French Elections Pave Way for Labor, Tax Reforms

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In the months following the election of President Emmanuel Macron, who is perceived as pro-business, as well as a parliamentary election in which the new president's party won the majority, companies and entrepreneurs have expressed optimism that corporate France may at last embark on ambitious and long overdue reforms to reduce the amount of red tape that they believe constrains the French economy.

Key proposals targeted at economic growth include reforms of certain aspects of the famously complex French labor legal system and of the tax structure.

Simplifying the French Labor Law System

France is seen as a complex and expensive country in which to conduct business. In large part, this is because of intricate labor laws that businesses say make it costly, litigious and time consuming to adapt the workforce to economic and strategic changes within the company. Many see the lack of flexibility in the laws, especially regarding the dismissal of employees, as the main reason for the high unemployment rate in the country and as a significant factor in whether foreign companies decide to invest in France. Adding flexibility to France's labor laws was one of President Macron's main campaign issues, and on August 31, 2017, the government announced changes designed to stimulate economic growth and the job market.

The reform proposal includes:

Simplification of Individual and Collective Dismissal

Under the current labor laws, when individuals are dismissed from their jobs, employers are exposed to unquantifiable damages if the employees successfully assert that they were dismissed without cause. These damages are in addition to the indemnity already owed to the employees as a matter of law and collective bargaining agreements.

Reform would introduce a standard termination letter template and a procedure designed to minimize the risk of challenges to dismissals. In addition, in cases of termination without cause, damages would be determined on a scale with a set minimum and maximum amount based mainly on employees' length of service and company size, except in discrimination cases. Moreover, the time limit for complaints has been reduced from two years to one.

Currently, collective dismissals must be justified by the company's financial problems. This creates a flexibility issue, since the test of whether collective dismissals due to economic problems are justified is assessed at a global level (*i.e.*, worldwide). Collective dismissals are thus at risk if the company is experiencing economic problems in France or at a European level that justify reducing the workforce, but the group is performing better elsewhere in the same business sector. Reform should address this issue by requiring that the economic difficulties of an entity of a worldwide group be assessed at the national level, except in cases of fraud. The administrative burden for collective dismissals also is expected to be eased for smaller companies.

Shift From Industrywide to Company-Level Agreements

Currently, collective bargaining agreements must generally comply with industrywide standards, which reduce the ability of companies to tailor agreements to their needs. Under the reform, aside from issues devoted to industrywide-level agreements (*e.g.*, work hours, minimum wage, professional equality), company-level agreements would become the standard.

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Red Tape Slashed for Firms With 50 or More Employees

Currently, when a company hires its 50th employee, it must comply with numerous requirements, notably the election of workers' representatives and the establishment of a works council and a health and safety committee. All three bodies would be folded into a single one, the Social and Economic Council ("Comité Social et Économique").

A Definite-Term Employment Agreement Tailored to the Needs of Professional Sectors

The reform would change the rules applying to the definite-term employment agreement, where duration and renewal terms would be set at the industry level through collective bargaining agreements. Companies of the same professional sector would thus be able to tailor rules applying to the definite-term agreement to their needs.

First Steps Toward a Competitive Fiscal Environment

The new government has pledged to lower taxes to restore France's competitiveness and attract international business by reforming laws to favor entrepreneurs, investors and companies. The plan is set to unfold over several years, with the first measures to be adopted at the end of 2017.

Attracting High Earners

The introduction of a 75 percent tax on high earners at the start of former President François Hollande's term in 2012 largely contributed to an exodus of financiers and established France's reputation as a hostile tax location. President Macron is eager to reverse this reputation and make France a more accommodating place for the finance community.

He has proposed to significantly curtail the wealth tax, which is assessed annually on net assets in excess of €1.3 million, to cover only real property. That would leave other assets — in particular, investment portfolios — untouched. It remains unclear how the reform would affect shares in companies that derive the majority of their value from real property, such as real estate investment trusts.

Another key element of the reform is the planned introduction of a 30 percent flat tax on investment income (dividends, interest and capital gains from the sale of securities), which would replace the current taxation at the marginal rate of the income tax brackets (up to 45 percent) and of additional contributions (15.5 percent), with its complex system of allowances and rebates. Given the cost of this change, implementation is likely to be postponed until 2019.

France expanded its "inpatriate" regime — which now provides tax breaks for up to eight years to individuals moving to France to take a new job there — in 2016, shortly after the Brexit vote. The government has openly expressed hopes that the tax breaks, coupled with the restructuring of income taxation, will lure London-based bankers, asset managers and other entrepreneurs and professionals to Paris — and with them, the companies and businesses that employ them.

Attracting International Companies

At 34.43 percent, France's corporate income tax rate stands out in Europe as one of the highest and is largely seen as untenable. The previous administration had announced a progressive reduction down to 28 percent, and President Macron aims to lower it even further, to 25 percent by 2022. Investors should note that their effective tax rate may not fall by the same proportion, as the French tax authorities have grown more and more aggressive about cracking down on tax avoidance and denying standard exemptions (for instance, on intragroup dividends or on the sale of investment securities) in nonabusive situations.

If Paris is to become a serious contender as a financial center, the government will also have to address the financial transaction tax, which is assessed on transfers of equities in large, listed French companies. The administration has announced that it would reverse an extension of the tax scheduled for 2018, and President Macron's recent lukewarm support of the adoption of a similar tax at the European level may foreshadow the repeal of a tax that the French financial industry strongly opposes.

Conclusion

President Macron has requested that his administration be allowed to pass labor law reforms by decree rather than through the traditional channels of Parliament. The decrees are expected to be officially adopted on September 22, 2017, and published shortly thereafter. The new administration will also present its first budget and main tax reforms at the end of the month.

President Macron's ability to pass these measures will stand as the first test in his resolution to significantly reform the country. While he enjoys strong support in Parliament, public opinion and — to a lesser extent — trade unions have forced previous administrations to withdraw reforms backed by parliamentary majorities. France also runs a large deficit, which makes implementing any new tax breaks while trying to balance the budget challenging.

However, if these measures are passed, proposals for reform in other areas in need of modernization will likely follow in 2018.