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REAL ESTATE NEWSLETTER

Dossier on

Construction and reconstruction

Recent developments

Editorial

Recent evolutions in law and tax related matters testify undoubtedly to the desire to encourage the densification of urban areas and the modernisation of existing real estate stocks, which is consistent with the modernisation, reconversion and densification approach applied in respect of a great many sites in the Ile-de-France region, such as those activities currently under conversion into service industry activities.
However, beyond the basic objectives put forth by statutes, practitioners are confronted, in the context of the implementation of a project, with a great many issues in terms of planning law, property law and tax law. For each instance, a detailed examination of the building’s history and of the precise nature of the works contemplated will prove decisive.
Thus in the field of planning law, works on existing buildings or the reconstruction of buildings implies that one scrutinizes all of the authorisations that have been issued, as well as the surveys-steps yet to be accomplished in order to carry out the contemplated project to a successful end. However buildings which have been unlawfully built or converted are not uncommon. In this context, a review of the situation regarding the most recent evolutions in terms of the law and case law which concern them seems particularly appropriate.
The major features of the most recent reform of planning law whose objective is to put an end to the regulatory planning approach in order to replace it with a project orientated planning approach also deserves to be mentioned; indeed they clearly display the objective of facilitating building operations.
If this recent tax and legal regime specific to sales of renovated buildings comes in response to a great many expectations, it remains that the determination of its precise scope of application is not always as straightforward as one might imagine, hence the brief panorama regarding the provisions concerned.
The provisions of the mandatory statute governing commercial leases which govern the case scenario of a construction or reconstruction lead to a questioning of the strategy that landlords should adopt in such case scenarios.
The building lease for its part will enable constructions without being the owner of the land.
However the legal and tax rules that are applicable to this instrument must be revisited in light of new practices: upgradeable buildings, versatile land.
The picture as regards construction-reconstruction operations would not be complete without examining the main aspects of direct taxation: in particular the treatment of demolition and rubble clearance expenses, as well as construction profits, in consideration of their accounting regime.
Finally, the chronology of the stages of a construction-reconstruction operation is not neutral from the standpoint of local taxes. Are thus placed out before you the pieces of the legal and tax puzzle. We hope you will enjoy piecing them together. ▪

Jean-Luc Tixier, Partner

Major refurbishments: consequences on local taxes

By **Cathy Goarant-Moraglia***, tax partner, focusing on the management of local taxes encumbering real estate programs, as well on major refurbishment operations or marketing processes. She also conducts assignments related to due diligence, assistance, technical consultancy and defence of undertakings in all business sectors.*
cathy.goarant@cms-bfl.com

and **Laurent Chatel***, tax partner. He heads the local tax department of CMS Bureau Francis Lefebvre. Within the framework of real estate transactions he checks the land and property values retained as a basis for local taxation, audits said values within the framework of deals for the sale of real estate stocks, and negotiates with the tax authorities the terms of liability under local tax within the framework of major refurbishment operations.*
laurent.chatel@cms-bfl.com

The more or less extensive renovation of buildings has formed over recent years a significant part of real estate operations and raises a certain amount of questions on the part of operators regarding its consequences on local taxation liabilities attaching to the buildings concerned.

If the question regarding liability to business tax and now to CFE remains ancillary as it implies that the building be occupied for the exercise of a professional activity, the renovation of buildings generates genuine queries in respect of local taxes affecting the very existence of the property and its use.

Thus within the framework of major renovation projects on premises spreading out over several years and of such extent that they can be analysed as full demolitions followed by a reconstruction, it is possible to solicit the taxation of the land exclusively under real estate tax on non-developed property (which is inferior to real estate tax on developed property) during the period of the works. One should then inform the relevant real estate tax office by filing an IL tax return form reporting the demolition.

"The renovation of buildings generates genuine queries in respect of local taxes affecting the very existence of the property and its use"

Having regard to the annual principle of taxation, it is important to establish evidence of the demolitions prior to the 1st of January of the year in respect of which the action is conducted. This element will be used as documentary evidence to be attached to the IL demolition return to be sent to the tax services.

At completion of the works, new constructions, reconstructions and additional constructions will be exempted from real estate tax on developed property during the first two years following that of their completion. For buildings which are not assigned to housing, this exemption is limited to the county fraction (*part départementale*). The exemption is total for residential use buildings, save a decision to the contrary of the *commune* or of their groups accordingly to the fraction of taxation which falls to them.

The benefit of this exemption is subordinated to the condition that the new constructions, as well as changes of consistency or assigned use are brought to the attention of the administrative authorities within 90 days from their definitive execution. In the event of untimely declaration, the exemption will apply for the period remaining after the 31 December of the following year. As concerns partial completions, the *Conseil d'Etat* has considered that the various parts of a same building can be considered at successive dates, when they can be used separately. It results that in the event of completions at successive dates, the return requirement under article 1406 of the Tax Code applies as per fraction of property completed.

