THE TAX DISPUTES AND LITIGATION REVIEW

SIXTH EDITION

Editor
Simon Whitehead

THE LAWREVIEWS

THE TAX DISPUTES AND LITIGATION REVIEW

SIXTH EDITION

Reproduced with permission from Law Business Research Ltd
This article was first published in March 2018
For further information please contact Nick.Barette@thelawreviews.co.uk

Editor
Simon Whitehead

THE LAWREVIEWS

PUBLISHER
Tom Barnes

SENIOR BUSINESS DEVELOPMENT MANAGER
Nick Barette

BUSINESS DEVELOPMENT MANAGERS
Thomas Lee, Joel Woods

ACCOUNT MANAGERS
Pere Aspinall, Sophie Emberson,
Laura Lynas, Jack Bagnall

PRODUCT MARKETING EXECUTIVE
Rebecca Mogridge

RESEARCHER
Arthur Hunter

EDITORIAL COORDINATOR
Gavin Jordan

HEAD OF PRODUCTION
Adam Myers

PRODUCTION EDITOR
Martin Roach

SUBEDITOR
Anna Andreoli

CHIEF EXECUTIVE OFFICER
Paul Howarth

Published in the United Kingdom
by Law Business Research Ltd, London
87 Lancaster Road, London, W11 1QQ, UK

www.TheLawReviews.co.uk

ISBN 978-1-912228-16-4

Printed in Great Britain by
Encompass Print Solutions, Derbyshire
Tel: 0844 2480 112

© 2018 Law Business Research Ltd

THE LAW REVIEWS

THE MERGERS AND ACQUISITIONS REVIEW

THE RESTRUCTURING REVIEW

THE PRIVATE COMPETITION ENFORCEMENT REVIEW

THE DISPUTE RESOLUTION REVIEW

THE EMPLOYMENT LAW REVIEW

THE PUBLIC COMPETITION ENFORCEMENT REVIEW

THE BANKING REGULATION REVIEW

THE INTERNATIONAL ARBITRATION REVIEW

THE MERGER CONTROL REVIEW

THE TECHNOLOGY, MEDIA AND TELECOMMUNICATIONS REVIEW

THE INWARD INVESTMENT AND INTERNATIONAL TAXATION REVIEW

THE CORPORATE GOVERNANCE REVIEW

THE CORPORATE IMMIGRATION REVIEW

THE INTERNATIONAL INVESTIGATIONS REVIEW

THE PROJECTS AND CONSTRUCTION REVIEW

THE INTERNATIONAL CAPITAL MARKETS REVIEW

THE REAL ESTATE LAW REVIEW

THE PRIVATE EQUITY REVIEW

THE ENERGY REGULATION AND MARKETS REVIEW

THE INTELLECTUAL PROPERTY REVIEW

THE ASSET MANAGEMENT REVIEW

THE PRIVATE WEALTH AND PRIVATE CLIENT REVIEW

THE MINING LAW REVIEW

THE EXECUTIVE REMUNERATION REVIEW

THE ANTI-BRIBERY AND ANTI-CORRUPTION REVIEW

THE CARTELS AND LENIENCY REVIEW

THE TAX DISPUTES AND LITIGATION REVIEW

THE LIFE SCIENCES LAW REVIEW

THE INSURANCE AND REINSURANCE LAW REVIEW

THE GOVERNMENT PROCUREMENT REVIEW

THE DOMINANCE AND MONOPOLIES REVIEW

THE AVIATION LAW REVIEW

THE FOREIGN INVESTMENT REGULATION REVIEW

THE ASSET TRACING AND RECOVERY REVIEW

THE INSOLVENCY REVIEW

THE OIL AND GAS LAW REVIEW

THE FRANCHISE LAW REVIEW

THE PRODUCT REGULATION AND LIABILITY REVIEW

THE SHIPPING LAW REVIEW

THE ACQUISITION AND LEVERAGED FINANCE REVIEW

THE PRIVACY, DATA PROTECTION AND CYBERSECURITY LAW REVIEW

THE PUBLIC–PRIVATE PARTNERSHIP LAW REVIEW

THE TRANSPORT FINANCE LAW REVIEW

THE SECURITIES LITIGATION REVIEW

THE LENDING AND SECURED FINANCE REVIEW

THE INTERNATIONAL TRADE LAW REVIEW

THE SPORTS LAW REVIEW

THE INVESTMENT TREATY ARBITRATION REVIEW

THE GAMBLING LAW REVIEW

THE INTELLECTUAL PROPERTY AND ANTITRUST REVIEW

THE REAL ESTATE M&A AND PRIVATE EQUITY REVIEW

THE SHAREHOLDER RIGHTS AND ACTIVISM REVIEW

THE ISLAMIC FINANCE AND MARKETS LAW REVIEW

THE ENVIRONMENT AND CLIMATE CHANGE LAW REVIEW

THE CONSUMER FINANCE LAW REVIEW

THE INITIAL PUBLIC OFFERINGS REVIEW

THE CLASS ACTIONS LAW REVIEW

THE TRANSFER PRICING LAW REVIEW

THE BANKING LITIGATION LAW REVIEW

THE HEALTHCARE LAW REVIEW

THE PATENT LITIGATION LAW REVIEW

THE THIRD PARTY LITIGATION FUNDING LAW REVIEW

THE TRADEMARKS LAW REVIEW

www.TheLawReviews.co.uk

ACKNOWLEDGEMENTS

The publisher acknowledges and thanks the following law firms for their learned assistance throughout the preparation of this book:

