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CONTENTS

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EDITORIAL

Widely practised in the business world but problematic for lawyers, the notion of the partial transfer of assets continues to raise questions about its identity and legal system. Its identity somewhat defies common sense. Compared to the usual contribution in kind, the partial transfer of assets results in the transfer of a set of properties making up an autonomous business segment. Case law has attached the benefit of the universal transfer of both assets and liabilities to this transfer as long as the spin-off system has been chosen. The solution is very practical but peculiar. It is understood that in a merger, both the assets and liabilities of the acquired company are fully passed on to the acquiring company: with the acquired company dissolved, who would assume the burden of the liabilities? In the partial transfer of assets, the transferring company continues to exist and receives corporate securities in exchange for its transfer. There is nothing natural about the universal transfer here: it is a technical trick. However, the partial transfer of assets has another identity problem: the lawyer and the tax specialist do not necessarily have a unified view of the operation. For the lawyer, being subject to the spin-off system is optional; for the tax specialist, whether there is an option or not, the system for mergers applies since there is a transfer of an autonomous business segment. A final part of the identity problem is that the partial transfer of assets is always handled through a process of referral to texts: in this case, to texts related to the spin-off system, itself originating from the merger system. This treatment by simple referral can cause difficulties when the difference between this operation and others comes to light: the recent law that simplifies the merger system seems partially inapplicable to the partial transfer system.

The ambiguities of the very nature of the operation relentlessly spill over on its system. Despite the mechanism of universal transfer, it seems difficult to forget that the transferor still exists. The creditor unpaid by the transfer's beneficiary will be tempted to go knock on the door of the transferring company; the transfer's beneficiary, faced with commitments that disturb it, will be tempted to claim that a particular obligation does not fall within the scope of the transfer and that the creditor will have to discuss the matter with the transferring company, which will use opposite reasoning. In addition, we can very well imagine that the labour judge must be particularly vigilant on these operations that can be the source of very strong protects from employees whose jobs are tied to the transferred business segment. The courts are also not in favour of the externalisation of liabilities through this type of transfer in principle and have expressed their disapproval since 1991[1]. This feature will provide illustrations of these remarks and certain tax issues related to the matter, including the problem of the retroactive effect, which was the subject of a very noteworthy decision of the Council of State.

	The partial transfer of assets is the very example of an issue that calls upon the differing perspectives of several disciplines and the debate of specialists. An ambiguous operation, it develops consequences in every area of law that are more or less consistent with each other, and the experts who contributed to this feature will now elaborate on them. *1. Com, 5 March 1991.* Alain Couret, partner

Partial transfer of assets, a preferred carve-out tool


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During the transfer of a company engaging in several distinct activities, it frequently occurs that one of these activities is not intended to be transferred, thus requiring the seller to first carry out a carve-out, which involves removing that particular activity from the scope of the transfer in order to reclassify it within its group. When such an activity has already been made a subsidiary, this carve-out generally occurs through reclassification of the securities of the subsidiary in question, an operation that is relatively easy to organise. However, when this activity is operated directly by the target company, the carve-out proves to be more complex to implement. In this situation, the partial transfer of assets (APA) of the activity in question by the target company to a company whose securities are then reclassified outside of the scope of the transfer can be a particularly appropriate carve-out tool to use.

From a legal point of view, the APA, subject to the legal system for spin-offs, first has the major advantage of bringing about a universal transfer of all of the rights, properties, and obligations for the business segment transferred under the APA. Therefore, in the context of a carve-out, using the APA rather than an outright transfer of the activity (a transfer that, in most cases, will be subject to the restrictive legal system for the sale of a business) is the obvious choice if this activity includes liabilities (as they are not automatically transferable in the sale of a business) or assets, the formalities of which would be particularly difficult to respect in case of an outright transfer (buildings, leases, receivables, business, etc.) but can be avoided under an APA. In addition, the benefit of this universal transfer, combined with the option of the companies that are parties to the operation to exclude any joint liability among them under the APA, makes it possible, in principle, to free the transferring company from the liabilities attached to the transferred segment, which is certainly an essential point in discussions between the seller and the buyer of the transferring company, as the buyer does not wish to assume any risk for the carved-out activity.

"Being able to prepare and study the carve-out's terms from the initial stage of thinking about the planned transfer is a must."

