



International  
Fiscal Association

***Bilateral Meeting IFA  
Italy and France***

**Hilton Molino Stucky Venice**

**6 – 7 June 2014**

# **Bilateral Meeting IFA**

## ***Italy and France***

### ***Recent developments***

**Venice, 6-7 June 2014**

Chair:

**Bruno Gibert**

Partner, CMS Bureau Francis Lefebvre

Chair of the Scientific Committee of the French Branch of IFA

Speakers:

**Daniel Gutmann**

Partner, CMS Bureau Francis Lefebvre

Professor at the Sorbonne Law School

**Carlo Romano**

Partner, PWC

Professor at SSEF



# Structure of the presentation



1. Tax fraud and tax evasion
2. General anti-avoidance rules
3. Exit taxation

## 1. Tax fraud and tax evasion

2. General anti-avoidance rules

3. Exit taxation

- France : **Tax Fraud Act**, 6 Dec. 2013
  - Tax fraud more heavily punished
  - New TP documentation obligations (see Session II on TP Trends)
  - Other disclosure obligations
  - New provision on business restructurings : held unconstitutional by the Constitutional Court
  - Procedural aspects : the powers of the tax police are enlarged. Special investigative techniques will be deployed in the case of organized or aggravated tax offences, including surveillance and phone tapping
  - Tax regularizations : voluntary declarations submitted by French taxpayers with untaxed accounts held abroad

- France
  - **Hybrid financing**
    - New rule (Budget Law for 2014)
    - Goal of the rule : deny double dip structures where interest is deductible in France without being taxed in the recipient's State, mostly because of different characterization (dividend),
    - Interest paid to a related entity is deductible to the extent that is subject to sufficient taxation at the level of the recipient,
    - Sufficient taxation means 25% of French CIT which would have been paid under ordinary French rules:
      - $25\% \times 33,1/3\% = 8,33\%$
    - Specific rules apply to transparent structures and to collective investment vehicles: no taxation at their level → not in the scope as such; however, partners in the scope if dual test is met : debtor is related to the fund + fund is related to partners,

## Italy: Law on tax crimes (D.Lgs. 74/2000)

- Tax fraud: filing of tax returns through the use of invoices, documents or other fraudulent means- "serious penalties" for which the application of the Arbitration Convention is denied;
- Doubts if TP documentation constitutes a shield to criminal penalties;
- Criminalization trends: as of 2001 more severe provisions, new tax crimes to ensure tax collection, thresholds for criminal relevance decreased;
- "Empowering law" (*Delega Fiscale*): review of the tax criminal penalty system (article 8 of the Law) according to the predetermination and proportionality criteria

## European Commission, *Combating tax fraud and evasion*:

*“Tax fraud is a form of deliberate evasion of tax which is generally punishable under criminal law. The term includes situations in which deliberately false statements are submitted or fake documents are produced.” (Commission contribution to the European Council of 22 May 2013).*

## Non-cooperative jurisdictions

### France

Definition of the concept of non-cooperative jurisdiction  
in the French tax code

Harsh consequences (WT)

Yearly update

➤ 21 August 2013 : Bermuda, BVI and Jersey

➤ Dec 2013 : Gvt announces that Bermuda and Jersey will be withdrawn  
with retroactive effect as of 1 January 2014

## Non-cooperative jurisdictions

### Italy

- It is foreseen in the law a list of cooperative countries (never enacted). Reference is made to the list of States with a preferred tax regime (Black List).
- Costs and expenses are not deductible if they arise from transactions with companies resident in a non-EU Member State with a preferred tax regime.
- These provisions do not apply if the Italian controlling entity proves that the localization abroad does not constitute an artificial scheme aimed at achieving undue tax advantages. To this end, the Italian resident has to apply for a ruling of the Italian tax authorities.
- Republic of San Marino excluded from black list.
- PEX not applicable in case of participation in Black List countries