Moreover as concerns the annual tax on office, commercial and storage premises and parking spaces in the Ile-de-France region, the latter will not be due if the property complex can be considered as having been the subject of a demolition. On the other hand, the administrative court of appeals of Paris has ruled on several occasions that the taxation will prevail where the building remains taxed under real estate tax on developed property even where it has become unusable on account of

the works (along these lines, CAA of Paris, 7 June 2007, no. 05PA02494, *Cie Foncière Parisienne*).

The management of the local taxes related to refurbished buildings therefore implies meticulous monitoring of the various return requirements, as well as treatment on a "case by case basis" having regard to the factual and legal specificities of each real estate operation. One should, moreover, take into account both the forthcoming reform of real estate valuations for 2014 and novelties in terms of planning matters. ■

Sales of buildings for renovation

By **Jean-Luc Tixier,** *partner, specialized in real estate law and public law. He provides advisory services to a great many commercial and industrial corporations, as well as property developers in matters of planning, construction, sales and rentals of buildings, long-term leaseholds and building leases. He lectures at Paris University (Paris I).*
jean-luc.tixier@cms-bfl.com

and **Philippe Tournès**, *partner, specialised in VAT issues, and in particular with respect to real estate matters.*
philippe.tournes@cms-bfl.com

Since late 2008, a legal regime specific to sales of buildings for renovation (Vente d'immeuble à rénover or VIR) (articles L262-1 et seq. and R 262-1 et seq. of the Construction and Housing Code), of public order, is applicable to any vendor of all or part of a developed building for a residential use (or for a mixed professional/residential use), who covenants within a period determined by contract to carry out works on the building, directly or indirectly and who receives sums of money from the purchaser prior to the delivery of the works.

Extension or full refurbishment works of a building, which can be assimilated to a reconstruction, do not come under the regime of the VIR but that of a Sale off plans (VEFA) (article L262-1, subparagraph 3). What are concerned are those works which make brand new (article R262-1):
- either the majority of the foundations;
- or the majority of non-foundation elements determining the resistance and rigidity of the development;
- or the majority of the consistency of the façades excluding façade renovation;
- or all elements of the following second fixings, in a proportion at least equal to two thirds for each of them: floors which do not determine the resistance or the rigidity of the development, external window and door frames, interior partitions, bathroom and plumbing facilities, electrical installations, heating system (for operations carried out in Metropolitan France).

The preliminary contract in the context of a VIR is a genuine sale and purchase or call option agreement which is subject to standard rules generally applicable (article L262-1 of the Construction and Housing Code). The regime of the VIR is closely inspired by that of the VEFA in the protected sector: immediate transfer of the proprietary rights to the soil and of title to existing constructions, supply of a financial completion guarantee…

The price must draw a distinction between existing structures at the date of the sale, paid at signature, and the works to be carried out by the vendor.
The sum of payments related to the price of the works, which can give rise to interim progress payments, can not exceed (article R262-10):
- 50% once completed of the works representing half the total price of the works;
- 95% once completed of all the works;
- the balance is payable at delivery, save non-conformities or apparent defects mentioned in the minutes of delivery.

It is interesting to note that the criteria that the legislator has adopted in terms of civil law, to distinguish the VIR from the VEFA, are the same as those which appear under article 257 of the Tax Code, which enable a distinction between the sale of brand new buildings, liable as of right under VAT, and sales of used pre-existing properties in principle exempted from VAT (but which can be subject to such tax upon exercise by the vendor of an option).

The regime of sales of buildings for renovation raises however issues of a certain complexity in matters of VAT.

"The VIR regime is closely inspired by that of the VEFA in the protected sector."

First of all, can one consider to any degree of certainty that each time that a VEFA contract is entered into, VAT applies and that each time that a VIR is entered into the sale does not come under the scope of VAT (save vendor's option)? It is true that when a VIR contract is entered into, VAT does not apply as of right to the sale of the building, the latter always being deemed as a used pre-existing building. On the other hand, on account of the interpretation by the tax authorities in its circular of 29 December 2010 (3A-9-10), certain sales entered into in the form of a VEFA shall not come under the scope of VAT.

Indeed, in these guidelines, the tax authorities specified that even if two thirds of the second fixings of a building are redone within the meaning of article 257, the latter shall not be deemed as brand new in the case scenario where, on the one hand, the works are invoiced at 19.6% by the contractors and where, on the other hand, the floors determine the resistance or the rigidity of the development.

Secondly, where all of the existing second fixings are not purely and simply replaced by new elements, according to what criteria is this two thirds proportion appraised? The tax authorities made do with specifying that the project owner (maître d'ouvrage) can retain any method that he can justify the relevance of… we will need to wait for the courts to express a position regarding this issue.■

Termination notice for the purpose of construction or reconstruction: practical aspects

By **Sandra Kabla***, lawyer specialized in commercial leases. She provides litigation, advisory, drafting and contractual negotiating services in the various fields of real estate and more specifically in the field of commercial lease litigation, for a client base of end user corporations and investors.*
sandra.kabla@cms-bfl.com

Article L145-18 of the Commercial Code combined with article L145-4, subparagraph 2 of the same Code affords landlords with the possibility to repossess the premises, either on the expiry of a triennial period, or at the end of the lease, when he has the intention of building or of rebuilding the existing property. The landlord will then have to pay an eviction indemnity or offer-up a set of replacement premises to the evicted tenant. The replacement premises must correspond to the needs and to the possibilities of the tenant at the date of the refusal to renew or of the notice to terminate, which excludes the case where the offer concerns the premises that the landlord purports to build. The notice must comply with the formalities of article L145-9 of the Commercial Code. It must specify the reasons for which it is served and duplicate in principle the last subparagraph of this article.