However, it should be noted that the principle of universal transfer has a few exceptions (assets made non-transferable by a legal provision, "intuitu personae" contracts, administrative contracts, etc.) and that, consequently, during the operation, it will be essential to identify the assets or liabilities requiring special approaches to be carried out with third parties or specific treatments to be agreed upon in the transfer's contractual documentation. In terms of timing and given the formality imposed by corporate law (appointment of a commissioner in court, holding of general meetings of shareholders, creditor objection period, etc.), the average time for completing an APA is at least three months, which may be extended because of other legal procedures (for example, procedure for informing/consulting personnel representative bodies) or contractual procedures (for example, contractual clause for third-party authorisation). Being able to prepare and study the carve-out's terms from the initial stage of thinking about the planned transfer is a must for optimal organisation of its timing. The carve-out will only be effective once the APA is carried out and the securities received as compensation are reclassified within the seller's group. In this regard, special attention will need to be given to the financing terms for this reclassification of securities. In particular, in order for the carve-out to be as neutral as possible as part of the transferring company's transfer, it is advisable for the proceeds from

the sale of the reclassified securities to be able to be paid to the seller prior to the transferring company's transfer through, for example, a partner current account repayment, a dividend distribution, or a capital reduction.

From an accounting perspective, the APA has the advantage, like from a taxation perspective, of being able to be carried out with a retroactive or delayed effect within the limits of the current fiscal year. In practice, the APA is usually carried out with a retroactive effect to the first day of the current fiscal year so that the beneficiary company takes over all of the loss or, conversely, all of the earnings relating to the transferred activity for this fiscal year. Here again is a very important point in discussions between the buyer and the seller, as it allows the transferring company to be freed from the accounting impacts of the activity for the fiscal year of completion of the APA. In addition, in the particular case in which the net assets of the activity to be transferred are negative ("badwill"), the transferred business segment should be recapitalised so as to be able to generate positive net assets, a legal prerequisite for carrying out the APA.

"From an accounting and taxation perspective, the APA can be carried out with a retroactive or delayed effect within the limits of the current fiscal year."

From a taxation perspective, the preferential treatment ensuring tax neutrality for an APA cannot benefit a carve-out operation if the target company cannot fulfil the commitment to hold the securities of the beneficiary company of the APA for three years. Similarly, in terms of tax consolidation, the mechanism of neutralisation of gains or losses at the time of any intragroup transfer operation involving capital assets or securities will not be to apply to the operation because of the target company's exit from the consolidated group. In practice, therefore, the APA will often be placed under the ordinary tax system by favouring a carve-out involving equity securities (with a tax impact of around 3.4%) with regard to taxation at the rate of 33.1/3% on other unrealised gains generated in connection with the operation.
In this situation, valuation of the transferred assets by an independent firm is highly recommended, both from a taxation perspective and with regard to the buyer of the target company. The carve-out of structurally loss-making activities, unwanted by the future buyer of the target company, will be carried out without any tax impact in the absence of significant unrealised gains on the transferred assets. Moreover, in the event of a recapitalisation of the transferred business segment through capitalisation of partner current accounts, the carve-out, prior to the transfer of the target company, could then allow the transferor to realise a loss on disposal of securities in part for the short term.
Lastly, note that the Council of State (see article on p10) recently gave a "fiscal boost" to the APA as a carve-out tool by deciding that the retroactive tax effect of an APA made to a beneficiary company formed in view of this APA can go back even beyond the date of creation of this company up to the opening date of the transferring company's current fiscal year. In concrete terms, this means that, for tax purposes, a loss-making activity can be made a subsidiary without generating any loss of the tax loss for the transferor.
Regarding registration fees, since the APA involves a complete, autonomous business segment, the operation has the option of being subject to the preferential system for mergers and spin-offs and may thus give rise to only the payment of a fixed fee. However, on the grounds of abuse of law, the tax authorities have not abandoned the idea of reclassifying operations used to transfer an activity or make it a subsidiary as transfers of a business. A prior analysis of the considered carve-out will therefore remain necessary in all circumstances.