BUSTAMANTE & BUSTAMANTE LAW FIRM

CHEVEZ RUIZ ZAMARRIPA Y CIA, SC

DDTC CONSULTING

DLA PIPER

FLICK GOCKE SCHAUMBURG

GARRIGUES PORTUGAL, SLP

GORRISSEN FEDERSPIEL

GUZMÁN ARIZA, ATTORNEYS AT LAW

JOSEPH HAGE AARONSON LLP

KPMG LAW ADVOKATFIRMA AS

LENZ & STAEHELIN

LEWIN & WILLS

LOYENS & LOEFF

MACHADO, MEYER, SENDACZ E OPICE ADVOGADOS

MAISTO E ASSOCIATI

MASON HAYES & CURRAN

MORRISON & FOERSTER LLP

NORTON ROSE FULBRIGHT CANADA LLP

OLD SOUTH BRITISH CHAMBERS

PHILIPPE DEROUIN

PHILIPPI PRIETOCARRIZOSA FERRERO DU & URÍA

PHOENIX LEGAL

PWC LEGAL

SELE FROMMELT & PARTNER ATTORNEYS AT LAW LTD

SOŁTYSIŃSKI KAWECKI & SZLĘZAK

STAVROPOULOS & PARTNERS LAW OFFICE

STREAMSOWERS & KÖHN

TMI ASSOCIATES

VAN CAMPEN LIEM

WASELIUS & WIST

WITHERS KHATTARWONG

CONTENTS

PREFACE

The objective of this book is to provide tax professionals involved in disputes with revenue authorities in multiple jurisdictions with an outline of the principal issues arising in those jurisdictions. In this, the sixth edition, we have continued to add to the key jurisdictions where disputes are likely to occur for multinational businesses.

Each chapter provides an overview of the procedural rules that govern tax appeals and highlights the pitfalls of which taxpayers need to be most aware. Aspects that are particularly relevant to multinationals, such as transfer pricing, are also considered. In particular, we have asked the authors to address an area where we have always found worrying and subtle variations in approach between courts in different jurisdictions, namely the differing ways in which double tax conventions can be interpreted and applied.

The idea behind this book commenced in 2013 with the general increase in litigation as tax authorities in a number of jurisdictions took a more aggressive approach to the collection of tax; in response, no doubt, to political pressure to address tax avoidance. In the UK alone we have seen the tax authority vested with broad new powers not only of disclosure but even to require tax to be paid in advance of any determination by a court that it is due. The provisions empower the revenue authority, an administrative body, to compel payment of a sum, the subject of a genuine dispute, without any form of judicial control or appeal.

Over the past year, the focus on perceived cross-border abuses has continued with action by the European Commission on past tax rulings in Ireland, Luxembourg and Belgium and the BEPS reaching a crescendo in the announcement of a 'diverted profits tax' to impose an additional tax in the UK when it is felt that a multinational is subject to too little corporation tax even in an EU context. The general targeting of cross-border tax avoidance now has European legislation behind it with the passage this year of the second Anti-Tax Avoidance Directive. The absence of much previous European legislation in direct tax has always been put down to the need for unanimity and the way in which Member States closely guard their taxing rights. The relatively speedy passage of this legislation (the Parent–Subsidiary Directive before it took some 10 years to pass) and its restriction of attractive tax regimes indicates the general political disrepute with which such practices are now viewed.

These are, perhaps, extreme examples, reflective of the parliamentary cycle, yet a general toughening of stance seems to be felt. In that light, this book provides an overview of each jurisdiction's anti-avoidance rules and any alternative mechanisms for resolving tax disputes, such as mediation, arbitration or restitution claims.

We have attempted to give readers a flavour of the tax litigation landscape in each jurisdiction. The authors have looked to the future and have summarised the policies and approaches of the revenue authorities regarding contentious matters, addressing important

questions such as how long cases take and situations in which some form of settlement might be available.

We have been lucky to obtain contributions from the leading tax litigation practitioners in their jurisdictions. Many of the authors are members of the EU Tax Group, a collection of independent law firms, of which we are a member, involved particularly in challenges to the compatibility of national tax laws with EU and EEA rights. We hope that you will find this book informative and useful.