A termination notice for the purpose of building implies that the rental applies not only to a building but also to a piece of building land; in this case, the demolition of the developed area would not be necessary. The landlord therefore has two solutions: either to leave the tenant in place if this does not hinder the performance of the construction works, or to evict the latter, paying an indemnity.

A termination notice for the purpose of rebuilding implies prior demolitions. The landlord must consequently be the owner of the constructions whose demolition is contemplated. Thus, repossession can not be exercised by the owner of the bare rented land on which the tenant has developed constructions. In addition, the reconstruction has to apply to the totality of the building or buildings forming the subject matter of the lease (*Cour de cassation*, Commercial Chamber, 19 January 1960, Bull. Civ., no.27).

"The main interest of a notice to terminate for the purpose of rebuilding lies in the possibility for the landlord to serve notice to terminate for the expiry of a triennial period."

The landlord must have, at the date of the notice, the intention to demolish himself the building for the purpose of rebuilding (*Cour de cassation*, 3rd civil chamber, 12 July 1995 Jurisdata no.003361). However, it has recently been judged that a landlord can validly deliver a notice for the purpose of building or rebuilding even if he does not proceed with the construction or reconstruction operations, but that he does so indirectly through the agency of a company that he is the managing partner of (*Cour de cassation*, 3rd civil chamber, 14 September 2010 Jurisdata no.2010-021517).

In any event, case law considers that the landlord's statement of repossession is presumed to be sincere (*Cour de cassation*, Commercial Chamber, 23 February 1953, Bull. Civ. III, no.80). The latter is therefore not under the obligation to file a demolition permit or planning permission application before serving notice to terminate. He does not either have to say why he is rebuilding. It will then be up to the evicted tenant to produce evidence supporting his claim for the cancellation of the notice. In the event of contestation of the notice by the tenant, the implementation of the construction project can be substantially delayed, having regard to the length of the proceedings that can follow and to the tenant's remaining within the premises throughout the duration of these proceedings. In conclusion, the main interest of a notice to terminate for the purpose of rebuilding lies in the possibility for the landlord to serve notice to terminate for the expiry of a triennial period and to thus elude the contractual term of the lease. As a consequence, if the landlord is considering, at the end of the lease, reclaiming the premises rented in view of carrying out construction or reconstruction works, his best interest would be not to invoke the benefit of the provisions of article L145-18 of the Commercial Code and to serve notice to terminate with a refusal to renew and an offer of an eviction indemnity, notice which need not be reasoned, contrarily as for the notice contemplated by article L145-18 of the Commercial Code, being specified that, in both cases, the landlord is liable for an eviction indemnity.

Tax treatment of construction-reconstruction operations in terms of direct taxation

*By **Richard Foissac**, partner, specialized in tax matters. He deals in particular with acquisitions and restructuring of listed and unlisted real estate groups and provides advisory services in the context of their transactions. He lectures in tax law at the Universities of Paris I and Nice Sophia-Antipolis.*
richard.foissac@cms-bfl.com

Expenditure related to the construction of buildings does not constitute an immediately deductible expense for enterprises carrying these out, as they have as due consideration an increase of assets. The amount thereof must be included under fixed assets or inventories, depending on the nature of the activity carried on by the enterprise.

Where the enterprise is induced to have to proceed with the destruction of buildings that it owns, in view of a reconstruction, the resulting tax consequences will differ depending on the initial assigned use of the building destroyed and of the nature of the works carried out.

Several case scenarios must thus be distinguished.

When the building to be destroyed was purchased specifically in view of being demolished and is replaced by a new construction, it is considered both by administrative case law and by the administrative authorities, that the purchase and the demolition then constitute two parts of a single project. It results that the purchase price of the building to be destroyed and the demolition expenses constitute a component of the cost price of the new building and must, to this extent, be depreciated on the same terms as this cost price (along this line, in particular see Conseil d'Etat, 4 May 1977, no. 2136 and 2137, 8th and 9th sub-sections: RJF 7/77 no.383; D. adm. 4 C-2111 no.23, 30 October 1997).

"The tax consequences of the destruction of buildings are different depending on the initial assigned use of the building destroyed and on the nature of the works carried out."

When on the other hand, the building to be demolished is already in the assets of the enterprise and that the latter decides to develop in its place new constructions, the residual accounting value of the building destroyed constitutes, according to the Conseil d'Etat (ruling of 16 July 1999, no. 177954), a deductible loss of the taxable income of the enterprise for the financial year during which the demolition occurred.

This decision invalidated the administrative guidelines according to which the residual value of the building destroyed constitutes a component of the cost price of the land.