# Structure of the presentation



1. Tax fraud and tax evasion

## **2. General anti-avoidance rules**

3. Exit taxation

- France
  - « Abuse of law » →
    - Fictitious acts, or
    - Fraudulent intent, i.e. exclusive tax objective + contradiction with the goals pursued by the drafters of the text at stake
  - Case law tends to extend the scope of abuse of law
    - Exclusive tax goal interpreted in an extensive way: « exclusive » tax objective exists even if a « negligible » non-tax goal is materialized
    - Abuse of law applies to tax treaties
      - Transfer of tax credits
      - Transfer of head office
        - » Ex. : transfer of head office of an Italian real estate company to Luxembourg in order to enjoy the benefit of the former French-Lux DTC
  - Reform of abuse of law held unconstitutional by the Constitutional Court

# General anti-avoidance rules



- Italy
  - no clear notion of “abuse of law”
    - Supreme Court: tax avoidance is embedded in the ability to pay and the progressivity
      - although not in conflict with any specific provision and in the absence of any sound economic reasons, produces undue tax advantages from the improper use of legal instruments (Supreme Court 30055-57/2008);
      - the right balance must be struck between aggressive tax planning and freedom of choice of legal form.
  - Tax Reform Law (*Delega Fiscale*): review of the legislation on tax avoidance and abuse of law (according to the criteria included in the “*Action Plan to strengthen the fight against tax fraud and tax evasion*”):
    - The purpose of obtaining undue tax advantages has to be the **main purpose**;
    - No abusive conduct if the operation is justified by **non-marginal business reasons**;
    - Criminal relevance? (SC decisions nos. 23730/06 and 144486/08-09).

- Italy

## Criminal Relevance of Tax Avoidance: The Recent Position of Italian Judges

- The Supreme Court has emphasized the fact that the tax avoidance concept must be applied with caution given that the right balance must be struck between aggressive tax planning and freedom of choice of legal form.
- The courts have not expressed a clear and comprehensive view.
- Supreme Court Decision No. 7739/2012 (Dolce & Gabbana Case) established a significant precedent, as it upheld the criminal relevance of tax avoidance behaviour.
- Purely elusive operations can have a criminal relevance only if constituting a specific violation of anti-avoidance rules (such as art. 37 bis of Presidential Decree 600/1973). Court of Milan dec. of 19/06/2013.

# Structure of the presentation



1. Tax fraud and tax evasion
2. General anti-avoidance rules

## **3. Exit taxation**

- **Corporations**

- France

- Transfer of head office to another EU country is neutral where assets remain taxable in France
- Same rule applies to transfer of assets to/from an EU PE
- However, taxation of assets transferred ; possibility to split taxation over 5 years
- Compatible with EU Law? Impact of ECJ, 23 Jan. 2014, 164/12, DMC Beteiligungsgesellschaft mbH
  - » § 62 : “in the light of the fact that the risk of non-recovery increases with the passing of time, the ability to spread payment of the tax owing before the capital gains are actually realised over a period of five years constitutes a satisfactory and proportionate measure for the attainment of the objective of preserving the balanced allocation of the power to impose taxes between Member States”.
  - » § 64 : “by giving the tax payer the choice between immediate recovery or recovery spread over a period of five years, the legislation at issue in the main action does not go beyond what is necessary to attain the objective of the preservation of the balanced allocation of the power to impose taxes between Member States”.

- **Corporations**

- **Italy**

- The provision concerning the transfer of seat was modified in 2012 following EU Commission's infringement procedure (n. 2010/4141). The transfer of the legal seat to another EU/EEA country is neutral for those assets remaining in a PE in Italy.
- The transferred assets are subject to the exit tax. A 2013 Decree (DM 2/8/2013) laid down the payment option in accordance with the EU case-law:
  - Immediate payment; or
  - Deferral of taxation of the deemed capital gain until the moment of actual realization as identified under Italian tax law, complying with specific reporting obligations (guarantees required); or
  - Payment of the exit tax due in 10 annual installments, including interest payments (guarantees required).