Finally, I would like to acknowledge the hard work of my colleague Ibar McCarthy in the editing and compilation of this book.

Simon Whitehead
Joseph Hage Aaronson LLP
London
February 2018

Chapter 12

FRANCE

Philippe Derouin[1]

I INTRODUCTION

The French system for assessing, auditing and challenging taxes has been extremely constant over the past few decades. The major changes essentially reflect progress in technology (use of digital data and equipment in tax audits, tax filings, tax payments and dispute procedures), the growing influence of international instruments of human rights and European Union law, and a tendency of both the tax authorities and taxpayers to be more aggressive than they used to be. Alternative dispute resolution methods have not developed, and a very effective method was terminated in 2010.

The French tax system is largely based upon self-assessment, with taxpayers filing their tax returns, and often assessing their own tax, on the basis of their assessment of the facts and interpretation of the law. In recent years, the filing and reporting obligations of taxpayers have been increased substantially, especially with respect to their cross-border assets and activities. Likewise, the French tax authorities have been granted easier access to widened means of information by the legislator in domestic situations and by international instruments in matters containing a foreign element.

Statutes of limitation have been successively amended to reduce limitation periods for certain taxpayers' claims, and to extend the periods available to the tax authorities for making reassessments or initiating criminal procedures. The criminal periods of limitation have been doubled, and no effective limitation applies to money laundering of the proceeds of tax fraud.

Statistics published by the French tax authorities in their annual report show that the overall number of tax reviews by the French tax authorities remains stable. A vast majority consists of unilateral reviews by a tax auditor of documents available to the authorities both for individuals (close to 1 million of them in total) and businesses (close to 300,000 of them in total). Taxpayers must be informed of the outcome of such reviews and may comment before the tax is assessed. More formal audit procedures are more inquisitive, and involve both a discussion with the taxpayer and counsel and access to an internal review. Their numbers are tending to slowly decline: in 2016, 45,314 audits with accounting checks were carried out with businesses, and 3,557 thorough audits of personal situations took place with individuals.

The amounts of reassessments and penalties slowed down to €19.5 billion in 2015, partly because of the voluntary disclosure programme for individuals holding assets abroad. Corporation tax reassessments also went down to €4 billion. The total amount of taxes and

1 Philippe Derouin, a member of the Paris Bar, runs his own law firm, Philippe Derouin.

penalties assessed in serious frauds (defined as triggering 40 per cent penalties or more after a tax audit) also went down to €4.9 billion, although this represents the same 31 per cent proportion of tax and penalties assessed in formal tax audit procedures over preceding years.

The amount and proportion of tax and penalties effectively collected over a period remain at approximately 55 per cent of the assessed amounts. This relatively stable proportion slightly increased to 57 per cent in 2015 and 2016 as a result of the voluntary disclosure programme. A 55 per cent proportion tends to confirm that a substantial amount of the taxes and penalties assessed after a tax audit are effectively reduced, by approximately €8 billion in total per year, as a result of internal reviews by, or negotiations with, the French tax authorities resulting in pre-litigation settlements; and also in pursuance of court decisions upon disputes.

II COMMENCING DISPUTES

Although there can be many steps, or administrative decisions, before a tax is assessed, taxpayers are generally barred from initiating any action until a tax is assessed. Only few exceptions enable an actual or potential taxpayer to start an action before a tax deed has been issued.

i Petitions for judicial review of administrative guidelines

Taxpayers, and certain taxpayers' associations, may file petitions for a judicial review of administrative guidelines that may be declared illegal on any point where they give an interpretation of the tax law that differs from the decision of an administrative judge on the relevant point. Such procedures have been used, successfully at times, to shortcut the lengthy administrative and judicial process of a tax controversy. Some of these petitions may be the basis for the administrative court to refer a preliminary question either to the Constitutional Council on certain matters where a legislative provision is challenged against any fundamental human rights enshrined in the French Constitution, or the European Court of Justice (ECJ) where a question of EU law is involved.

The recent challenge to the 3 per cent corporation tax surcharge on distributed amounts provides such an example where petitions were filed by certain taxpayers and by AFEP, the French association of large businesses, before the Council of State in 2016. Both categories of petitioners claimed the administrative guidelines were illegal because they commented upon a piece of legislation that was against the principle of equal rights on certain points and contrary to the EU Parent–Subsidiary Directive on other points. The Council of State decided in June 2016 to refer the equal treatment point to the French Constitutional Council, and the Directive points to the ECJ. The Constitutional Council found the law to be discriminatory and unconstitutional in a ruling of 30 September. The law was amended accordingly by the Finance Act of 29 December 2016, which extended the benefit of an exemption for intragroup dividends to domestic, European and most third-country corporate relationships. The EU case was decided by the ECJ in May 2017 after which the French Council of State further referred the case to the French Constitutional Council, which finally decided in October 2017 that the 3 per cent surcharge on dividends was entirely unconstitutional. The cost to the government approximated €10 billion and required an extraordinary surcharge to partly finance it.