However this case law does not apply in the case where it can be established that the acquisition of the building destroyed was only carried out with the sole purpose of developing subsequently to its demolition, on the land base, a new construction, into the cost price of which would then have to be incorporated the value of the former building.

This was thus held by the Conseil d'Etat, in the case of a company which had acquired a property complex for a hotel use and had immediately elaborated a renovation and extension project involving the demolition of part of the buildings concerned, although at the time of the demolition, the hotel had been operated on an "as was" basis during two seasons (see Conseil d'Etat, 5 May 2008, no. 290382 and 290383, 10th and 9th sub-sections, Vinales).

A distinction must moreover be drawn between the tax treatment of the cost price of the demolished property and that of the demolition and rubble clearance expenses.

The latter expenses, indeed, do not constitute a deductible expense, but are analysed most often as a component of the cost price of the new building developed, and thus even where the demolition is not decided by the enterprise but is imposed upon it, as for instance further to a damaging event.

The Conseil d'Etat has even ruled in certain situations, that the demolition expenses of a building could contribute to an increase in the value of the land base where the latter was intended to be used as bare land, considering that the expenses in question were to be incorporated into the cost price of the land (ruling of 6 November 1985 no.47800 having addressed the situation of a company operating a department store which had demolished various buildings which were timeworn and fully depreciated on a neighbouring piece of land, in view of the construction of a car park intended to improve customer access and having considered that the demolition expenses were supported by due consideration as per the increase of the land's value). ■

Panorama of law and tax liabilities pertaining to building leases

By **Jean-Luc Tixier,** partner, specialized in real estate law and public law.
jean-luc.tixier@cms-bfl.com

Gaëtan Berger-Picq, partner specialised in VAT issues, and in particular with respect to real estate matters.
gaetan.berger-picq@cms-bfl.com

and **Agnès Rivière-Durieux**, tax lawyer specialising on issues of income tax and corporate income tax related in particular to real estate.
agnes.riviere@cms-bfl.com

The building lease should enable, and should be binding on this point, in a material respect, a party to build on a piece of land without being the owner of such land. In a great many projects, where the landlord would like to be able to force its tenant to carry out a partial development or light renovation works, this will not be the right instrument, without, for all that, it being possible to resort to a long term leasehold. The legal device of the building lease was combined, right from its creation in 1964, with tax rules which were designed to be favourable and to encourage construction; over time the legal specificities of the building lease have come to light, and the operations that are likely to occur during the course of the contract have appeared: additional constructions, whether contractual or not, termination, extension and assignments in a concomitant manner of their rights by the landlord and the tenant.
However, in a certain number of case scenarios, the original character of the legal situation has not always been echoed from a tax standpoint, and the tax solution applicable neutralizes to a certain extent the interest or the consequences of the solutions considered as legally conceivable.
The table attached itemizes some of the main legal and tax rules applicable to this contract. ■

