

Opinion Leaders

Corporate / Private Equity / Financing

JANUARY 2009

No. 8

In this month's issue:

Editorial.....1

Legal and Tax Watch3

Recent Legal Advice and

Key Deals – Upcoming

Conferences12

EDITORIAL

Best wishes for 2009 and good luck!

2008 started out with no small uncertainty on a number of issues closely affecting French Private Equity players: entry into force of the TEPA act and its ISF wealth tax deduction, transposition into internal law of the European regulation on state aid and the *de minimis* rules, understanding and getting to grips with the consequences of the transposition of MiFID into internal law.

Then little by little, during 2008, like a bright patch in an overcast sky, some aspects of these complex regulations began to come clear and further details emerged, to more or less felicitous effect.

In the end, the outcome of the spring 2008 wealth tax campaign by investment funds proved to be exceptional, in spite of the uncertainties and a curtailed timetable.

These good results augur well for our economy and our SMEs, especially in the turmoil caused by the financial crisis.

After that, 2008 ended with the usual procession of diverse and varied reform proposals, with all the manifold fresh uncertainties that go with that process.

The most symptomatic of these proposals would have been the reform of the tax treatment of carried interest. From a shaky start, this ended up with a regime that was unnecessarily rigid and in certain respects unfair, particularly on all those who, as part of their professional activities, not only contribute to the creation and development of our businesses, but also invest a significant part of their wealth in them, probably from their own inclinations, but above all for the purpose of assuring their principals - the investors - that they both share the same interests.

As a result, everybody has now ended up in the same boat without any real reflection of the different levels of financial risk taken by different people.



Olivier DUMAS

Partner

Worse still, particularly against a lackluster economic backdrop, these people are being required to run even greater risks than their principals the investors: from now on, repayment of the amounts they invested is subject to repayment of investors' capital. This puts us back where we were six years ago!

Private Equity fund managers are, from now on, "for tax purposes" required to bear a disproportionate share of any losses that they make on financial investments. Even the investors themselves didn't ask for all that! What is more, yet again, foreign investors may think of this "practice" as being specifically a French peculiarity: no foreign Private Investment fund places such a restriction on its managers, nor do any foreign regulations.

The other subject that would again have been in everyone's mind at the end of that year would have been the fate of the future of the ISF wealth tax deduction in the TEPA act, particularly the one allowing ISF holding companies to be set up. Exit holding companies offering investments to the public or those doing so with a constitution not allowing them the benefit of this tax treatment.

Finally, that year-end would see a few further details of the "contractual FCPR" regime emerge, after the AMF published FAQs on this new type of fund. However, some uncertainties also remained on this apparently promising vehicle.

Spring is coming. We hope that plenty of illumination will arrive with it.

Legal and Tax Watch

Finance Act 2009

The Finance Act 2009 appeared in the Journal Officiel of 28 December 2008, bringing a certain number of reforms that we outline in the table below, differentiating the measures applicable to individuals from those applicable to legal entities:

Individuals		Finance Act article (CGI tax code article)	Effective from
Changes to income tax rates and bands	The bands are increased by 2.9%	art. 2 (art. 197)	1/01/2009 (2008 income taxable in 2009)
Changes to wealth tax [ISF] rates and bands	The exemption threshold is raised to €790,000 and the bands are also increased by 2.9%	art. 2 (art. 885 U)	1/01/2009
Overall tax deductions and allowances cap	The total tax advantages deriving from a number of deductions/allowances cannot give rise to an income tax deduction of greater than €25,000, increased by an amount equal to 10% of the net taxable revenue of the family tax group. Particularly affected are tax allowances in respect of: <ul style="list-style-type: none"> - subscriptions to share capital in SMEs and shares/units in French FCPI and FIP innovation and local area investment funds, - the Robien-Borloo [buy-to-let property] relief, - the Malraux [property restoration] relief, - investments in French overseas territories, - employing a domestic worker, - loan interest borne for acquisition of principal residence, - plant and machinery for sustainable development 	art. 91 (art. 200 quaterdecies III)	Income tax 2009
Capital gains on securities	The exemption threshold rises from €25,000 to €25,730	art. 2 (art. 150-0 A)	1/01/2009
Wealth tax [ISF] holding companies	In addition to the existing requirements, investment in a	art. 106 (art. 885-0 V)	Payments made from