Other parallel procedures are less radical, and have both narrower scope and lower chances of success.

Petitions for judicial review could also be introduced with respect to individual decisions, such as an unsatisfactory ruling, notified to a taxpayer. The French tax courts have been excessively restrictive upon the admission of such petitions on the ground that, except in very special circumstances, the decision was not separable from the taxation procedure.

ii Pre-audit search warrants

Prior to a tax audit, the tax authorities may apply to a civil judge for a warrant to search premises and attach documents that could be used as evidence that a business is carried out in France and should be taxable in France. Approximately 200 searches are performed on that basis each year. Many undisclosed permanent establishments of foreign entities are being the purpose of such warrants. As a result of an European Court of Human Rights (ECHR) ruling in *Ravon*, French law was amended to the effect of allowing the potential taxpayer and the tenant of the searched premises to immediately appeal from the warrant to the president of the court of appeals and challenge the basis for the authorities' suspicions. They may also challenge the validity of the search on grounds of breach of confidentiality. Such appeals and challenges are commonly introduced shortly after the searches have been made and before the tax assessments are established. They seldom succeed in court. However, challenging the warrant may often be useful as it enables the potential taxpayer to access the documents supplied by the French tax investigators in their application for the warrant and bring forward certain points of defence to be considered, if not by the court, by the French tax authorities at a later stage.

After the search, the French tax authorities may use the collected documents against the potential taxpayer only after carrying out a full audit of its accounts with the assistance of a counsel and a discussion in person. The French tax authorities simultaneously send a request for omitted tax returns. Although the non-resident entity may claim it has no taxable presence in France, where it maintains no corporate accounts and consider that it has no tax return to file in France, it is generally advisable to cooperate with the French tax authorities.

Under French tax law, any audited business must supply its accounts and supporting documents for inspection, in their original digital format where applicable. Where cross-border transactions occur with related parties, the audited entity must also make its transfer pricing policy available to the French tax auditors. As a result, the French tax auditors would expect, and generally require, to review such documents, failing which they are entitled to formally record that they were not presented and to draw certain conclusions.

A non-resident entity that considers that it has no taxable presence in France presumably would not have separate accounts, or a transfer pricing policy, with respect to its operations in France, especially where these operations are carried out by a French subsidiary or other related entity. As a matter of law, there is no requirement for a foreign entity to have separate accounts for its French operations, even where carried out through a permanent establishment. Business entities established outside France and doing business in France from abroad accordingly are entitled to indicate that they did not maintain separate accounts but should be prepared to provide the relevant documents to French tax auditors. The accounting documents could be their full set of accounts in their original digital format and any relevant transfer pricing policy.

Depending upon the circumstances, these documents may support the position that the entity had no, or a limited, presence in France, with no or limited tax consequences. This may be true especially where the deemed permanent establishment in France can be seen as merely supplying support functions to the head office and principal activities abroad. In such

a situation, no VAT would apply, especially within the European Union, and the corporate income tax implications would not substantially differ from a transfer pricing adjustment, if any.

In anticipation of such possible outcomes, the potential taxpayer may defer to the request of the French tax authorities and file the corresponding tax returns within 30 days of the request to do so. In these tax returns, the foreign entity may indicate why there was no reportable VAT transaction in France or how the transfer pricing policy would result in no or limited taxable income attributable to the hypothetical French permanent establishment. If a reassessment occurs, the entity may claim treaty benefits where applicable and access the mutual agreement procedure.

This scenario implies that, at some stage, the investigated taxpayer makes the decision to either challenge the existence of the permanent establishment, including before the court, or to negotiate with the French tax authorities, concede the establishment and mitigate the French tax consequences.

As a means to press the non-resident entity for such admission, the French tax authorities may take the position that the permanent establishment was not only undisclosed but hidden or concealed. Such an ugly characterisation would result in an extended period of limitation (10 years instead of three or four) and the risk of a severe penalty (80 per cent instead of 10 per cent). Depending upon the circumstances, and the country of origin of the taxpayer, defences may be available either on both grounds or in relation to the penalty only.

iii Tax claims and challenges

French tax disputes commence when a tax is assessed or paid and the taxpayer either challenges the administrative reassessment or claims for a tax refund.

Under French tax procedure, the first step for challenging a tax assessment or for claiming a tax refund is a petition to the head of the relevant tax department whatever tax is involved and even where the tax was assessed according to the taxpayer's return. Around 3 million petitions are filed, and decided upon, each year, mainly with respect to income taxes assessed by the authorities on individuals or to local taxes. Businesses file approximately 50 to 56,000 such petitions on corporation tax and a similar number on VAT.