## Italy – main open issues

- Exit tax Decree not yet in force.
- Applicability to M&As
- Losses
- Monitoring values

# Bilateral Meeting IFA Italy and France

## Tax audits and BEPS Venice, June 6, 2014

### Speakers:

- Massimo Cremona,  
Partner Pirola Pennuto Zei e Associati

- Caroline Silberztein,  
Partner Baker McKenzie

### Chair:

- Bruno Gibert,  
Partner CMS Bureau Francis Lefebvre  
Chair Scientific Committee of the French Branch of IFA



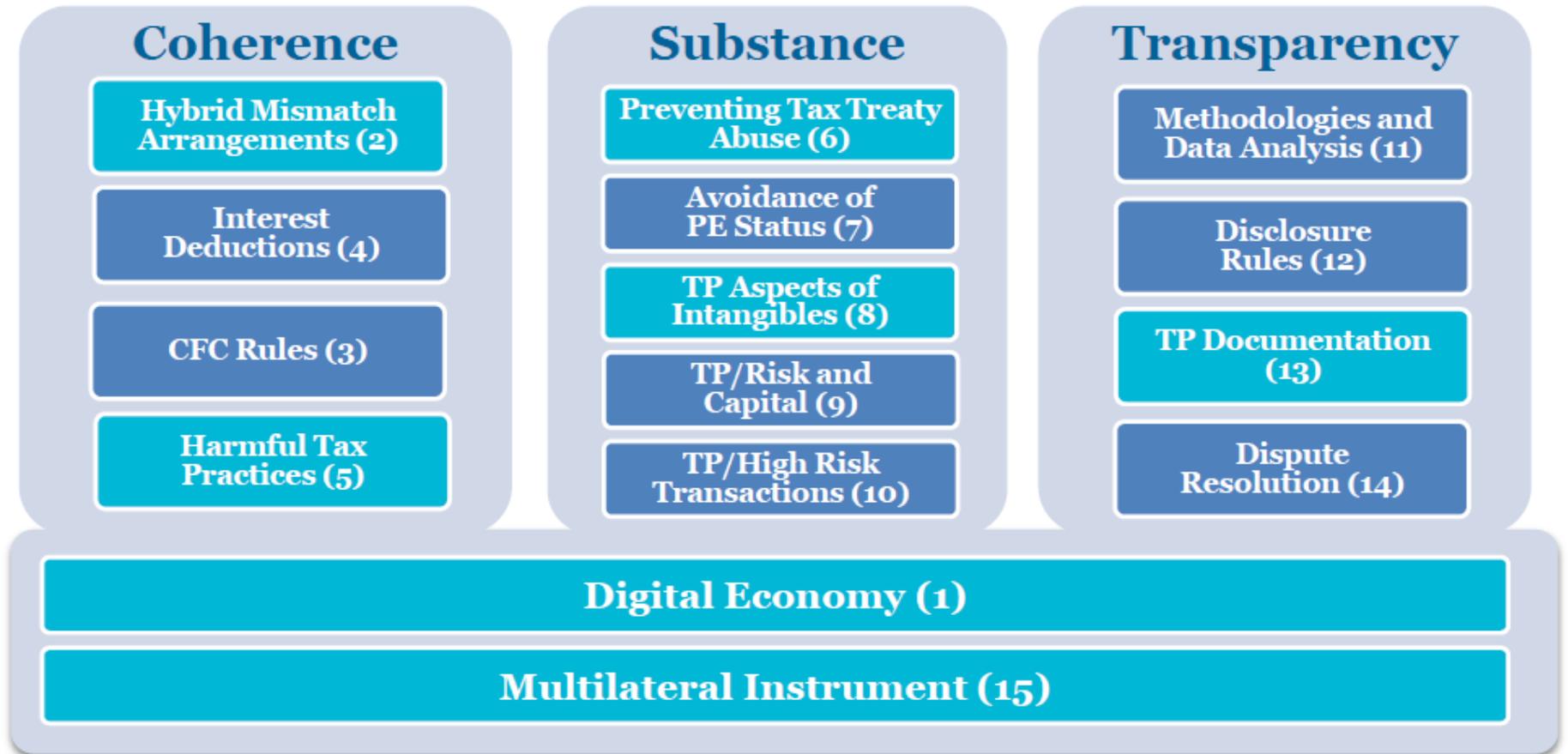
# Tax audits and Beps



## Introduction

# Tax audits and Beps

## The Beps project



Source: May 26, 2014 OECD Webcast

# Tax audits and Beps



## Agenda

**1. Horizontal issue:** address the challenge of digital economy - Action 1

### **2. Substance**

2.1 Assure that Transfer Pricing outcomes are in line with value creation - Actions 8 - 9 - 10

2.2 Preventing Treaty abuse - Action 6

### **3. Coherence**

3.1 Neutralize the effect of hybrid mismatch arrangements - Action 2

3.2 Strengthen CFC rules - Action 3

## **1. Horizontal action: address the challenge of digital economy - Action 1**

# Tax audits and Beps – Action 1 digital economy



- Discussion draft issued on march 24, 2014
- Public consultation on April 23, 2014
- Comments discussed at 3<sup>o</sup> meeting of task force april 24-25
- Task force meeting on may 26-28
- Final delivery on September 2014
- On track

# Tax audits and Beps – Action 1 digital economy



- Key issues:
  - Digital economy cannot be ring fenced
  - Complex description of the digital economy
  - Different business models
  - Different BEPS issues with some key features for consumption and income tax
  - Different options available for VAT and direct taxation

# Tax audits and Beps – Action 1 digital economy



- Examples of key issues
  - **No physical presence in the State where are sales**
  - **Value attribution to list of datas**
  - **Cloud services and tax characterization**
  - **Consumption tax**

# Tax audits and Beps – Action 1 digital economy



- Personal comments
  - a lot of work should be done
  - very complex issues to deal with
  - Many options available for CIT and Vat

# Tax audits and Beps – Action 1 digital economy



- Tax audits
  - **Significant number of digital companies tax audited**
  - **Mainly PE remarks**
  - **No unique approach in tax audit due to different business model**