	Définition	Term extension	Assignment sub-rental	Price of the lease	Assignment of rights/termination	Outcome of the lease
Legal	Article L251-1 1° of the Housing and Construction Code (CCH) A building lease is a lease by virtue of which the tenant covenants, in a principal respect, to erect constructions on the landlord's land. The obligation to build/fit-out is decisive as to the qualification (≠ with the long term leasehold). The erection of new constructions can be subject to the landlord's prior authorisation. This lease confers an *in rem* right over the building. The tenant holds on this account an extremely extensive right of use and enjoyment. However in the absence of provisions of public order regarding the intended use of the constructions erected, the building lease can impose restrictions on the activities carried on within the building. If the lease does not provide an obligation to build, or if it deprives the tenant of material prerogatives, it will be disqualified.	Article L251 Minimum term of 18 years and can not exceed 99 years. Extension via tacit continuation is impossible. However, extensions agreed by mutual consent in the initial contract or prior to the expiry of the lease are possible. The contract can not make provision for any close-out before its outcome, such as a triennial termination right. The necessity as to new constructions or improvements to the initial constructions carried out by the tenant to justify such an extension is still under debate. The extension of a building lease for several years in consideration for a substantial increase of the rent shall not necessarily operate novation of the building lease into a standard lease.	Article L251-3 3° of the CCH. Free assignment of the lease. This liberty must be total and unrestricted. This principle is of public order. Article L251-3 and article L251-6 of the CCH. Free sub-rental of the constructions. This liberty must be total and unrestricted. Any clause related to the control of assignments of the rights to the lease or of any sub-rental by the tenant shall disqualify the building lease, and transform it into an ordinary lease or into a commercial lease.	The price of the lease shall essentially take the following forms: - payment of periodic rent in a cash payment (Article L251-5, subparagraph 2 of the CCH) or not; - surrender of the constructions to the landlord during the course of the lease (Article L251-5, subparagraph 1 of the CCH) - surrender in an ancillary respect of the constructions to the landlord on a piece of land other than that under rental; - surrender of the constructions to the landlord, with or without compensation, at the end of the lease (Article L251-2 of the CCH)	The building lease can come to an end further to the acquisition of the land base by the tenant during the lease; in this case, the acquisition will operate extinguishment of the lease by concurrent holding of both capacities. An as of right termination clause in favour of the landlord in the event of failure to pay the rent confers the tenant's enjoyment with a precarious character which is incompatible with this type of lease. The termination of the lease will grant the landlord access to the ownership of the developed buildings prior to the expiry of the lease (*Cour de cassation*, Commercial Chamber, 24 June 1997, n°95-13 038, SIC Agnel-Teissonnière)	Failing an agreement, the landlord shall become the owner at the end of the lease of the constructions developed and shall profit from the improvements (article L251-2 of the CCH). Non contractual additional constructions can, depending on the case, give rise to compensation. The building lease can also come to an end via the definitive acquisition of title to the land by the tenant (a "retro building lease"). The building lease would then be coupled with a clause contemplating the transfer of title to the land in favour of the tenant in consideration for an additional rent, as a price of assignment of the land.
VAT			In the event of sub-rental of the constructions, the VAT regime will depend on various parameters. Broadly speaking, rentals applying to equipped premises are in principle taxable as of right under VAT, whereas rentals of bare premises are exempted, save exceptions (article 261 D of the Tax Code). Rentals of professional premises which are exempted can moreover be the subject of voluntary taxation upon option exercised by the landlord (article 260, 2° of the Tax Code).	The cash rent and the surrender value of the constructions at the end of the lease are in principle exempted from VAT (article 261 D, 1° bis of the Tax Code). Taxation upon exercise of an option is nevertheless possible (landlord's choice expressed in the building lease agreement) by operation of article 260, 5° of the Tax Code. In the event of such taxation, VAT will be based: - on the amount of the rent in cash/payable at the time of their encashment; - on the value of the constructions that will be surrendered at the end of the lease, after deduction of the possible compensation due by the landlord to the tenant payable in this respect at the time of conclusion of the building lease.	The assignment of the rights of the landlord or of the tenant under a building lease is assimilated to that of the building to which the building lease applies (article 257 I-1, 1° of the Tax Code). It results that: - where the assignment takes place within five years from the completion of the building, it will be taxed as of right under VAT; - where the assignment takes place after the expiry of this period of five years, it is in principle exempted, save the assignor's option for voluntary taxation. The termination will entail a transfer of the constructions in favour of the landlord, taxed as such (taxation if the constructions have been completed for five years at most, exemption, save option, in the contrary case).	The surrender of the constructions contemplated by the building lease does not entail taxation under VAT, as it is caught right from the conclusion of the lease (exemption save landlord's option for voluntary taxation).The surrender of additional constructions, which are not contractual, must be treated as an ordinary assignment (taxation if the constructions have been completed for five years at most, exemption, save option, in the contrary case). In the event of assignment of the land to the tenant contemplated by an unconditional clause of the building lease, the transfer will be taxed like that of the building, depending on the period that has lapsed since the completion of the constructions. In the event of a mere promise, the building lease will be treated as such and the transfer will be taxed according to the situation of the building at the time at which such occurs.

Direct tax (excluding CET)		Date of taxation of the additional rent resulting from the gratuitous surrender of the constructions erected by the tenant in the event of extension of the lease: - for the administrative authorities: in respect of the year of expiry initially contemplated save extension for economic reasons; - for the *Conseil d'Etat*: in respect of the financial year or of the year of the new term (CE 26/01/2006 n°271523)	Taxation of the income drawn from sub-rentals granted: -by an individual: income tax, category of property income; - by an individual entrepreneur having entered the constructions into his/its assets: income tax, category of commercial and industrial profits (the rule should change in 2012 further to the cancellation of the balance sheet theory); - by a company liable to corporate income tax: taxation at the standard rate.	Tax applicable and category of income depending on the landlord's status: the same applies to income from sub-rentals. Connection of the income represented by the value of the constructions surrendered during or at the end of the lease: upon request, apportionment over the year or the financial year of surrender of the asset and the following 14 years. Valuation of the income represented by the value of the constructions: cost price. For the exemption applicable to the surrender at the end of the lease: see last column.	In the event of assignment of the land to the tenant prior to the expiry of the lease, case law considers that the sale produces, from a tax standpoint, the same effects as a voluntary termination of the lease entailing the surrender of the constructions to the landlord and the taxation of the corresponding profits (the same applies in the event of contribution of the land to the tenant and the takeover of the landlord by the tenant or of assignment by the landlord and the tenant to a third party of their respective rights). Apart from these cases, the assignment of the rights of the landlord or of the tenant will bring out a capital gain which is taxable under the regime applicable to the assignor.	The surrender of the constructions shall not give rise to any taxation where the term of the lease is at least equal to 30 Years. If the term of the lease is inferior to this, application to the cost price of the constructions of a discount of 8% per year of the lease beyond the 18th year. Where the building lease includes a clause contemplating the transfer of the land to the tenant at the end of the lease, the capital gains realized by a landlord who is an individual will be determined and taxed according to specific rules (article 151 quarter of the Tax Code); for enterprises, according to standard rules.