The petition must be filed, before any referral to any court, to the head of the tax office that has jurisdiction over the relevant tax. It must:

a specify the tax that is being challenged;
b provide a summary of the facts, pleas and arguments;
c be signed by the taxpayer or an authorised agent; and
d be accompanied by a copy of the Treasury claim concerned (assessment notice, collection notice or withholding document, in the case of withholding taxes).

Generally, the claim must be filed by 31 December of the second year following that of the assessment, collection notice or payment. An extension applies after a tax audit.

Submitting a claim does not exempt the taxpayer from the obligation to pay the taxes and penalties imposed. However, the taxpayer may request that payment be suspended. Suspension of payment is granted in exchange for the provision of guarantees (e.g., mortgage or pledge up to the amount of the principal taxes; penalties need not to be secured). The suspension remains until a lower court decision on the dispute is issued.

If the lower court rules in favour of the tax authorities, the suspended tax and penalties become payable, and the taxpayer would be liable to pay a 5 or 10 per cent surcharge plus

interest on the arrears. The rate of interest was 0.4 per cent per month or 4.8 per cent per annum up to 31 December 2017 and has been reduced to 0.2 per cent per month or 2.4 per cent per annum since 1 January 2018. Conversely, if the court finds for the taxpayer who has already paid the taxes claimed, the taxpayer is entitled to interest on arrears at the same rates. Considering the prevailing market rates, it has been and still could be financially advantageous for taxpayers to pay and not to apply for suspension.

The authorities must decide on a claim within six months. Failing a formal decision after six months or if the claim is totally or partially rejected, in writing or implicitly, the taxpayer is entitled to bring an action before the administrative or civil courts, depending on the case.

III THE COURTS AND TRIBUNALS

Where the taxpayer is not satisfied by a decision, the dispute may be brought before the courts. There are no special tax courts in France, and tax cases are heard by the common administrative, civil or criminal courts, depending upon the tax that is challenged or the penalty applied.

i Types of court

Administrative courts have jurisdiction over income tax, corporation tax, VAT and local taxes, and over the related tax penalties. Each year, approximately 20,000 tax cases are introduced in the lower administrative courts. In 2016, 3,879 appeals were recorded with administrative courts of appeals, and 440 further appeals were lodged with the Council of State, the supreme administrative court. Overall, the administrative courts decided partly or totally in favour of the taxpayers in approximately 12.4 per cent of the cases (13.6 per cent on VAT matters, and 14.8 per cent on income and corporation tax matters) in 2015.

Civil courts have jurisdiction over stamp duties, gift and inheritance taxes, annual wealth taxes and some excise duties, together with the related tax penalties. In 2016, 868 cases were filed with the lower civil courts, 220 with the courts of appeals and 58 with the Court of Cassation, the supreme court of the judiciary. Civil courts decided in favour of the taxpayers in approximately 33 per cent of the cases.

Criminal prosecutions may be initiated at the request of the tax authorities on any matter of tax fraud, which is widely defined, whatever the tax involved. Approximately 900 such procedures are held each year. Around 80 further procedures are investigated by the 'tax police', a special department of the prosecutor's office with tax auditors The criminal procedure for money laundering of the proceeds of tax fraud (no public statistics, so far) or for tax swindles (around 133 cases on VAT carousel and other tax credit cases) may be initiated by the public prosecutor without request from the tax authorities. Criminal sanctions such as fines and imprisonment may be applied on top of the tax penalties.

Each type of court comprises three levels: the first level consists of the administrative courts and the courts of first instance; the second level consists of the courts of appeal and the administrative appeal courts; and the highest level consists of the Court of Cassation and the Council of State, which generally rule only on points of law and not fact.

Each court may, and in certain situations must, refer certain questions either to the Constitutional Council or the ECJ. The Constitutional Council has exclusive jurisdiction to decide upon the conformity of French legislative provisions with the human rights protected by the Constitution, including the Declaration of Human and Civic Rights of 1789. Several

dozens of tax provisions have been reviewed accordingly upon the request of taxpayers. Referrals to the ECJ are commonly ordered by the Council of State or the Court of Cassation, including for tax matters. Lower courts are much more restrictive or reluctant to do so, and some, like the administrative courts of Paris, have never referred a tax case to the ECJ.

ii Proceedings

Before French courts, and particularly in relation to tax matters, the procedure is conducted primarily in writing, and results in an exchange of briefs and pieces of evidence between the taxpayer and the authorities.

The taxpayer must petition the court within a prescribed time following the formal rejection of its claim by the tax director. The time limit is generally two months. The petition must be reasoned and attach the tax deed, plus any piece of evidence the taxpayer would rely on, even where previously submitted to the tax authorities, since these are not expected to forward any of these to the court.