Asset transfers: whether to opt for the universal transfer of assets and liabilities

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When a transfer involves a set of properties, the transferring company and the transfer's beneficiary have the option of placing the operation under the spin-off system. The use of this option – regardless of the transfer's tax treatment – results in the universal transfer of assets and liabilities (TUP) attached to the transferred activity. In this case, all of the assets and liabilities related to the transferred business segment are automatically transferred to the beneficiary company of the transfer. This option has significant advantages: it permits the transfer of a set of assets related to any activity without needing to prepare a precise list of them and also authorises the transfer of liabilities and contracts related to these assets without any special formalities and without the approval of the co-contracting parties in most cases.
However, there are limits to this automatic transfer: in particular, contracts entered into in consideration of the person of the co-contracting party ("intuitu personae") or those for which the law or contractual stipulations prohibit their automatic transfer may not be transferred without the approval of the co-contracting party.
Beyond these limits, should the TUP always be chosen in order to form a subsidiary from an activity and, more generally, to transfer a set of properties to a company, particularly in the creation of joint ventures?

"The automatic transfer of holdings can be a significant disadvantage for the beneficiary company of this operation."

The automatic transfer of holdings, and particularly the automatic transfer of all of the liabilities related to the transferred business segment, can be a significant disadvantage for the beneficiary company of this operation, which will need to take the risk of taking over obligations and liabilities without necessarily having precise knowledge of their extent. As part of an operation with a third party (creation of a joint venture, for example), the option for the spin-off system will require the beneficiary to perform more due diligence prior to the operation (audit tasks) and negotiate detailed declarations and guarantees in order to be reassured about the contents of the assets and liabilities that will be received. With regard to declarations and guarantees, they will often turn out to be difficult to structure. In particular, who must benefit from these guarantees? Logic would dictate that it would be the company receiving the transferred assets and liabilities. However, a different approach, closer to the economic reality of the operation, is to have the transferor's future co-shareholder benefit from these guarantees. Although it has not received any assets or liabilities, it is this future co-shareholder who will agree with the transferor in order to determine the operation's financial balance and accept a dilution based on what the transferor declared to it. Such guarantees may also prove to be complicated to implement. It will often be difficult to request compensation from a partner with whom a joint venture has been established without calling into question the operation of the partnership and the future of the "common adventure".
Not opting for the TUP can thus make it possible to overcome these disadvantages by precisely listing the transferred assets and liabilities (subject to the approval of the creditors for the liabilities as a general rule). This also makes it possible to avoid joint liability between the transferor and the beneficiary or the creditor objection period if this joint liability has been excluded by the parties. The option for the spin-off system will therefore depend on the circumstances particular to each situation and must be chosen by balancing the practical (and tax) advantages that it has with regard to the legal risks that it may involve.

The mechanism of the universal transfer and its limits

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Case law has attached the benefit of the universal transfer to the partial transfer of assets starting with a landmark ruling on 16 February 1988. This solution did not arise by itself: it is unsettling to admit the existence of a universal transfer of assets and liability even though the transferring company has retained its legal personality; however, it is hardly discussed anymore, as the solution is obviously valid only if the operation was subject to the spin-off system However, this universal transfer has some limitations that we wanted to present here.
The principle is therefore that of the universal transfer: case law recites applications of the rule and exceptions over the years. In general, the exceptions to the principle of universal transfer that could be identified today are intended to apply to partial transfers of assets subject to the spin-off system because of the referral mechanism that occurs.
The key issue is that of the exact scope of the transfer. The transfer is done on a universal basis: it therefore involves a set of liabilities correlated with a set of assets. However, the discussion can focus on the outlines of the set. A partial transfer of assets agreement must be prepared and be as precise as possible in its description of the transferred items. But what about items that were not expressly indicated? Case law provides us with some clarifications on this point.

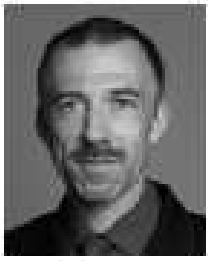
"The key issue is that of the exact scope of the transfer."