	holding company will not give rise to a wealth tax reduction unless the company: - does not have more than 50 shareholders or unit holders, and - its corporate offices are exclusively natural persons, and - it provides no capital guarantee to its shareholders or unit holders in consideration for their subscriptions nor any automatic exit arrangements at the end of five years.	bis)	the deadline for filing the 2009 return
Carried interest shares	Tightening of restrictions for qualifying for the capital gains on securities tax treatment.	art. 15 (art. 150-0 A, 163 quinquies C and 80 quindecies)	Date of publication of the implementing legislation and at the latest, 30/06/2009
Distribution of FCPR assets	Where the share/unit holder in an FCPR venture capital fund (individual or legal entity liable to corporate tax) sells or has shares redeemed on which he has received a distribution of assets, the tax exempt proportion of that distribution will serve to reduce the share/unit subscription or purchase price.	art. 15 (art. 38 and 150-0 D)	1/01/2009
Legal entities			
Offset of losses of foreign subsidiaries	Provision for SMEs to offset losses of foreign subsidiaries or branches subject to them being: - at least 95% owned, and - established in an EU member state or a state that has concluded a double tax convention with France containing an administrative assistance clause, and - subject to a tax equivalent to French corporate income tax.	art. 22 (art. 209 C)	Affects accounting periods starting on or after 1/01/2009
IFA [French minimum corporate tax]	Phased abolition of IFA over three years.	art. 14 (art. 223 septies, 1681 septies)	Between 1/01/2009 and 1/01/2011
Golden parachute termination payments	Golden parachute termination payments paid to listed company directors will not qualify for deduction against the company's	art. 21 (art. 39)	Accounting periods ending on or after

	net profit unless they are limited to six times the annual social security cap per recipient (€205,848 in 2009).		31/12/2008
Real estate gains	Certain real estate gains will no longer be taxed at the 16.5% rate, but at the 19% rate.	art. 25 (art. 219)	Capital gains realized on or after 1/01/2009
R&D tax credits	Certain subcontracted expenditure will be included in the calculation of R&D tax credits.	art. 27 and 101 (244 quater B)	R&D tax credits calculated in respect of 2008

Overview of the new tax treatment of carried interest securities (units, shares, rights)

1- What is the scope of the new regime?

- Income affected:
 - Distributions from gains and,
 - net profits realized, directly or through an intermediary, on sale or redemption of carried interest securities.

- Securities involved:

Carried interest securities issued in the form of:

- FCPR, FCPI and FIP [innovation fund, local area investment fund] shares/units,
- and venture capital shares,
- rights representing a financial investment in an entity set up in an EC member state or in an EEA state that has concluded a double tax convention with France containing an administrative assistance clause for combating fraud and tax evasion and the principal objective of which is investing in unlisted companies.

You are reminded that carried interest securities comprise only those that:

- give rise to differential rights over the net assets or income of the issuing structure, and
- the allotment of which depends on the person's position and status.

- Persons affected

Employees and directors of the following structures:

- venture capital companies,
- FCPR management companies,
- SCR management companies,
- entities as above,
- companies that render services relating to the management of FCPR or SCR funds or entities.

2- What is the new tax treatment of these securities?

a – Exception: taxation per the gains on securities regime

Distributions pertaining to these securities as well as capital gains realized on sale of these securities (as defined above) are in principle taxable to the regime for capital gains on securities contained in article 150-0 A) of the CGI. They are therefore taxable at the rate of 18% to which must be added social security contributions which in 2009 amount to 12.1% (CSG, CRDS, and the additional 1.1% RSA solidarity contributions); making an overall rate of 30.1%.