The assistance of a registered attorney is not legally required in the first instance. Before the appellate courts, representation by a registered lawyer is mandatory. Before the Council of State and Court of Cassation, the taxpayer must be represented by one of the 60 barristers admitted to represent clients before these supreme courts. This restriction does not apply before the Constitutional Council or the ECJ, where any registered lawyer may assist the parties, and the government is generally represented by its own agents.

No more than two briefs are commonly exchanged by each party, but this is not a hard rule. Following these exchanges, the court may, and often does, pronounce the closure of the period for submissions (also named 'instruction') and schedules a date for the hearing.

Administrative and civil courts conduct hearings differently and have different views of their own missions. Civil courts recognise taxpayers' right to a fair trial before them, in line with Article 6 of the European Convention of Human Rights.[2] Administrative courts have taken the opposite view on the grounds that Article 6 applies only to civil obligations and criminal charges, and would not apply to tax matters except where the tax penalties are equivalent to a criminal sanction. This position was not altered after the European Charter of Fundamental Rights, which does not distinguish between these positions, obtained treaty force in December 2009.

In practical terms, these differing views entail certain consequences, the most important of which are that the administrative courts consider that it is part of their mission to challenge the petition of the taxpayer, including on points of law and points of fact that are not discussed by the French tax authorities; and that in doing so, they are not raising a plea of their own motion, and accordingly can forgo from informing the parties (i.e., the taxpayer) and inviting them to submit their comments.[3]

Before both types of courts, a reporting judge summarises the case at a hearing. Witnesses and experts are not heard. Both parties are entitled to present oral arguments and plead their case (however briefly).

Before the administrative courts, a public reporter, who is a member of the court that does not participate in the decision-making, delivers an opinion that is based upon a draft judgment, and may raise issues that were not addressed by the parties. At this point, the parties are informed of such issues. They may then make very brief observations and,

2 C cass; Ass plén 14 June 1996 *Kloeckner*, bull civ AP No. 5.

3 Council of State 2 June 2010 No. 318014 *Fondation de France*.

where appropriate, file a 'post-hearing brief' to clarify any points that have been raised, or overlooked, by the public reporter. The court must consider this post-hearing brief and decide whether it reopens the case before reaching a decision.

iii Effectiveness of the system

The costs of such procedures are fairly limited and are not an obstacle for taxpayers to put their case. However, the length of the proceedings is a weakness that may dissuade taxpayers from initiating them. One reason is that the tax authorities often take a long time to reply to briefs filed by taxpayers, and taxpayers do not really have any way to compel the administration to issue a response.

It is not uncommon for the administrative courts of first instance to take up to three years to rule on a matter brought before them. Regarding appeals, it can take up to 10 years to resolve a tax dispute, which penalises the taxpayer more than the tax administration.

A taxpayer who has been unsuccessful before the national courts may apply to the ECHR where fundamental rights are at stake. However, this is extremely rare, even though, in certain cases, the judgments delivered by the ECHR have had a real impact on French tax procedures.[4]

IV PENALTIES AND REMEDIES

i Tax penalties

Default interest

Tax increases set by the tax offices are systematically increased through default interest of 0.2 (0.4 until 2017) per cent each month, that is, 2.4 (4.8 until 2017) per cent per annum. This default interest is not considered a penalty as such, but rather as fair compensation for the damage incurred by the Treasury owing to late payment of taxes by the taxpayer.

Since the default interest is not considered a penalty, it is applied automatically and does not have to be motivated by the tax authorities.

In practice, and for the same reason, it has become very difficult to obtain a total or partial exemption from default interest even when taxpayers act in good faith.

Surcharges

Assessments for back taxes are often accompanied by surcharges, the rate of which varies depending on the circumstances of the case and on whether the taxpayer is deemed to have acted in good faith.

A 10 per cent surcharge applies in cases of delay by the taxpayer in satisfying his or her declaratory obligations, plus default interest. A 40 per cent surcharge applies to unpaid taxes either where the taxpayer did not file its tax returns after a second formal request or where the authorities consider that the taxpayer's dissimulation of declared amounts was deliberate. This latter surcharge is raised to 80 per cent in the event of fraud and 'abuse of the law'. The deliberate nature of offences (*mens rea*) must be demonstrated by the tax authorities, who

4 See in particular ECHR, 21 February 2008 No. 18497/03 (*Ravon*) in connection with house searches, and ECHR 30 June 2011 No. 8916/05 (*Jehovah's Witnesses*) in connection with the retroactivity of tax measures.

apply the above penalties in approximately 30 per cent of reassessments following full audits, and who bear the onus of proof in the case of a challenge before the tax courts. Tax penalties may be, and often are, mitigated by the tax authorities to reach out-of court settlements.

ii Criminal penalties

On top of tax surcharges, criminal penalties may apply in a wide range of situations.