The parties can thus exclude properties or debts of the transferred branch. The exclusion must be unequivocal: in a case where a branch was involved, the branch was never cited in the appendices of the transfer contract containing the list. Nevertheless, the trade and companies register extract related to the transferring company's new name mentioned various trade brands, including the branch's[1].
At times, the legislature is careful to specify the consequences of this transfer and its limits. This is the case with commercial leases. Article L.145-16 paragraph 2 of the French commercial code specifies that the beneficiary company, notwithstanding any contrary stipulation, is substituted for the company who was granted the lease under all of the rights and obligations resulting from this lease. This substitution is public information. As a result, the lease is transferred automatically without any formality other than those provided for by the corporate law and regardless of any contrary or restrictive clauses of the lease.
However, this text establishes limits. The final paragraph of Article L.145-16 stipulates that *"in case (...) of a transfer, if the guarantee obligation can no longer be ensured under the terms of the agreement, the court may substitute any guarantees that it deems sufficient"*. The guarantee obligation in question particularly refers to the common clause of joint guarantee. The text gives the court broader powers on the very principle of the granting of guarantees than on their determination. After analysing some decisions handed down on this point, it turns out that the courts mainly grant bank guarantees. According to case law, it is up to the lessor to request a substitution guarantee. No time frame is stipulated for referral to the court.

Once discussions about the scope of the partial transfer of assets are over, the specificity of the legal system for partial transfers of assets appears especially from the perspective of transfers of liability that can occur between the transferring company and the beneficiary company (see p8).

[1] Court of Cassation, Commercial Section 7-10-2008 no. 07-17.731

How labour law challenges partial transfers



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The partial transfer of assets has the effect of transferring an activity and the employees associated with it within a new structure, created specifically for this purpose or pre-existing and already engaging in an activity. In principle, once the transfer is carried out, the employees are governed by the rules specific to the receiving business, and the ties with the original business cease. However, a number of labour law rules that favour the de facto situation for the employing legal entity can partially neutralise the effects of partial transfers of assets and take the unit formed by the transferring company and the beneficiary company of the transfer into consideration.

The obligation to put joint personnel representative institutions into place

In accordance with Article L.2322-1 of the French labour code, a works council must be formed in businesses with 50 or more employees. As an exception, Article L.2322-4 of the French labour code stipulates that when a unit of economic and employee interest with more than 50 employees is recognised by agreement or court decision, among several legally distinct businesses, the establishment of a joint works council is mandatory.

The unit of economic and employee interest is characterised by two elements:

– a unit of economic interest resulting from the concentration of management powers and capital as well as a similar or complementary activity;

– a unit of employee interest resulting from a similar employment status and working conditions in the two companies and, where applicable, interchangeability of employees. In order to recognise these different elements, the judge uses the "body of evidence" method and rules based on very concrete elements.

It is common for a new company created through a partial transfer of assets to meet all of the above criteria (identity of manager, shareholders, complementary activities, comparable or even identical employment status) during its early years. Indeed, in most cases, soon after the transfer, the employment status of the transferred employees has not changed enough to be different from that of the original company. Consequently, there is a risk that a judge will agree to recognise the existence of a unit of economic and employee interest that will have the effect of requiring the establishment of a works council involving the transferring company and the transfer's beneficiary company. In practice, the field of jurisdiction of this works council will be identical to that of the company's works council prior to the transfer. This risk is higher if the company that carries out the transfer was about to exceed the threshold of 50 employees.

The risk is more limited when the company benefiting from the transfer already has an activity and personnel regulations of its own.

The obligation to establish employee profit-sharing

Article L.3322-2 of the French labour code requires the establishment of profit-sharing in businesses with more than 50 employees but also in businesses constituting a unit of economic and employee interest with more than 50 employees. Therefore, the existence of a unit of economic and employee interest recognised by a court decision or by an agreement will lead to the establishment of a profit-sharing agreement in the company resulting from a partial transfer of assets, even if it has fewer than 50 employees, if the unit of economic and employee interest formed with the transferring company employs a total of more than 50 employees. However, in this case, it should be noted that company leaders will have the choice of establishing either a single profit-sharing agreement for the two companies (with a rather similar reproduction of the agreement that would have existed without the transfer) or two separate agreements: one within the transferring company and the other within the transfer's beneficiary company.