Construction profits: an incomplete tax framework

By **Frédéric Gerner***, lawyer, specializing in tax law. He provides both advisory and litigation services with regard to issues related to direct taxation, in particular in connection with intra-group restructuring and real estate.*
frederic.gerner@cms-bfl.com

The catchment of construction profits continues to present various specificities which need to be taken into careful consideration by the enterprises concerned. Traditionally the results of operations for the construction and sale of buildings are apprehended from an accounting standpoint at delivery of the buildings, including in the case where they are sold off plans, on account in particular of the deemed contingent character of profits in connection with the construction of a building. The same applies for the determination of taxable income by application of the provisions of article 38-2 bis of the Tax Code, according to which the proceeds corresponding to trade account receivables or to payments received in advance in payment of the price are connected to the financial year of delivery of the assets or of completion of the services.

However, in reference to the standards applicable in matters of consolidated accounts, and where they are transposed into the corporate accounts, certain operators apprehend from an accounting standpoint the results from building construction operations according to the percentage-of-completion method, that is to say progressively, even before the buildings considered are completed and definitively delivered – method which is not taken into account by tax laws.

To avoid in this type of situation, a distortion between accounting treatment and tax treatment, which is a source of complexity and uncertainty, the tax authorities have allowed the application of the percentage-of-completion method from a tax standpoint to contractors' works carried out by contractors in the public works and building sectors (BTP). The latter, normally only required to declare the income drawn from their activity at the date of provisional acceptance (whether complete or partial) of the development, can opt to tax each year the progress payments which have become payable, such as they appear on the works progress statements sent to clients (see administrative document 4A 2531 n°14, 9 march 2011). This authorises them, moreover, correlatively, to allocate provisions covering the decennial warranty, right from the entry of the income concerned for the fraction of risk corresponding to the work progress status (see ruling of the *Conseil d'Etat*, 13 January 2006, no.259824).

"The tax authorities have allowed the application of the percentage-of-completion method from a tax standpoint to contractors' works carried out by contractors in the public works and building sectors."

Such an option is however only contemplated for contractors in the public works and building sectors which, by definition, carry out works on properties that they do not own. It has not been clearly extended to the case of buildings sold off plans. Property developers who consider that the percentage-of-completion method better conveys the reality of their activities and of their results are thus confronted with a regrettable lack of flexibility from a tax standpoint, liable to force them to deal with two separate methods and to operate re-treatments for the determination of their taxable results both at the level of income and expenses. Under these circumstances several wishes can be expressed. First of all, it would be worthwhile for the administrative authorities to formally extend to property developers the tolerance contemplated for contractors in the public works and building sectors by offering them the possibility to choose between the legal regime of catchment of income at delivery and the alignment of tax treatment on the accounting treatment where the percentage-of-completion method has been opted for. Secondly, in a constantly evolving environment, the legal certainty of contractors would stand to gain if the accounting and tax authorities were to align their positions and to clarify the conditions, terms and consequences of the application of the percentage-of-completion method, which would satisfy the objective, often announced by the tax authorities, of avoiding to the fullest extent possible distortions between accounting and tax rules. ■

Specificities of constructions-reconstructions and planning law

*By **Céline Cloche-Dubois**, lawyer. Specialized in public law and environmental law. She provides both advisory and litigation services to corporations and public entities.*
celine.cloche-dubois@cms-bfl.com

Works on an existing building or the reconstruction of a building, subsequently for instance to a damaging event, often afford an opportunity to examine its precise legal situation and to look-into all of the authorisations which have been delivered and all of the surveys-steps to be accomplished in order to see the envisaged project through to a successful end. It is therefore important to not leave out any of the following elements.

The construction of buildings is subject to the prior delivery of a planning authorisation, planning permission or decision of no-objection against a prior declaration in the event of works of minor importance (on the terms specified by articles R421-9 et seq. of the planning code). The modification of an existing building or its reconstruction also implies the delivery of such an authorisation; ordinance no.2005-1527 of 8 December 2005 and order no.2007-18 of 5 January 2007 inserted into the planning code various provisions specific to the works carried out on existing constructions[1].

Case scenario of works on an existing building

Fate of a building developed unlawfully. A building may have no legal existence, from an administrative standpoint, if it was developed without an authorisation (or if the authorisation granted is cancelled), or if it has been developed in infringement of the latter. For the Conseil d'Etat, administrative authorities solicited by an application tending for works to be authorised for such a building, are under the obligation to ask the applicant to present an application for the whole of the building, even if these works, construed individually, conform to planning rules and do not worsen the existing situation[2].

Absence of an administrative limitation period for constructions carried out without a planning permission. In order to mitigate the effects of this case law, the legislator introduced the principle of an administrative limitation period[3], with an extremely limited scope of application. Indeed, under the terms of article L111-12 of the planning code, "where a construction has been completed for more than ten years, the refusal of planning permission or of a prior declaration of works can not be based on the unlawful character of the initial construction having regard to the law of planning. The provisions of the first subparagraph are not applicable: (…) e) Where the construction was carried out without a planning permission". Buildings for which no planning permission has been delivered (or even applied for) but also those for which the permit has been withdrawn or cancelled will therefore not be entitled to benefit from this provision.

