Executive summary
The French Minister of Finance has confirmed the introduction of French withholding tax with effect from 1 January 2018. Details of the reform will be presented to the Parliament on 28 September 2016, alongside the Tax Bill for 2017.

In addition to this, the French inpatriate regime is due to be amended in order to offer greater flexibility to French inbound individuals.

Employers should begin to assess how the introduction of withholding will impact their payroll operations, international assignment programs and approach to employee communications.

Calculating and operating the withholding tax
A coding system will be implemented in order to allow the employer to properly calculate the withholding taxes due, negating the need to ask their employees questions regarding their personal situation.

The withholding rates to be operated by the employer will be calculated by the French tax administration when assessing the respective individual’s 2016 income. The relevant rate will be indicated on the tax bill normally issued in September 2017, and this will be communicated to the employer through the employer’s monthly wage reports, also known as the Déclaration Sociale Nominative (DSN).

Under certain conditions it will be possible to operate a standard tax rate schedule, which applies only to single taxpayers. For example, this standard schedule will apply to new taxpayers such as (but not limited to) former students and new French tax residents.

There will be a certain degree of flexibility for an individual to increase or decrease their withholding tax rate. In principle, any adjustment must be requested by the taxpayer via their individual tax portal on the French Ministry of Finance website (impots.gouv.fr). The local tax center will be responsible for calculating the revised withholding tax rate and transmitting this to the employer through the DSN. Joint filers may also request separate rates depending upon their respective incomes.

Implementation process and scope of withholding tax
The withholding tax system will apply to wages, pension payments, and unemployment allowances paid by French entities. Wages paid by non-French legal employers through a payroll outside France will not be subject to withholding. Further advice should be sought if the employer is in any doubt as to whether withholding tax should be operated.

For income not subject to the withholding tax such as business income, self-employment income, rental income, and employment income paid by non-French employers (where this income is paid via a foreign payroll by a foreign legal employer), monthly or
quarterly income tax payments will be requested. It is understood at present that the taxpayer will be able to elect to make their payments monthly or quarterly, however, this will be confirmed when the reform is finalized. The rules for passive income such as interest, dividends, and capital gains will remain unchanged.

Both resident and non-resident taxpayers will continue to have an annual French income tax return filing obligation. In 2017 taxpayers will pay the tax due on their 2016 income. From January 2018, the tax on employment income will be deducted at source by way of the withholding tax, which means that 2017 employment income may end up being partly or fully tax exempt. In practice, an income tax return must be filed in May 2018 in respect of a taxpayer’s 2017 income, however, taxpayers will benefit from a special tax credit called CIMR (broadly translated as “tax credit for modernization of the income tax collection”). This tax credit will cancel, at least in part, the French income tax due on non-exceptional employment income. For this purpose, types of exceptional employment income may include, but is not limited to, termination or severance payments, lump sum payments, or deferred compensation. Personal tax credits and tax reductions may be either offset against future liabilities or reimbursed over, or after, a couple of years.

More comprehensive details will be known by the end of September, subject to a final vote by the Parliament.

French inpatriate regime amendments
The French favorable regime (section 155B of the French tax code) for inpatriates is due to be amended. The key expected changes to the regime are summarized as follows:

► The length of time for which the relief is available, currently at a maximum of five tax years, may be extended to eight tax years.
► Current restrictions in place to ensure that taxes paid by inpatriates are of a similar level to those of locally employed individuals (in a similar employment position) may be made more flexible.

Next steps
Large companies should begin to assess how the introduction of a withholding tax system will impact their payroll operations including shadow payrolls, international assignment programs, and tax-equalization policies as well as their approach to employee communication on matters of taxation.