The inability to apply only the employment status of the transfer's beneficiary company
Employees who are assigned to the business segment transferred under the partial transfer of assets and are transferred to a company already engaging in its own activity and having personnel regulations will benefit from the status in force in that company.
However, Article L.2261-14 of the French labour code organises a provisional survival period for collective agreements (for a company or branch) that applied to the employees before the partial transfer of assets. During this period, usually fifteen months, the transferred employees receive the benefits most favourable for them: those arising from agreements that applied within their original company or those in force within the receiving company. The labour code thus limits sudden losses of the original employment status if it is favourable to the employees.
Similarly, the unilateral customs and commitments of the former employer continue to apply at the new employee whenever they are more favourable for the transferred employees, as long as the beneficiary company of the transfer does not validly terminate these customs and commitments.

"There is a risk that a judge will agree to recognise the existence of a unit of economic and employee interest involving the transferring company and the beneficiary of the transfer."

Joint liability in case of a workplace accident caused by the employer's gross negligence
By two decisions of 7 April 2011 and 17 March 2011, the Court of Cassation held that the victim of a workplace accident, who can bring a civil liability action against his or her employer in the event of the employer's gross negligence, may continue the take action against the employer in case of a partial transfer of assets whenever the legal entity does not disappear in this transfer, regardless of the agreements made. In addition, the High Court acknowledges that the victim can also rely on the terms of the transfer agreement and summons, at the same time, the beneficiary company of the transfer whenever this company has become the holder of the rights and obligations of any kind relating to the transferred branch.

Consideration of the group's companies with regard to job transfers
Article L.1233-4 of the French labour code specifies that redundancy for economic reasons may occur only when the employee cannot be transferred to another position in the same company or in other companies of the group to which it belongs. If the beneficiary company of the partial transfer is still part of the transferring company's group and carries out a redundancy for economic reasons, it shall offer the vacant positions existing within it and within the transferring company (unless the transferring company's activity stands in the way of any swapping of positions).
Failure by the transferring company to comply with its job transfer obligation exposes the transfer's beneficiary company to the payment of damages.

The need to take the business segment into account with regard to redundancies for economic reasons
The Court of Cassation deems that economic difficulties likely to justify a redundancy for economic reasons must first exist within the affected company but also within the various companies making up the business segment of the group to which the affected company belongs. Therefore, if the partial transfer involves separating, for example, a production and marketing activity or production and storage activity, activities belonging to the same sector, in the event of a dismissal within the transfer's beneficiary company, the economic situation existing within it as well as the transferring company will need to be taken into consideration.
The dismissal will be based on a real and serious cause only if the two companies belonging to the same sector must cope with difficulties.
In conclusion, carrying out a partial transfer of assets is not always enough to completely separate two activities, as labour law makes it possible to maintain more or less significant connections in certain cases.

Is the universal transfer of assets and liabilities accompanied by a transfer of liability?


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The partial transfer of assets subject to the spin-off system brings about, in principle, a universal transfer of assets and liabilities (TUP) of the transferring company to the beneficiary company, to which all of the rights and properties comprising the transferred branch as well as all of the debts attached to it are transferred[2].
The partial transfer of assets thus produces the same effects as the spin-off, namely the transfer of existing assets and liabilities, which includes criminal or administrative fines already imposed by a decision having the authority of a final judgement. However, there is a difference between the two operations: while the company being divided (like the acquired company in a merger) disappears, the transferring company survives the transfer and retains its legal existence.
As a result, it remains jointly required with the transfer's beneficiary to pay the debts passed to the beneficiary[3], unless the parties have chosen, as frequently done in practice, to exclude this joint liability through an express exemption in the transfer contract (cf. Art. L.236-20 s. of the French commercial code).
But this joint liability is not the only impact of the legal survival of the transferring company. It also has consequences on the accountability for the liabilities that may be incurred for criminal offences, market abuses, or anti-competitive practices committed in connection with the transferred activity and not yet punished.

"The transferring company that continues to exist can still be prosecuted for its offences."