## 2. Substance

2.1 Assure that Transfer Pricing outcomes are in line with value creation – Actions 8 - 9 - 10

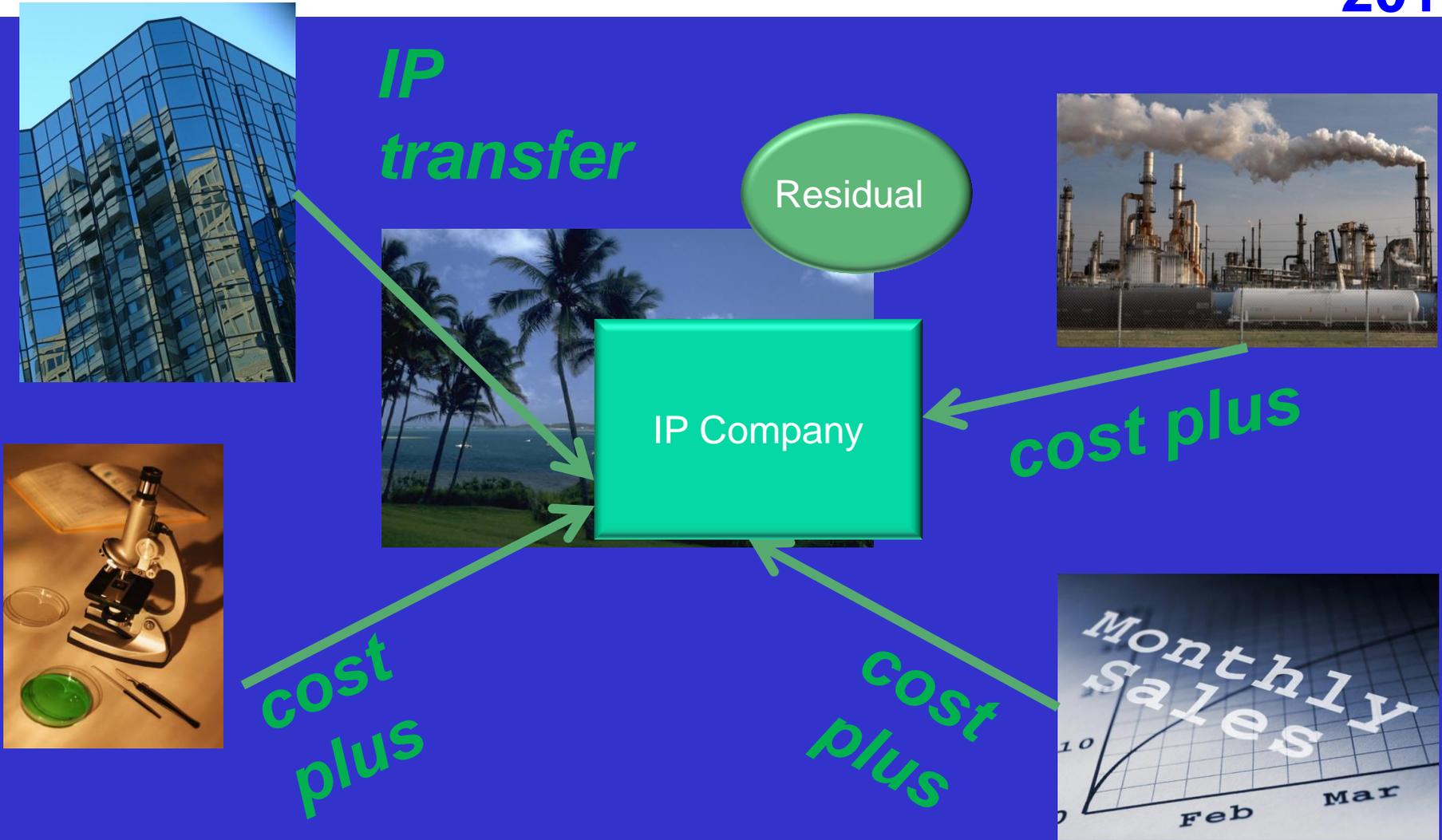
2.2 Preventing Treaty abuse - Action 6

# Tax audits and Beps



2.1 Assure that Transfer Pricing outcomes are in line with value creation – Actions 8 - 9 - 10

# Transfer pricing intangibles – Action 8



# Transfer pricing intangibles – Action 8

## – OECD BEPS Action Plan’s proposals

Calls for developing transfer pricing rules or special measures to prevent BEPS by moving intangibles among group members, through:

- 1. Adopting a broad and clearly delineated definition of intangibles**
- 2. Ensuring profits from transfer and use of intangibles are appropriately allocated in accordance with value creation**
- 3. Developing transfer pricing rules or special measures for transfers of hard-to-value intangibles**
- 4. Updating the guidance on cost contribution arrangements**

# Transfer pricing intangibles – Action 8

## – July 30, 2013: Revised discussion draft on TP aspects of Intangibles



### □ Intangibles definition

- “Something which is not a physical asset or a financial asset,
- which is capable of being owned or controlled for use in commercial activities, and
- whose use or transfer would be compensated had it occurred in a transaction between independent parties in comparable circumstances.”
- New definitions of “marketing intangibles”, “unique and valuable intangibles” ; marketing intangibles include consumer data.
- Synergies, locations specific advantages are not intangibles but comparability factors.

