publication of the law i.e. as from 1 August 2012.

VI. VAT

New!

Final Guidelines: position of the tax authorities

The tax authorities confirmed that the re invoicing of the tax to the end investor is not subject to VAT (no. 81).

VII. The accountable party: the investment service provider or securities account holder

The law provides that the FTT shall be assessed and paid by:

- the operator providing investment services (the broker in most of the cases) as defined in Article L.321-1 of the French Monetary and Financial Code, which has executed the order to buy the securities or has traded in the securities for its own account, regardless of location; or
- the institution acting as the securities account holder of the investor, as defined in paragraph 1 of Article L.321-2 of the French Monetary and Financial Code, when the acquisition is executed without the involvement of an investment service provider (this is the case in most over-the-counter (OTC) transactions).

New!

Second Amended Finance Bill for 2012: amendment

The Second Amended Finance Bill for 2012 provides that when several operators are involved in the execution of a purchase order, the tax is assessed and paid by the one receiving directly the purchase order from the final investor.

New!

Final Guidelines: position of the tax authorities

The Final Guidelines provide that intermediaries receiving orders from clients and transmitting orders for their execution to another party shall be considered as accountable parties unless they are not authorized to execute orders within the meaning of article L.321-1 of the French Monetary and Financial Code

The Guidelines provide that ISP transmitting orders for their own account for their execution to another ISP shall be regarded as the accountable parties.

✚ **The identification of the accountable party has to be construed for each type of transaction and is obviously key to define the role and obligations of all the parties involved. This is particularly relevant in broker to broker transactions.**

Final Guidelines: position of the tax authorities

When the security account holder is the accountable party, the Guidelines specify that it has to require the necessary information from the purchaser for the purpose of the computation of the tax. Should such information not be provided, the acquisitions will be deemed to be taxable.

✚ **The French Tax Authorities have indicated that the end investor does not qualify as the accountable party. Only the service provider will be audited by the French Tax Authorities. Appropriate documentation shall therefore be retained by the ISP.**

VIII. Taxable event: exception in respect of the entry into force date

New option available in relation to the date on which the transfer of ownership occurs (i.e., the taxable event)

New!

Final Guidelines: position of the tax authorities

The accountable party may elect for taking into account the theoretical date of settlement (transactions on the market) or the date of settlement as agreed upon by the parties (OTC trades) and ignoring the possible pending operations which may postpone the actual settlement (no. 47).

Under the standard process, the tax is collected by Euroclear France before the 5th of the month following the acquisition (i.e. 5th January 2013 for taxable acquisitions undertaken in December 2012).

An interim schedule of declaration and payment is provided to enable operators to adapt their systems. Tax relating to acquisitions that occur between 1st August 2012 and 31st October 2012 will have to be declared to Euroclear France and paid before 10th November 2012.

Final Guidelines: position of the tax authorities

By way of exception, the Final Guidelines confirm that the FTT will only be due in respect of the transactions traded as from 1st August 2012 (and therefore settled in most cases as from 3rd August 2012) on the condition that the transfer of ownership occurs less than 4 working days after the trade date.

IX. Compensation of Euroclear France: additional remuneration

Tax collected by Euroclear France (before the 5th of the month following the acquisition in most of the cases) will be kept in a segregated account held with a deposit bank, in the name of Euroclear France.

This account will be exclusively used to collect the FTT. Euroclear France will then have to pay the tax due to the French Treasury before the 25th of the month following the acquisition.

✚ **According to Euroclear France, interest income generated in respect of the tax collected may not cover all of the costs incurred. Additional fees may therefore be charged by Euroclear France.**

X. Enforceability of the tax outside France

We have to note that there is some uncertainty on the legal grounds on which the French tax authorities can collect the tax due by non-French resident accountable person. It may be worth checking whether the tax can be enforced based on the existing agreement concluded between France and the country of residence of the accountable party and whether a specific new agreement will be required.

The way forward

In the light of the rules set forth above, all the accountable parties and other affected persons (including the end investors), involved in trades on French listed securities or certificates representing French shares will have to organize:

↳ **the impact assessment phase:** this assessment phase will consist of:


- the identification of the relevant business lines and desks, as the case may be, that would be impacted by the FTT (the impact in respect of French registration duties may also be included in the analysis)
- the determination of the roles of the entities involved in the trading on eligible securities (e.g. accountable parties, end investors, custodians, Euroclear members, clearing houses, other intermediaries involved in the information and tax returns chain) and their related obligations (reporting, payment, filing the returns, transmitting the returns, sending the information in relation to the transactions,...)
- the identification of the treatment applicable to the transactions on eligible securities and the applicable exemptions as the case may be (including the organization of the relevant documentation to sustain the exemptions)
- the determination whether it is advisable to elect for any of the available options, when relevant
- the review of the relevant legal documentation and customer terms and conditions
- the IT organization and the gap analysis

↳ **the operational implementation phase:** this implementation phase will consist of:

- the modification of the IT systems and procedures in order to organize the filing and transfer of the tax returns and the payment of the tax, depending upon the role of the entities involved in the chain. The structure shall be flexible in the sense that it shall be easily modified to take into account any change in the rate/scope of the tax or applicable exemptions
- the enhancement of the interfaces and links with relevant payment infrastructure and of the control infrastructure
- the adjustment of adequate accounting, financial and regulatory reporting (particularly in respect of client invoicing)
- the adjustment of the relevant legal documentation which would in particular cover the recharge of the FTT, the organization and impact of the reassessments as the case may be and the organization of the information/tax returns chains and related liabilities
- the preparation of the transactions mapping to benefit from the exemptions and related documentation
- the preparation of option letters to be sent, if relevant
- the preparation of the client communications, taking into account local law constraints.

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