To take advantage of this regime, all the following conditions have to be met:

- the seller must be in receipt of normal remuneration under an office or employment contract that allowed him to subscribe for or to acquire the shares;
- the shares sold were subscribed for or acquired in consideration for a price corresponding to the value of the securities;
- carried interest securities constitute a single category of security;
- these securities must represent at least 1% of the total amount of subscriptions in the issuing structure. Nevertheless, the decree issued implementing the AMF opinion will determine cases in which a lower threshold could be set (this might apply to FCPIs and FIPs or depend upon certain investment policies).
- the amounts or consideration to which the securities give entitlement must be paid within five years after the date that the FCPR fund is set up or these shares and rights are issued. Furthermore, for FCPR venture capital fund units, including FCPI and FIP units, this must also be paid after repayment of other unit holders' (investors') capital.

b – Principle: taxation per the income from employment regime

If the above conditions are not met, distributions and profits are taxable to income tax according to the rules applying to income from employment.

This new tax treatment will apply to FCPR venture capital funds set up and to shares and rights issued on or after the date of publication of the implementing legislation, or at the latest 30 June 2009. Up to that date, the Instruction of 23 March 2002 will continue to apply.

Legal News

Publication of the law promoting income from work

Act no. 2008-1258 of 3 December 2008 promoting income from work, which reforms the treatment of stock-option, incentive and profit sharing plans was published in the Journal Officiel of 4/12/2008. In particular, it authorizes businesses with incentive schemes to make a payment before 1st October 2009 of an exceptional bonus capped at €1,500 per payee, attracting the same exemptions as the incentive plan.

Decree no. 2008-1341 of 17 December 2008 setting a cap on holdings by simplified FCPRs of unlisted company debt.

Simplified FCPRs are authorized *"up to the limit of their assets set by decree"* to acquire unlisted company debts.

The decree which has just appeared sets this limit at 15%. To calculate this limit, the denominator is the higher of the two following amounts: fund net assets or the fully paid-up amount of subscriptions to the fund (art. D. 214-50-1 of the CMF [Financial Markets Committee]).

Marketing of financial instruments, savings product and life assurance: codes of conduct for relations between producers and distributors

Order no. 2008-1271 of 5 December 2008 authorizes the Minister of Finance to approve the codes of best conduct that will be produced in the near future by the professional bodies representing the finance and insurance industries (Journal Officiel of 6/12/2008). The purpose of the codes is to govern the relations between the product issuers and distributors, for marketing financial instruments, savings products and life insurance. They are to define the information and advisory obligations of financial intermediaries who sell savings, investment or life insurance products. Furthermore, to improve the quality of documentation advertising these products, the entity designing the financial products must monitor the correctness of the promotional documentation used by the distributor.

"Side pocket" UCITS: following the order of 23 October 2008

The order of 23 October 2008 reforming the framework for third-party asset management authorizes all UCITS (SICAV and FCPs, open- and closed-ended funds) to transfer certain of their assets, disposal of which would not be in the interest of their investors, to a new structure of the same type (SICAV or FCP).

A decree 12 December 2008 (Journal Officiel of 14/12/2008) gives details of the conditions applying to the structure set up to receive these assets. In particular, it provides that transfer of a SICAV's assets can only be made to a contractual open-ended investment fund (art. D. 214-20-3 of the CMF). Similarly, an FCP mutual

fund can only transfer its assets to a contractual closed-ended fund (art.. D. 214-22-1 of the CMF).

Finally, parts III and IV of the AMF General Regulations have had several articles added on the subject and the AMF has produced a number of clarifications in a document published on 22 December: *"Questions and answers relating to UCITS spin outs under paragraph 2 of article L. 214-19 or paragraph 2 of article L. 214-30 of the Monetary and Financial Code"*.

The decree of 18 December 2008 on recognition of the NYSE LIFFE market

The NYSE LIFFE market is henceforth a foreign market recognized within the meaning of article L. 423-1 of the Monetary and Financial Code.

Insurance companies: new prudential and accounting provisions

A decree of 22 December 2008 containing various prudential provisions applicable to insurance bodies in particular determines the cases in which the Regulatory Authority can require a higher solvency ratio of an insurance business, or conversely to limit it, together with an impairment provision.

Finally a decree of 29 December 2008 ratifies regulation no. 2008-14 of the French Accounting Regulation Committee on the presentation of pro forma information on the consolidation and combination rules for businesses governed by the insurance code.