With regard to civil liability, while the transferring company can no longer, except in cases of fraud, be prosecuted for offences that it personally committed as part of the transferred activity, as the consequences of these offences must be borne by the substituting beneficiary[4], it is a different matter in other fields of liability.
Thus, the principle of the individual nature of penalties (cf. Art. 121-1 of the French criminal code) prohibits the transfer's beneficiary (like the acquiring company) from being held criminally liable for offences arising because of the transferring company or even having a penalty not yet pronounced as at the day of the transfer transferred to it[5]. But unlike what happens with a merger, the transferring company, which continues to exist, can still be prosecuted for the offences. The universal transfer of the activity that was the subject of the offences is irrelevant in this regard.
This principle of "legal continuity" also prevails regarding the imputation of market abuses and anti-competitive practices. For anti-competitive practices, as long as the offending company retains its legal personality, it remains liable for its wrongful conduct, regardless of whether the material and

[2] *Court of Cassation, Commercial Section, 10 December 2003, no. 1790.*
[3] *Court of Cassation, Commercial Section, 12 December 2006, no. 1428; and 8 February 2011, no. 100.*
[4] *Court of Cassation, Commercial Section, 10 December 2003, supra.*
[5] *Court of Cassation, Commercial Section, 20 November 2001, no. 1915.*

human resources that allowed the offence to be committed have been transferred to a third party[6]. The beneficiary company of the transfer is therefore released from any liability in this regard[7], except in choosing to perpetuate the unlawful practice, in which case, it incurs liability on its own.
Does this mean that it does not run any risk because of arrangements or abuse of dominant position used by the transferring company? Not necessarily, because the competition authorities can extend the spectrum of "economic continuity". Initially used, when the perpetrator of the practice has legally disappeared, to transfer its liability to the legal entity that received the offending business[8], it can also be applied without obligation, however, when the initiator of the practice has retained its legal existence but no longer engages in any economic activity ("shell"). The transferring company and the beneficiary then form the same "unit of economic interest" due to structural links uniting them, which makes it possible to attribute the original operator's offences to the new operator of the company[9]. In competition law, forget the company. Follow the business instead!

[6] *Court of Cassation, Criminal Section, 20 June 2000, no. 4129 and 14 October 2003, no. 4992*
[7] *Paris Court of Appeal, 20 October 1998, SA Béton travaux/Competition Council*
[8] *Competition Council, decision 7-D-11 of 28 March 2007; and Paris Court of Appeal of 10 January 2009.*
[9] *TUE 30, September 2009, case T-161/05; and ADLC, decision 10-D-28 of 20 September 2010*

The concept of complete business segment: uncertainties remain

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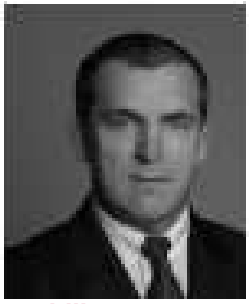
Despite several recent decisions, the concept of complete business segment remains a source of questions that, pending clarifications by the Council of State, should encourage companies to be cautious.

The concept of a complete business segment is of considerable importance in partial transfers of assets.
The system of tax neutrality for mergers can apply to a transfer operation only if it involves a complete business segment. Without any definition in the French general tax code, we must refer to the definition given by the community directive of 23 July 1990, itself incorporated by the tax authorities and according to which the concept of complete business segment covers "all assets and liabilities of a division of a company that constitute, from the organisation's point of view, an autonomous operation, i.e. a unit capable of operating by its own means".
The characterisation of a complete segment therefore proves to be a particularly tricky exercise, since, on one hand, it involves a largely factual matter and, on the other hand, the administrative approach is particularly strict. However, in an order dated 27 July 2005 (no. 259052, sté BL), the Council of State proved to be more flexible by ruling that "in order to be entitled to the benefit of the aforementioned provisions of the second paragraph of point 1 of Article 210 B of the French general tax code, a partial transfer of assets must involve a business segment likely to be the subject of autonomous operation at the transferring company like at the transfer's beneficiary company, provided that this transfer brings about a complete transfer of the essential elements of this activity as they existed in the transferring company's asset base and under conditions permitting the transfer's beneficiary company to have all of these elements for the long term". Thus, according to the Council of State, it is not necessary for the transfer to involve "all assets and liabilities" insofar as the "essential elements" are transferred.

"The characteristic of a complete segment proves to be a particularly tricky exercise."