Legal and natural persons may be found guilty of tax evasion where they fraudulently evaded or tried to fraudulently evade the assessment or collection of tax. The French equivalent of deferred prosecution agreements now is available to legal entities, and the first such agreement was made with HSBC Private Bank Swiss to settle the criminal charges against it, including laundering of the proceeds of tax fraud. The agreement was approved by the president of the Paris court on 14 November 2017. It provides for a total payment of €300 million, made up of a criminal fine of €158 million, reported to be the maximum in the circumstances, and a €142 million indemnity to the French tax authorities, reported to have been based upon an average tax rate applied to the amount of managed assets less the sums recovered or to be recovered from the taxpayers.

Criminal penalties for 'ordinary' tax evasion include a fine of €500,000 and a prison sentence of up to five years. The fine is increased to €750,000 if the evasion was carried out or facilitated by means of purchases or sales without invoices, or where invoices do not relate to real transactions.

'Aggravated' tax evasion may be subject to a €2 million fine or seven years' imprisonment in situations where it was carried out or facilitated by using foreign bank accounts or entities such as trusts located in third countries, false identities or any false documents, fictional or artificial acts or entities, or abusive tax residence in another state. The same penalties would be applicable in cases of tax fraud carried out in organised groups. Any accessory to such offences may be charged with the same penalties.

The Constitutional Court found the French system to be compatible with the '*non bis in idem*' principle on the basis that criminal prosecutions are dedicated to the most serious offences, which may be selected by the tax authorities upon a favourable opinion from the Tax Offence Commission. As previously mentioned, the tax authorities file around 1,000 tax evasion complaints each year.

The statute of limitations applicable to the offence of tax evasion has been extended from three to six years by the Tax Fraud Act, which also introduced a 'repentance provision' according to which the offender may benefit from a reduction of a prison term on the condition that he or she helps the tax authorities to identify his or her accomplices.

V TAX CLAIMS

i Recovering overpaid tax

Taxpayers who believe they have paid too much tax and wish to claim it back must follow a procedure similar to that for challenging a tax reassessment. The procedure applies to a taxpayer residing abroad who has incurred French withholding tax at the statutory rate, and who wishes to invoke a bilateral tax treaty to benefit from a reduced rate of withholding tax and to claim back the excess tax paid. Both the non-resident taxpayer and the paying agent may lodge a claim with the relevant office (in this example, the tax office for non-residents) within the legal time limit. If the claim is implicitly or explicitly rejected, the taxpayer or the withholding agent may bring the case to the competent courts.

In the particular case where it is claimed the tax in question breaches EU law, taxpayers are entitled to demand an exemption from or a reduction of the taxes and the repayment of any excess based on the fact that the texts applied are contrary to EU law; and compensation for the damage incurred. The amount of tax repayment, plus interest, is assessed each year in the Finance Bill. Currently it stands at approximately €21 billion.[5]

The remedy follows the tax claim procedure described above, particularly as regards the time in which to file an action.

ii Challenging administrative decisions

Taxpayers and certain other persons may ask an administrative judge to review certain administrative decisions that they deem illegal within the framework of an abuse of power contest.

When examining an abuse of power contest against an administrative act upon which a tax is based, the administrative judge who finds the act to be illegal may declare it null, but may not decide upon the corresponding tax charges.

iii Claimants

Tax claims may be brought only by the taxpayer, or the withholding agent in the case of withholding taxes. Group actions are not allowed in tax disputes.

VI COSTS

Costs are limited to counsel and other fees, as the French administration of justice is free of charge.

Within the framework of court action, the losing party may be ordered to pay the successful party a sum intended to cover 'irrecoverable' costs.

A taxpayer whose action was unsuccessful may be ordered to compensate the Treasury for its legal costs.

Regardless of which party brings the action, incurred costs are almost never refunded in full. Compensation seldom exceeds a few thousand euros.

VII ALTERNATIVE DISPUTE RESOLUTION

Strictly speaking, in France there are no alternatives to the tax dispute resolution procedures described in this chapter.

However, at any time during the procedure, and even when the dispute is before the courts, the taxpayer can reach a settlement with the tax authorities to end the dispute.

In the context of such settlements, the parties generally agree on a tax base. Quite often, the authorities grant a partial or total exemption from penalties. It has been the French tax authorities' policy not to settle when they contemplate filing a criminal complaint or when the taxpayer has tried to delay the procedure in bad faith. In this respect, it was recently observed that the tax authorities tended to 'inflate' the amount of the penalties in the adjustment notices sent to taxpayers to retain some room for negotiation in the event of a settlement.

5 National Assembly, Report on Finance Bill 2017, No. 4125, Annex 41, by Dominique Lefevre.

VIII ANTI-AVOIDANCE

French law contains both general anti-avoidance rules, namely '*abus de droit*' (or abuse of the law) and 'act of mismanagement' theories, and specific anti-avoidance rules.