The decree of 29 December 2008 ratifying regulations no. 2008-13, no. 2008-15, no. 2008-16 and no. 2008-17 of the Accounting Regulation Committee

The various regulations mainly cover:

- the presentation of the pro forma information of regulation no. 99-07 of the Accounting Regulation Committee on consolidation rules;
- the accounting treatment of plans for options for purchase or subscription for shares and plans for employee share award schemes.

Order on the reform of the law on businesses in difficulty

Order no. 2008-1345 of 18 December 2008 on the reform of the law of businesses in difficulty makes the protection procedure more attractive by easing the access criteria and increasing protection for the head of the enterprise. It also improves liquidation procedures, speeding up progress of operations for the smallest businesses and promotes lending to businesses through increased effectiveness of certain guarantees in the event of liquidation. This Order will come into force on 15 February 2009.

Order on the reform of the law on financial instruments

Published in the Journal Officiel of 9 January, it gives a new definition of financial instruments. These now include, on one hand, financial contracts (that is to say forward contracts appearing on a list laid down by decree) and, on the other hand, financial securities.

This is an example of something that, although already modified in 2007 by the MiFID directive, will now undergo fresh changes following last October's Order on asset management. Greater stability in our system would be desirable. This is of course just wishful thinking since at least two other Orders are expected in the coming weeks. These will apply to SICAFs [closed-end investment funds] and to publicly traded companies on their transparency obligations.

Decree of 5 January 2009 on cross-border company mergers

The decree particularly sets out the information that must appear in the joint merger project and the project notification to be gazetted.

European news

The Commission launches a public consultation on hedge funds

The European Commission launched a public consultation on hedge funds, particularly on systemic risk, the integrity and efficiency of markets, risk management, and transparency in respect of investors and investor protection. The consultation ends on 31 January 2009.

State Aid: the European Commission has reviewed state aid de minimis thresholds and private equity guidelines upwards

On 17 December last, the European Commission adopted a new framework for state aid. This is a temporary framework: it is to apply from 17 December 2008 to 31 December 2010. It provides for de minimis aid levels to rise from €200,000 to €500,000 (over 3 fiscal years) and the cap on Private Equity set at €1.5 million now rises to €2.5 million (over 12 months).

It is to be hoped that the French government authorities will act swiftly to bring our legislation into line, whenever necessary, particularly on the subject of the wealth tax deduction.

Tax news

Amended Finance Act 2008

Act no. 2008-1443 of 30 December 2008 amending Finance Act 2008 (Journal Officiel of 31/12/2008) deals mainly with the reform of tax procedures (procedure for abuse of law, advance rulings, audits, etc), and partly also with the economic recovery plan.

It should nevertheless be noted that the income tax deduction granted for investment in SMEs (the "Madelin" act) was, subject to certain conditions, increased. Indeed, subject to the recipient company meeting certain additional conditions (company less than 5 years old, employing less than 50 staff, with annual revenues or balance sheet total of below €10 million), the tax deduction can amount to €12,500 or €25,000 depending on whether the taxpayer is single or married.

Finally to take into account the publication of the Commission Regulation (EC) No 800/2008 of 6 August 2008 declaring certain types of aid compatible with the common market in application of articles 87 and 88 of the treaty (General regulation of exemption by category), which in Annex I contains a definition of SMEs, the Finance Act updated several articles of the CGI which referred back to annex I of the Commission Regulation No (EC) 70/20001 of 12 January 2001 concerning application of articles 87 and 88 the EC treaty to state aid for SMEs: articles 199 terdecies-0 A ("Madelin" deduction), 885-0 V bis (wealth tax deduction for investment in SMEs). In practical terms this amendment has no effect since the definition of an SME is unchanged.

Most recent legislation and Instructions published:

- **Decree no. 2008-1403 of 19 December 2008 applying article 199 terdecies-0 B of the French General Tax Code**
The decree relates to the income tax deduction for borrowings incurred for buying into a business.
- **Instruction 5 F-1-09 of 5 January 2009:** Options for subscription or purchase of shares. Comments on articles 38, 39, 43 and 62 of the Law promoting profit-sharing and employee share ownership and article 8 of the Law promoting work, employment and purchasing power and article 74 of the Finance Act 2008.
- **Instruction 4 H-10-08 of 26 December 2008:** Tax credits for industrial, commercial and agricultural businesses incurring R&D expenditure.