## □ Supplementary guidance on transfer pricing methods and comparability analysis

- CUTs unavailable in “many, if not most, cases”
- Important not to simply assume residual profit goes to owner of intangible
- “Expected future economic benefits” a factor to consider in selecting TP method
- One-sided methods generally unreliable for directly valuing intangibles
- More work to be done on “hard to value intangibles” (profit split ? commensurate with income standard ?)
- Somewhat warmer treatment of valuation techniques such as DCF

## □ Specific fact patterns

- Development and enhancement of marketing intangibles
- R&D and process improvement
- Use of company name
- Use of intangibles in connection with the sale of goods or provision of services

## □ Ownership of intangibles (“Section B”)

- Analytical framework for determining ownership starts from contracts / legal registrations ; but “simply a reference point”
- Right to retain return from exploiting the intangible depends on parties’ contributions to “anticipated value” through FAR
- **Section B not included in the 2014 approved revised chapter VI ; to be rediscussed in 2015 with capital, risk and recharacterisation issues.**

## □ Sharing the residual profit

- When is profit split more appropriate than one-sided methods ?
- What return for the IP Company who funds intangible (acquisition or development) and bears associated risk ?
  - » Financial return ? Share in residual profit ?
- If the Principal gets a financial return, how is the residual shared between :
  - » R&D;
  - » Manufacturing;
  - » Marketing & Sales;
  - » Management;
  - » Other functions?

# Transfer pricing intangibles – Action 8



- Transfer pricing rules or special measures to prevent BEPS through transferring risks among, or allocating excessive capital to, group members
- Ensure that inappropriate returns do not accrue to an entity solely because it has contractually assumed risks or provided capital
- **Circumstances in which transactions can be recharacterized**
- **Clarify the application of TP methods, especially profit splits, in context of global value chains**
- **Protect countries against common types of base eroding payments (e.g., management fees)**
- A discussion draft on risks, capital and recharacterization issues is expected to be released in December 2014.

# Assure that transfer pricing outcomes are in line with value creation – Actions 8 -10

- Country developments
- Tax audits current practice and future trends

## 2.2 Preventing Treaty abuse – Action 6

# Prevent treaty abuse – Action 6

- **Challenges cited in the OECD Action Plan on BEPS**
  1. **Interposition of third countries in bilateral structures, involving schemes such as:**
    - Low-tax branches of a foreign company
    - Conduit companies
    - Artificial shifting of income through transfer pricing arrangements
  2. **Need to modify domestic and international rules to more closely align allocation of income with the economic activity that generates the income**

# Prevent treaty abuse – Action 6

- **Action Plan's proposals**

- 1. Development of model treaty provisions and/or recommendations on design of domestic rules to prevent granting of treaty benefits in inappropriate circumstances**
- 2. Clarification that treaties are not intended to generate double non-taxation**
- 3. Identification of tax policy considerations countries should consider before entering into a treaty**

# Prevent treaty abuse – Action 6

## – Discussion draft issued March 14, 2014:

1. **Specific treaty anti-abuse rules targeted at circumventing the limitations provided by the treaty itself:**
  - **US-style Limitation of Benefits (LoB) article;**
  - **Main Purpose Test rule;**
  - **Other specific anti-abuse rules:**
    - i. **Proposed addition of minimum shareholding period;**
    - ii. **Proposed look-back period;**
    - iii. **Tie breaker rule for determining the treaty residence of entities;**
    - iv. **Anti-abuse rule for permanent establishments situated in third States.**
  
2. **Abuse targeted at circumventing domestic tax law by using treaties.**

# Prevent treaty abuse – Action 6

## Limitation of benefits

Would precisely restrict the list of persons entitled to treaty benefits :

- Qualified persons, e.g. listed companies (either listed in one contracting State, or whose primary place of management and control is in the Contracting State of which it is a resident),
- A resident of a Contracting State which is engaged in the active conduct of a trade or business in the Contracting State of which it is a resident (other than the business of making or managing investments for the resident's own account, unless these activities are banking, insurance or securities activities carried on by a bank, insurance company or registered securities dealer respectively), and the income derived from the other Contracting State is derived in connection with, or is incidental to, that trade or business.