"A building may have no legal existence, from an administrative standpoint, if it was developed without an authorisation (or if the authorisation granted is cancelled), or if it has been developed in infringement of the latter."

Slight mitigation. In a ruling dated 3 May 2011[4], the Conseil d'Etat considered that the administrative authorities had the possibility of authorising, among those works which have been applied for, those that are necessary for the preservation of the building and for compliance with standards, and thus, despite its unlawful development and the impossibility to legalize the situation having regard to applicable planning rules. However, the Supreme Court laid down two conditions. First of all, criminal or civil actions having to no longer be possible[5], the building therefore being, hypothetically speaking, relatively old; second of all, the works must be necessary to its preservation and to compliance with standards. Finally, we would note that it is not the Conseil d'Etat's intention to make this relaxation of the rules an absolute principle, leaving the relevant administrative authorities the freedom to authorise works or not depending on the various public and private interests at stake.

Case scenario of the reconstruction of an existing building

Possibility to reconstruct a building in an identical manner. Under the terms of article L111-3 of the Planning code, such as stemming from law no.2009-526 of 12 May 2009, the "reconstruction in an identical manner of a building destroyed or demolished for less than ten years will be authorised despite any planning rule to the contrary, unless the municipal plan, the local zoning plan or the plan for the prevention of foreseeable natural hazards should provide otherwise, to the extent where it was lawfully developed". Thus, any building destroyed fortuitously or voluntarily[6], can

be rebuilt, without any loss of constructability whereas applicable planning rules (local zoning plan, municipal plan, the national planning regulations…) would no longer permit this. Several conditions are however set forth: the planning document must not contain any written and/or graphic provisions of an explicit nature the purpose of which is to exclude such a right to rebuild or to define the framework of reconstruction. The initial building must moreover have been lawfully developed: a planning authorisation was required at the date of its construction, it must have therefore been developed in accordance with such authorisation, which must not have been cancelled or withdrawn. The building reconstructed must be identical to the building demolished, being specified that the administrative guidelines adopt a strict interpretation of this provision[7]. Finally, this right to reconstruct is subject to a deadline of ten years as from the demolition or destruction of the building. Of course, we would specify that the benefit of this provision of the planning code does not exempt those persons considering the reconstruction of the building from filing for and obtaining a new planning authorisation.

"Any building destroyed fortuitously or voluntarily can be rebuilt, without any loss of constructability, whereas applicable planning rules would no longer permit this."

Exemption from the "tax on the creation of office space"[8] in the event of reconstruction of an existing building. In principle and in accordance with article L520-1 of the Planning code, is collected in the Ile-de-France region a tax on the occasion of the construction of premises in particular for an office use. Thus operations which purport to create office areas, or to rehabilitate such, if they create construction areas, come as of right under the scope of application of the tax on the creation of office areas. However, in a derogatory and transitional respect, article L520-8 of the planning code excluded demolition and reconstruction operations for which the planning permission was delivered prior to 1st January 2014 from the ambit of said tax. ■

[1] *Articles R421-13 and R421-17 of the planning code.*
[1] *Conseil d'Etat, 9 March 1984, Macé, no.41314 ; Conseil d'Etat, 9 July 1986, Thalamy, no.51172.*
[1] *Law no. 2006-872 of 13 July 2006.*
[1] *Conseil d'Etat, 3 May 2011, Ely, no.320545.*
[1] *Criminal actions being time barred after three years and any civil actions for demolition being time barred ten years after completion of the works.*
[1] *Prior to the law of 12 May 2009, only those buildings destroyed by a damaging event benefitted from this provision. The law Commission of the French Sénat noted however that a large number of existing timeworn buildings, although having been lawfully developed, were in conflict with various subsequent planning rules and that, for economic and technical reasons, the demolition and reconstruction was sometimes preferable to a rehabilitation process.*
[1] *Ministerial answer no.90267, Official Journal of the Assemblée Nationale, 21 December 2010: "the right to proceed with the reconstruction of a damaged building must (…) be understood as a strict obligation to reconstruct the building destroyed according to the same positioning, the same surface area and the same volume. Where the project is different to the damaged construction, there is no reason to apply the provisions of article L111-3 of the planning code which are aimed at preserving vested rights, and the project will be appraised taking into account planning rules in force at the time of reconstruction"*
[1] *More precisely, the tax on premises for an office use, on commercial premises and on storage premises defined in III of article 231 ter of the Tax Code.*

The current reform of planning law: working towards a "project orientated planning" approach

*By **Jean-Luc Tixier**, partner, specialized in real estate law and public law.*
jean-luc.tixier@cms-bfl.com

*and **Vanina Ferracci**, Lawyer specialising in public law. She provides services in the fields of planning and development law. She has a long standing record of providing advisory and litigation services both to corporations and to local authorities*
vanina.ferracci@cms-bfl.com

Initiated by the Government in 2010 by the organisation of task forces including all of the professionals concerned, the stated objective of the planning reforms is to put an end to the regulatory planning approach in favour of a project orientated planning approach. All of the 70 proposals, presented at close of proceedings of the task forces "for project orientated urban planning", will be the subject of orders or will be inserted into various legal vehicles between now and 2012. Here is a general overview thereof.