Special administrative procedural rules apply to '*abus de droit*'. Article L64 of the tax procedure code (LPF) provides that the tax authorities are entitled to reject as inapplicable to them acts that constitute fraud, and to restore the true character thereof where those acts either are shams that are fictitious ('fictitiousness' theory) or that comply with the letter of the law but are contrary to the purpose of its authors and inspired by no other reason than to elude or reduce the tax burden ('fraudulent evasion' theory). A special 80 per cent surcharge applies on the evaded tax where the taxpayer was the principal instigator or principal beneficiary of such a scheme. A surcharge of 40 per cent applies where the taxpayer was neither.

Where the tax authorities have notified a reassessment based upon abuse of law, the taxpayer may refer the matter to the Abuse of Law Committee and present its observations in a written statement. It is then summoned to a Committee session to present its oral observations and answer the questions of Committee members. Prior to the meeting, and in the absence of the taxpayer or its counsel, the Committee members hear a reporter, generally appointed from the French tax authorities. The Committee decides in favour of the applicant taxpayer in approximately one case in three.

IX DOUBLE TAXATION TREATIES

France has one of the largest networks of international tax treaties. Currently, it has concluded 126 treaties for the avoidance of double taxation.[6]

Most of these treaties conform to the OECD or UN models, and when interpreting them the courts pay close attention to the OECD Comments. France also signed the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting on 7 June 2017 with certain reservations on Articles 3, 4, 5, 10, 11. Eighty-eight tax treaties are covered.

Recent controversial decisions on the implementation of double taxation treaties have held that tax-exempt parties are not regarded as residents of the other contracting state and must be denied treaty benefits. This applies to both offshore activities[7] and pension funds,[8] including in situations where the foreign entity provided a certificate of tax residency from its country of origin. Arguably the question should have been referred to the mutual agreement procedure under double taxation treaties before being referred to the national tax courts. Similar issues arise where the French tax authorities deny a French taxpayer the tax credit for a foreign withholding they deem inappropriate, sometimes with reason. The French tax department reports that 212 procedures were opened in 2016, 238 were completed and 794 procedures were outstanding at year end.

France recently concluded 25 treaties in conformity with Article 26 of the OECD Model Convention, the purpose of which is limited to the exchange of information.

6 bofip.impots.gouv.fr, BOI-ANNX-000306.

7 Council of State, 20 May 2016, No. 389994 *Easy Vista*; and Administrative Court of Appeal of Versailles, 29 November 2016, No. 16VE01537.

8 Council of State, 9 November 2015, No. 371132 *Santander pensiones*; and Administrative Court of Appeal of Versailles, 29 November 2016, No. 14VE01266.

On the other hand, certain foreign states or territories have not concluded any agreement with France for the exchange of fiscal information. Under French domestic law, they are regarded as 'non-cooperative' and are the subject of specific tax provisions (e.g., an increase in the withholding tax on income paid to companies that are established in such states). The short list of these states and territories is updated annually.[9] Pursuant to Constitutional Council decisions, the presumption of tax avoidance attached to transactions with such territories may be rebutted.

X AREAS OF FOCUS

To defend their rights, taxpayers can of course rely on the law, as voted by Parliament, as well as regulatory measures taken by the government that are codified in the General Tax Code and the LPF. Moreover, the administration's own doctrine, consisting of its guidelines, instructions, ministerial replies to questions from members of Parliament or the administrative decisions on questions put to it by taxpayers (rulings), may be invoked by taxpayers in the same situation, and are binding both for the tax authorities and the tax courts.[10]

XI OUTLOOK AND CONCLUSIONS

French authorities regularly emphasise the need to combat fraud and tax avoidance, especially in cross-border contexts.

Proposals regularly submitted to Parliament aim at reinforcing the means available to the authorities and increase the obligations placed on taxpayers, as well as impose tougher penalties for breaches. More often than not, these specific measures need to be, and effectively are, checked by the fundamental rights protected by the Constitution and international instruments.

9 Currently, an order of 8 April 2016.

10 Article L80A of the LPF.

Appendix 1

ABOUT THE AUTHORS

PHILIPPE DEROUIN

Philippe Derouin

Philippe Derouin is a member of the Paris Bar with more than 40 years of experience. Before running his own firm, he had been a partner with major international law firms, namely Gide Loyrette Nouel, Linklaters LLP and Skadden Arps Slate Meagher & Flom LLP, for about 30 years. He was a member of the Paris Bar council and also chaired the French institute of tax advisors and the French branch of the International Fiscal Association.

PHILIPPE DEROUIN

140, rue du Faubourg Saint Honoré
75008 Paris
France
Tel: +33 1 42 25 88 91
Fax: +33 1 42 25 88 44
philippe.derouin@cabinet-derouin.com
www.philippe-derouin.com

ISBN 978-1-912228-16-4