- **Instruction 4 H-9-08 of 24 December 2008:** Impact on companies - Exemption for profits made by companies formed to take over an industrial business in difficulties.
- **Instruction 4 E-2-08 of 24 December 2008:** Industrial and commercial profits - Corporate income tax - Provision for impairment in equity investments - Deduction limits.
- **Instruction 4 H-8-08 of 22 December 2008:** Corporate income tax – Sundry provisions - Tax treatment of groups of companies.
- **Instruction 4 H-7-08 of 9 December 2008:** Corporate income tax - Tax treatment of holding companies - Article 21 of the Amended Finance Act 2007.
- **Instruction 4 C-6-08 of 25 November 2008:** Costs and expenditure (Industrial and commercial profits, corporate income tax, Common provisions). Interest on third-party equity. Conditions and limits for deduction of interest on advances granted by shareholders over and above their shareholding. Maximum rates of interest deductible for tax purposes.

AMF news

Chairmanship of AMF

On 15 December, Mr Jean-Pierre Jouyet took over the chairmanship of the AMF succeeding Mr Michel Prada. Gérard Rameix may also leave the AMF in the next few weeks to move to the Cour des comptes.

Instruction 2008-06 of 9 December 2008 relating to the organization of portfolio manager companies and investment service providers on behalf of third parties on the subject of valuation of financial instruments

In outline, this regulation applies to portfolio manager companies and investment service providers providing portfolio management services on behalf of third parties. It deals with the valuation of financial instruments held by UCITS, OPCI real estate funds and as part of asset management mandates. It will not apply to shares or securities convertible into shares or to unquoted debt securities held as assets by FCPRs, employee savings plan UCITS holding the businesses' own shares, or for OPCI real estate funds.

This Instruction sets out a certain number of principles: the valuation must be accurate and independent; the valuation methods must be appropriate and therefore *"the investment service provider may not make use of financial instruments that they cannot value"*; the investment service provider must establish and maintain formal valuation and operational procedures, proportional to the type and complexity of the financial instruments involved; they must analyze changes in price of the financial instruments at suitable intervals of time, especially using movements in various market data and put in place an independent check of the valuation made

AMF consultation on its draft general regulation relating to offering investments to the public

To prepare for coming amendments on offers to the public (and the purchase of shares), the AMF has put the amendments that it intends to make to its general regulations out for consultation. It makes one important stipulation: exemptions from the rules for offers to the public should no longer be limited only to public companies and limited partnerships.

New FCPR regulations

The COB Instructions of 6 June 2000 relating in part to approved FCPRs including FCPIs and FIPs, and also to light-regulation FCPRs should soon be replaced by four new regulations. The first two, which have been the subject of industry consultation, deal with Fund approval and returns procedures together with information for unit holders. The remaining two which have not at this stage been released for consultation are expected to deal with the contents of fund prospectuses.

Recent Legal Advice and Key Deals: Upcoming conferences

Recent Legal Advice and Key Deals:

- secondary sale of portfolios;
- tax cases on article 209 B;
- tax cases on SCR "taxe professionnelle" [Regional business tax];
- study on the marketing of unlisted company securities/IT trading platform;
- implementation and monitoring of an ad hoc mandate to seek buyers for a holding in an investment fund portfolio;

- consultation on the liability of directors/shareholders in the event commencement of insolvency proceedings;
- projected sale of controlling holdings in a company listed on Eurolist B;
- consultation on the regulatory conditions for providing post-market services (clearing, settlement-delivery) in France (in a European context);
- consultation on the regulatory obligations applying to French investment service providers providing certain investment services to customers located outside the EU/EEA;
- consultation on the obligation to register with the SEC for French investment service providers providing a certain number of US customers with financial investment advisory and depository services in France.

Upcoming conferences:

- **TEPA Capital, on 21 January at the Palais du Luxembourg (Paris)** - A day set aside for professionals in SME investment to better understand the finer points of the TEPA act. Contributions from Me Daniel Schmidt and Me Florence Moulin.

