

# Tax treatments in France

Hervé Ballone explains the tax treatment of the debt waiver granted by a mother company to its subsidiary having financial difficulties in France



**HERVÉ BALLONE**  
Insolvency and Bankruptcy Officer,  
Official Liquidator office in France

**A** company might, in certain circumstances, voluntarily waive its debt owed to a client, hence the term “debt waiver”. This particular act is regularly used when the company is in difficulty and is unable to face repayment of its debts with the flows generated by its economic assets.

This type of operation occurs *ipso facto* tax implications, which depend on the nature and circumstances of the waived debt. Indeed, the waiver may have:

- a commercial nature: the waiver permits to continue business opportunities or to preserve sources of supply,
- a financial nature: the waiver is justified within a group, between a parent company and one of its subsidiaries.

Where the debt waiver has both a commercial and a financial nature, it must be determined if the commerciality is predominant. If so, the waiver is commercial, if not, it is financial.

Provided that the waiver comes from a normal management, a commercial debt waiver is taxable at the level of the beneficiary and deductible at the level of the mother company.

Regarding the financial debt waiver, the tax treatment is different at the level of the mother company from the one at the level of the subsidiary.

## Tax treatment of the financial debt waiver at the level of the mother company

According to the Law dated 16/08/2012, the company which

grants a debt waiver can no longer deduct it. However, the Law allows a partial deductibility of the debt waiver granted to a subsidiary under a “*procédure de sauvegarde*” (safeguard proceedings), “*redressement judiciaire*” (judicial restructuring) or liquidation proceeding, and during a conciliation procedure (Law dated 29/12/2012) or approved under the provisions of Article L 611-8 of the Commercial Code.

The administration extends this measure to debt waivers granted within the framework of insolvency proceedings mentioned in Schedule A of the EU Regulation 1346/2000 dated 25 May 2000.

The debt waiver remains deductible up to the negative net worth of the subsidiary and its positive equity in proportion to the holdings of the other shareholders. The net position is equal to the amount of equity (art. 434-1 of the Plan Comptable Général) after deduction of settlement expenses.

Thus, three scenarios are possible when the beneficiary of the said debt waiver is subject to one of the above proceedings.

### 1. There is a net position before and after the waiver: the waiver is fully deductible

For example: *Company A* owns 100% of the shares in *Company B*, which is under safeguard proceedings: *Company A* grants a €50,000 debt waiver to *Company B*.

Net equity before the waiver: –€100,000; Net equity after the waiver –€50,000

### 2. The negative net position becomes positive after the debt waiver: the waiver is deductible up to the amount of the negative equity before the waiver, plus the amount of the positive equity in proportion to the fraction of capital belonging to other shareholders

If the waiver is granted by a sole shareholder:

For example: *Company A* holds 80% of the shares in *Company B*, which is under restructuring. *Company A* grants a €180,000 debt waiver to *Company B*.

Net equity before the waiver: –€150,000; Net equity after the waiver: €30,000.

Thus, the amount of the deductible debt waiver is €156,000: 150,000 + (30,000 x 20%).

If the waiver is granted by two shareholders:

For example: *Company A* and *Company B* hold respectively 30% and 20% of the shares of the company *Company C*, which is under restructuring – the shareholders respectively grant a debt waiver of €300,000 and €200,000.

Net equity before the waiver: –€400,000; Net equity after the waiver: €100,000.

Thus, the amount of the deductible debt waiver is €450,000:

€270,000 (400,000 x 300,000/500,000 = 240,000 + (300,000 - 240,000) x 50% = 30,000); €180,000 (400,000 x 200,000/500,000 = 160,000 + (200,000 - 160,000) x 50% = 20,000)

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**3. The net position is positive before and after the debt waiver: the waiver is deductible up to the shares held by the other shareholders**

*If the waiver is granted by a sole shareholder:*

For example: *Company A* holds 80% of the shares in *Company B*, which is under safeguard proceedings: *Company A* grants a €80,000 debt waiver to *Company B*.

Net equity before the waiver: €50,000; Net equity after the waiver: €130,000.

Thus, the amount of the deductible debt waiver is €16,000 (80,000 x 20%)

*If the waiver is granted by two shareholders:*

For example: *Company A* and *Company B* hold respectively 30% and 20% of the shares of the company *Company C*, which is under restructuring. The shareholders respectively grant a debt waiver of €100,000 and €50,000.

Net equity before the waiver: €80,000; Net equity after the waiver: €230,000.

Thus, the amount of the deductible debt waiver is €750,000:

€50,000 (100,000 x 50%) + €25,000 (50,000 x 50%).

**Tax treatment of the financial debt waiver at the level of the subsidiary**

In principle, the debt waiver is taxable at the level of the subsidiary. As an exception (art 216A of the French Tax Code), where the beneficiary of the debt waiver is subject to corporation tax, the fraction of the non-deductible waiver for the mother company who has granted it, is not taxable at the level of the subsidiary, provided that the following conditions are met:

- the subsidiary commits to increase its capital in favour of the mother company for an amount equivalent to the debt waiver granted by the end of

the second year following the year of the waiver (eg. by 31/12/2013, if the waiver is granted during the year ended at 31/12/2011)

- the waiver is granted by a mother company in the meaning of the article 145 of the French tax Code.

In case of breach of the above commitment, the debtor company must reintegrate the amount of the waiver granted to the taxable income of the year in which it has been granted. ■



**A COMMERCIAL DEBT WAIVER IS TAXABLE AT THE LEVEL OF THE BENEFICIARY AND DEDUCTIBLE AT THE LEVEL OF THE MOTHER COMPANY**