This being the case, the carve-out of a segment often remains a dangerous exercise, as the case law definition remains restrictive and subject to interpretation despite the flexibility provided. Several recent decisions handed down by lower courts show that many questions have still not been definitively resolved. Such is the case, for example, of issues related to the transfer of intangible assets (Bordeaux Administrative Court of Appeals, 30 December 2010, no. 09BX02218), the takeover by the transfer's beneficiary of liabilities greater than those of the segment (same order), the transfer of personnel (Lyon Administrative Court, 12 October 2010, no. 08-2020; and Rouen Administrative Court, 1 June 2010, no. 09-2729, handed down in related fields), or the provision of common services (Rouen Administrative Court, 17 February 2011, no. 0501355).
In conclusion, the definition of a complete business segment still leads to hesitations. The scope of the recent decisions handed down by the lower courts, sometimes encouraging, therefore deserves to be confirmed or at least clarified by the Council of State. In the meantime, we can only encourage businesses to be very rigorous in their work in carving out segments and in the wording of transfer agreements. Lastly, in case of serious doubt, obtaining an approval or a ruling issued by the administration will make it possible to secure the operations, but this approach must have been anticipated in the timing of the operations.

The retroactive effect of a partial transfer of assets to a new company



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Regarding corporate tax, the Council of State[10] has deemed that the retroactive effect legally or contractually attached to a contract entered into by a company subject to the corporate tax can allocate the earnings of the tax period during which this contract was entered into but can in no case lead to a correction of those of the previous period. This case law, evident for mergers, regardless of the system under which the operation is placed, has then been extended to partial transfers of assets[11], and these rules has been accepted by the tax authorities[12].
It has also been decided:
- that the retroactive effect must not go beyond the date on which the acquiring company opened the fiscal year during which the merger was definitively approved[13];
- and that when the parties have agreed on a retroactive effect clause, they do not have the option of waiving the incorporation of all of the proceeds and expenses coming from the operation of the transferred activities during the interim period[14].
As a result of this case law construction, in the generality of restructuring operations, except for TUPs, the tax effective date is the accounting effective date, provided, however, that this date is not prior to the opening of the fiscal year of the transfer's beneficiary company during which the operation is carried out.

"The Council of State clearly invalidated the administrative doctrine according to which the operation cannot have a retroactive effect to a date prior to the registration of the new beneficiary company of the transfers."

However, the scope of the retroactive effect clause remained to be confirmed in the particular situation of transfers to new companies since the entry into force of the law of 1988, which introduced, in Article 372-2 of the law of 1966 on commercial companies (later L.236-4 of the French commercial code), the clarification according to which, in case of creation of a new company, the merger or the spin-off takes effect on the date of registration of this company with the trade and companies register.
In a case prior to 1988 involving the transfer of a business to a company, the Council of State had ruled, in 1997, based on the provisions of Article 5 of the law of 24 July 1966 and Article 38 of the French general tax code, that when the parties have agreed to give a retroactive effect to the transfer, it can take effect on the opening day of the fiscal year during which the company was registered[15]. In this case, it was accepted that the transfer can have a retroactive effect to 1 October 1979, even though the company had not been registered with the trade and companies register until 9 November 1979.
Confirming its position, the Council of State just ruled[16] that the provisions of Article 372-2 of the law of 24 July 1966, as amended in 1988, merely explained, for the purposes of transposition of community

[10] *CE (Council of State), 12 July 1974, no. 81753.*
[11] *CE (Council of State), 18 March 1992, no. 62402.*
[12] *BOI, 4-I-1-93.*
[13] *CE (Council of State), 26 May 1993, no. 78156.*
[14] *CE (Council of State), 18 March 1992, no. 62402.*
[15] *CE (Council of State), 28 February 1997, no. 141459.*
[16] *CE (Council of State), 29 June 2011, no. 317212.*

directives, the rule that already resulted from Article 5, according to which when a merger or a spin-off gives rise to the creation of a new company, the new company enjoys the legal personality starting from its registration with the trade and companies register. Consequently, these provisions may not prevent the parties from making the operation effective on a date prior to that on which the personality of the new company is acquired or prevent this retroactive effect from being taken into account from a taxation perspective, within the limit of the opening day of the fiscal year during which the new company was registered with the trade and companies register.
The Council of State therefore clearly reversed the administrative doctrine according to which the operation cannot have a retroactive effect to a date prior to the registration of the new beneficiary company of the transfers[17].