# Prevent treaty abuse – Action 6

## Main purpose test

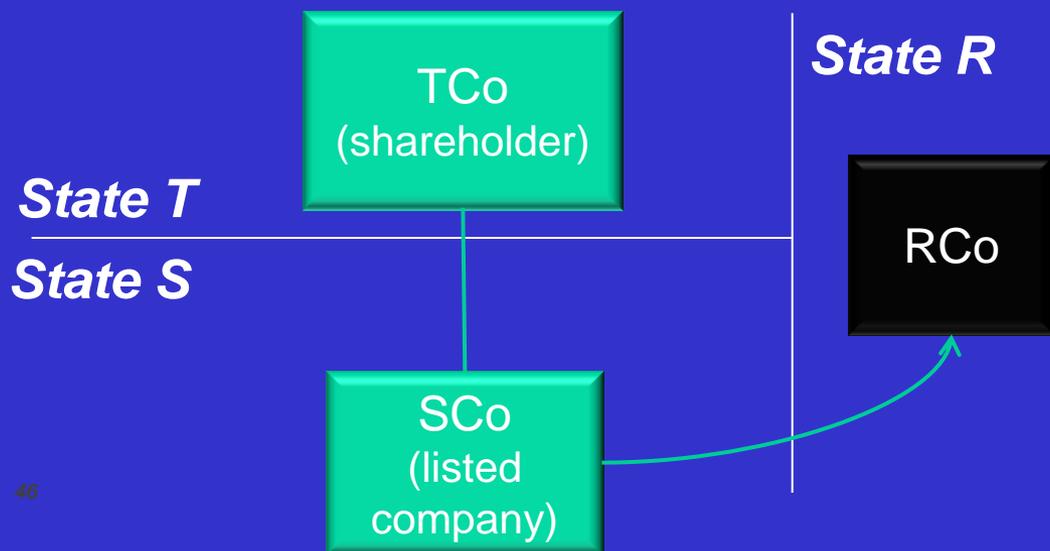
- Would deny treaty benefits in respect of an item of income if it is reasonable to conclude, having regard to all relevant facts and circumstances, that obtaining that benefit was one of the main purposes of any arrangement or transaction that resulted directly or indirectly in that benefit, unless it is established that granting that benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of this Convention.

# Prevent treaty abuse – Action 6

## Main purpose test

*Discussion draft example in which the main purpose test would be applied*

- *No tax convention between State T and State S: WHT on dividends of 25% under domestic law of State S;*
- *Tax convention between State S and State R: no WHT on dividends paid by a company resident of a Contracting State and beneficially owned by a company resident of the other State*



*Tco assigns to Rco the right to the payment of dividends that have been declared but have not yet been paid by SCo.*

# Prevent treaty abuse – Action 6

## Main purpose test

- Public consultation held 14/15 April 2014. According to the May 26, 2014 OECD webcast:
  1. Agreement that LOB alone will not address all situations of treaty abuse and treaty shopping (especially not conduit financing situations).
  2. Concerns about combined approach (LOB/Main Purpose Test)
  3. Design issues related to the LOB rule:
    - Treatment of Collective Investment Vehicles, pension funds and dual listed companies;
    - Derivative benefits;
    - Discretionary relief;
  4. Interaction between domestic anti abuse rules and treaty anti abuse rules.

# Prevent treaty abuse – Action 6

## Main purpose test

- Next steps:
  - Redraft of treaty abuse by WP1's Focus Group on Treaty Abuse is finalized and submitted to the approval of WP1 and the CFA.
- Country developments
- Tax audits current practice and future trends

## 3. Coherence

3.1 Neutralize the effect of hybrid mismatch arrangements – Action 2

3.2 Strengthen CFC rules – Action 3