The local zoning plans (PLU) would be entirely reorganised.

The regulations would thereafter only include four theme-topics (instead of fourteen currently): use of the ground/economic, social and environmental functions; ecological continuity function; Road and Utility prescriptions; urban form. The role of the Planning and Sustainable Development Plan would be reinforced: "project sectors" could be created in urban areas or areas to be urbanised; these sectors would not include a set of regulations but exclusively industry specific and enforceable policies, so that a modification of the PLU would not be necessary to carry out projects therein; the objective is that the planning document should adapt to the project, and no longer merely the other way round. In addition, in these sectors, it would be possible to negotiate the adaptation of certain rules of the construction and housing code or of the civil code to the scale of the sector.

Several aspects would affect planning authorisations in order to facilitate construction. Besides the replacement of floor areas to all pre-existing types of surface areas (an average gain of constructability of 10% approximately is expected), the examination of certain planning permission applications would be simplified: separation between planning permissions and authorisations in respect of the construction and housing code for establishments receiving the public, increase of the threshold for the requirement of an authorisation for an extension or for ancillary premises in respect of existing premises, or yet still reduction of the examination period of authorisation applications within the perimeter of historical monuments. Finally, the regime of subdivision estates would be simplified and clarified; the same would apply for the other methods of land division, including for planning permissions operating division.

Several courses of action are being examined in order to limit any possible litigation, such as the communication of the planning permission application file prior to lodging, this measure being intended to enable the project's evolution prior to the delivery of the authorisation to exclude risks of litigation, or the introduction into the Code of administrative justice of conciliation proceedings under the patronage of the administrative judge. In parallel, the finalisation of means to combat unreasonable exercise of legal recourse is being examined.

"The objective is that the planning document should adapt to the project, and no longer merely the other way round."

The chapter reforming planning taxes and contributions has already been adopted in the context of the amended finance bill for 2010 of 29 December 2010 (see Real Estate Newsletter of 21 March 2011, p.8 "The tax system applicable to planning matters: a new mechanism for 2012"). It shall enter into force on the 1st March 2012.

A reform of tax liabilities of non-developed constructible land is contemplated, with the objective of "unlocking" the offer in terms of land, in particular by putting an end to the tax benefits in connection with the property holding period. In order to provide "oxygen", it is contemplated for this reform to enter into force "in stages", in order to incite the land owners concerned to assign their property before entry into force of the new system. The tax rules discussed before Parliament will have potentially an impact on this aspect of the reform.

A bill proposal aiming to improve and secure exercise of pre-emption rights was adopted on 29 June 2011 by the *Sénat*. Under the terms of this text, various "future operations zones" (ZOF) will be created within which a pre-emption right would be granted in favour of communes during a period of six years renewable.

The scope of application of the urban pre-emption right would be extended to buildings or groups of corporate interests forming the subject matter of a gift, with the exception of family gifts.

The contents of the declaration of intention to dispose of property would be completed (incorporating information related to the possible presence of a facility classified for the protection of the environment) and the holder of the pre-emption right would have the possibility to solicit additional information intended to appraise the consistency and the condition of the building, or yet still to visit the asset. The terms of waiver by the pre-emption right holder would also be modified. The waiver would thus no longer be possible where a judge is solicited and that the price that he or she sets is not superior by more than 10% to the appraisal conducted by the Estates Department. On the other hand, the holder of the right could waive the right to pre-empt in the event where hidden defects are discovered. In any event, in the case of a waiver, the assignment could be carried out for the price set out in the Declaration of Intention to Dispose of Property, including where the waiver should intervene prior to the judicial determination of the price.

Finally, the use of the property could differ to that having provided grounds for pre-emption, to the extent where such is among those contemplated under article L210-1 of the Planning Code, the owner having a right of reassignment if such use or disposal should intervene within a period of five years.

These proposals are still to date projects and will be able, of course, to vary before the orders are drafted or, for the reform of the pre-emption right, before the definitive adoption of the text.■

If you would like to contact the authors of this newsletter, please write to the editorial staff which shall pass your remarks on to the persons concerned. You can also write to:

CMS Bureau Francis Lefebvre
1-3 villa Emile Bergerat
92522 Neuilly-sur-Seine Cedex, France
Tél : 01 47 38 55 00
Fax : 01 47 38 55 55
www.cms-bfl.com

M^e Gaëtan Berger-Picq, gaetan.berger-picq@cms-bfl.com
M^e Laurent Chatel, laurent.chatel@cms-bfl.com
M^e Richard Foissac, richard.foissac@cms-bfl.com
M^e Cathy Goarant-Moraglia, cathy.goarant-moraglia@cms-bfl.com
M^e Jean-Luc Tixier, jean-luc.tixier@cms-bfl.com
M^e Philippe Tournès, philippe.tournes@cms-bfl.com