[17] *BOI 4-I-1-93, no. 29*

The new regional economic contribution (CET), 2011 restructurings, and their consequences

By **Laurent Chatel,** partner in taxation, manager of the local tax department. laurent.chatel@cms-bfl.com

2011 is the second year of application of the regional economic contribution (CET) made up of the company real estate contribution (CFE) and the company value-added contribution (CVAE).
As is the case under the business tax, the retroactive effects that the operations entail have no impact with regard to CET, so that in case of an operation during the year, the former operator remains taxable until its final completion. In case of a universal transfer of assets and liabilities (TUP), the change in operator therefore occurs starting from the expiry of the 30-day creditor objection period.
In order to no longer be subject to the CFE starting from the following year, letters providing notification of the operation should be sent before 31 December 2011. For property tax, it is imperative to ensure that the publication in the land register was actually completed to avoid the risk of not obtaining the registration transfer.

"In order to no longer be subject to the CFE starting from the following year, letters providing notification of the operation should be sent before 31 December 2011."

As an operator as at 1 January 2011, the former operator now finds itself needing to calculate its added value for the CVAE based on its period of activity.
In accordance with Article 1586 octies II-2° of the French general tax code, in case of a universal transfer of assets and liabilities, transfer and cessation of business, or upon the death of the taxpayer, the successor must settle its CVAE within 60 days from the operation.
The 2011 value adopted in order to settle the former operator's 2011 CVAE (unless it closed a twelve-month fiscal year in 2011) will be determined based on the income and expenses of the period between 1 January 2011 and the date of the operation based on an accounting balance.
The turnover produced for 2011 used to define the scope of application and the rate of the CVAE must be corrected in order to correspond to a full year, while the added value used as the basis for the CVAE will remain determined on the actual period of activity. It should then be considered whether the capping mechanism can apply in this case. However, recall that pursuant to the new Article 1647 B *sexies* of the French general tax code, in the absence of a transfer or cessation of a business during the tax year, the amount of the added value is corrected in order to correspond to a full year. In addition, in case of a universal transfer of assets and liabilities or a transfer or cessation of business, the amount of the cappable CFE is adjusted based on the ratio between the length of the reference period and the calendar year.
Starting in 2012, the new operator will become subject to the CFE for the establishment(s) that it has taken over. For this purpose, before 31 December 2011, it must send a form 1447 C to the corporate tax offices (SIE) governing these establishments in order to inform them of the operation.
The CVAE will be determined based on the added value produced during the twelve-month fiscal year closed in 2012, necessarily including the added value of the activity taken over, while the 2012 CVAE instalments will be determined based on the 2011 added value including only some of the added value coming from the activity taken over.
If the former operator used the capping mechanism in 2010, it is not transferred to the successor for 2012 (50%) and 2013 (25%). In case of changes in operator, the capping is lost.
Given the new wording of Article 1518 B of the French general tax code, and even if the premises occupied by the new operator are industrial in nature, it is more than likely that no change in the property value used as the basis for the CFE will result from the operation, as the two companies are related.

LBO and tax loss reform: a very "cash" effect

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After the cold snap endured at the beginning of the year with the extension, albeit limited, of tax rules to fight under-capitalisation in certain acquisition schemes (see the Mergers & Acquisitions and Private Equity Newsletter of 4 April 2011), LBO operators must now deal with a blow to the tax efficiency of their structurings by the government's "austerity plan" passed on 19 September.
We know that in order to avoid a free fall in corporate income tax receipts (IS), the tax law now restricts the use of a loss carryforward by capping it at 60% of the fiscal year's earnings, for its share exceeding €1 million, with the remaining 40% being subject to income tax at the full rate. We also know that because of the many costs incurred for their implementation (acquisition costs, issuance costs, loan interest), LBO schemes mechanically generate "access" to a loss carryforward.
This carryforward is then generally cleared from the net profit of the next fiscal year(s) of the tax consolidation group newly formed by the takeover holding company and the target companies, so that no income tax payment is assumed in principle in the early years of the operation.
The new tax loss limitation rule seriously disrupts these impeccable mechanics: now, the tax carryforward generated in the first year will be able to erase only 60% of earnings of the next fiscal year(s), and, in any case, effective taxation of around 13.33% (i.e. 33.33% of 40%) will apply to the share of the taxable income of the fiscal year exceeding €1 million. The cash flow plans of structurings will therefore need to be adjusted accordingly, sometimes even "with immediate effect", as the income tax instalment for 15 December may, in certain situations, need to be revised upward. Austerity rules...

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