For all financial professionals and intermediaries involved (Business Angels, start-up funds, FCPIs, FIPs, financial/wealth advisors) this event will give them a clear idea of the TEPA/wealth tax relief addressing the many issues and questions raised by this innovative method of financing SMEs: - Investment holding encyclopedia? - How to spot good investment targets? - What's new for financial and wealth advisors? - How to become a professional Business Angel? - How to take advantage of the TEPA measures without falling foul of the law?

Full programme on <http://www.tepacapital.com/>



- **“Class Actions” seminar**, on 22 January from 9 AM to 5:30 PM, with Me Valérie Lafarge-Sarkozy and Me Nicolas Faguer as speakers, at Centre d’affaires Eurosites Georges V, 28 avenue Georges V, 75008 Paris. With the participation of Me Mireille Dany and Me Guillaume Kellner. This seminar is organized in partnership with Dii.
- **Club RH “Negotiations in company : principles and borders”**, on 22 January, Me Beatrice Pola as speaker, organized in partnership with AEF, in the Paris office of Proskauer Rose.
- **“Private Equity legal, tax and accounting news” seminar**, on 27 January from 9 AM to 6 PM at Pavillon Ledoyen, a seminar on current events organized by "Association Française des Investisseurs en Capital" (AFIC) with Me Olivier Dumas, Me Guillaume Kellner, Me Maïté Lavrilleux and Me Florence Moulin as speakers.
Full programme available on the AFIC site www.afic.asso.fr
- **Round-table conference - CRA / CLENAM Meeting**, about “the business angels investment in SME’s”, on 2 February from 6 PM to 8 PM, at the “Maison des Arts et Métiers” in Paris. With Me Daniel Schmidt as speaker.
- **Super Return International Conference**, from 2nd to 5th of February in Berlin, with the presence of the Private Equity teams from Boston, London and Paris (Me Olivier Dumas). Proskauer Rose is sponsor of this event.
- **Debate LJA about “Economic lay-off”**, on 3 February from 9 AM to 11:30 AM at the Hotel de Crillon in Paris, with Me Yasmine Tarasewicz as speaker.
- **“La Faute Inexcusable” conference**, on 5 February, with Me Valérie Lafarge-Sarkozy and Me Philippe Goossens as speakers, organized in partnership with the EACC, in the Paris office of Proskauer Rose.
- **Club RH “Revue de jurisprudence du droit du travail”**, on 12 February, with Me Beatrice Pola as speaker, organized in partnership with AEF in the Paris office of Proskauer Rose.
- **IBA Corporate Counsel Forum**, from the 22nd to the 23rd of February in Paris, with the participation of Me Grégoire Goussu. Proskauer Rose is sponsor of this event.
- **Club RH “Salariés étrangers - Salariés à l’étranger”**, on 19 March, with Me Beatrice Pola as speaker, organized in partnership with AEF in the Paris office of Proskauer Rose.

- **“Leaders criminal liability” conference**, on 27 March, with Me Philippe Goossens and Me Eric Deprez as speakers, organized in partnership with Dii.
- **Annual Conference of Investment Capital**, on 7 April from 8 AM to 6:30 PM in Palais Brongniart in Paris, with Me Daniel Schmidt as speaker, organized by the AFIC. Proskauer Rose is sponsor of this event.

Corporate / Private Equity / Financing

For more information about this practice area, contact:

Daniel Schmidt
33.1.53.05.60.00 – dschmidt@proskauer.com

Florence Moulin
33.1.53.05.60.00 – fmoulin@proskauer.com

Publication E-mail: leaders.dopinion@proskauer.com

This publication is a service to our clients and friends. It is designed only to give general information on the developments actually covered. It is not intended to be a comprehensive summary of recent developments in the law, treat exhaustively the subjects covered, provide legal advice, or render a legal opinion.

BOCA RATON | BOSTON | CHICAGO | HONG KONG | LONDON | LOS ANGELES | NEWARK | NEW ORLEANS | NEW YORK | PARIS |
SÃO PAULO | WASHINGTON, D.C.
www.proskauer.com

© 2008 PROSKAUER ROSE LLP. All Rights Reserved. Attorney Advertising..