



Anti-abuse rules: The French Experience

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Lukasz P. STANKIEWICZ

Associate Professor of Law – Maître de conférences

Vice Dean for European and Int'l Relations
Faculty of Law- FACULTÉ DE DROIT

Full Professor of Law – Professeur des universités
Université de Limoges (as of 1 Sept. 2018)





I. GAAR vs. SAAR

- Anti-abuse (avoidance) rule: what are we talking about?
- The GAAR: art. L. 64 of the *Livre des procédures fiscales (LPF)*
- SAAR: numerous examples
 - The CFC rule: art. 209B of the Code général des impôts (CGI)
 - Thin capitalization rule: art. 212 CGI, etc.
 - The MLI PPT rule as a type of SAAR



I. The GAAR: LPF, art. 64

*“In order to reconstitute their true character, the Administration can **disregard** (...), acts [i.e. transactions of taxpayer] constituting **abuse of law**, **either** when these acts are fictitious **or** when, searching to benefit from a textual application of texts or decisions against the objectives pursued by their authors, they [these acts] could not have been inspired by any other motive than that to avoid or attenuate (...) [taxes] that the taxpayer, given her situation or her real activities, would have been charged with if these acts were not (...) realized”.*

[own translation]

Enacted by Act n° 2008-1443 of 30 december 2008, art. 35



I. The GAAR: LPF, art. 64

« Afin d'en restituer le véritable caractère, l'administration est en droit d'écarter, comme ne lui étant pas opposables, les actes constitutifs d'un abus de droit, soit que ces actes ont un caractère fictif, soit que, recherchant le bénéfice d'une application littérale des textes ou de décisions à l'encontre des objectifs poursuivis par leurs auteurs, ils n'ont pu être inspirés par aucun autre motif que celui d'éluider ou d'atténuer les charges fiscales que l'intéressé, si ces actes n'avaient pas été passés ou réalisés, aurait normalement supportées eu égard à sa situation ou à ses activités réelles. »

<http://www.legifrance.gouv.fr>



I. The GAAR: LPF, art. 64

- **Important specificity of the French GAAR - double nature:**
- **1/ Administrative power to disregard transactions**
- **2/ A procedure (*Procédure de l'abus de droit fiscal*)**



I. The GAAR: LPF, art. 64 - The procedure:

- When disregarding transactions under the abuse of tax law provision, tax authorities must follow a special procedure which offers both the administration and the taxpayer an opportunity to refer the case to a special committee - **Committee of the Abuse of Tax Law** (*Comité de l'abus de droit fiscal*) - for its recommendation.
- The **recommendation of the committee** is not binding but, if favorable to the administration, will shift the burden of proof to the taxpayer in case of litigation before courts.



I. The GAAR: LPF, art. 64 - The procedure:

- Unless authorized by some specific anti-avoidance rule, **the administration cannot disregard or recharacterize taxpayer's transaction outside of the abuse of tax law procedure.** The opportunity to have the case heard before the Committee is recognized as a substantial guarantee of taxpayer's rights that tax authorities must honor.
- A specific penalty: initially, 200% of the amount of the assessment. The penalty was **scaled down by the Act of 8 July 1987 to 80%**, where it stands today. However, in 2008 a milder 40% penalty was introduced in case it is not proved that the taxpayer was the principal initiator of the scheme or that she was its principal beneficiary.
- **Quasi-criminal nature of the procedure**



I. The GAAR: LPF, art. 64 :

The two criteria of abuse of tax law:

- “Fictivity” → *simulation* (sham/hollow device)
- *Fraude à la loi*
 - *Fraude de ley* in Spain, *fraus legis* in the Netherlands, *Gesetzesumgehung* in Germany. The German term evokes literally the circumvention of law.



I. The GAAR: LPF, art. 64 :

- Simulation:

- Simulation is a civil law concept which consists in “creating an apparent juridical act which does not correspond to the reality of things”
 - (*Dictionary of the Civil Code*, LexisNexis, Paris, 2014, p. 525).
- The apparent act can be **fictitious** such as in case of a gift in which the donor subsequently retains control of sums apparently disposed of.
- Another common example is that of a gift **disguised** as a sale.
- In principle, tax considerations are irrelevant in characterizing simulations since, as a legal sham, the transaction can be disregarded as a matter of civil law, even if simulated transactions are frequently entered into for tax reasons.



I. The GAAR: LPF, art. 64 :

- **Fraude à loi:**
- “*Fraude à la loi*” applies to transactions that are regular under civil or commercial law.
- For instance, as a general rule, a company will not be fictitious if corporation law’s forms are respected (i.e. proper accounts are kept, the board meets, etc.) but it can be disregarded under “*fraude à la loi*”, if it had been artificially introduced in a flow of income with the sole objective to avoid taxation, as the case may be in the treaty shopping devices in international taxation.
- Raises an acute problem of **legal security**
- **For a long time: not recognized in France in tax matters**



I. The GAAR: LPF, art. 64 : history

- **The 1941 codification of the abuse of law concept and enactment of the specific procedure**
- But “Simulations” were disregarded on the tax plane well before the Act of 1941. There are cases which go back well into the XIX century in the field of registration duties.
- On its face, the 1941 text was limited to simulations: It stipulated the administration could recharacterize transactions which “dissimulated the real nature of a contract or convention”.



I. The GAAR: LPF, art. 64 : history

- **1981: judge-made extension of abuse of tax law to “*fraude à la loi*”**
- Conseil d’Etat, 10 June 1981, n°19079, referred to the “case of the vineyard of Bordelais”
- After that expansion, the statute not only targeted simulations in which a transaction failed to meet muster even in terms of its form, but also transactions that meet the letter of the law but violate its spirit. However, such a violation would only be found when a transaction was entered into for the sole motive of avoiding taxation.



I. The GAAR: LPF, art. 64 : history

- **The 2006 Janfin case: *fraude à la loi* without text**
- After 1981 it remained unclear whether “*fraude à la loi*” applied to taxes not specifically covered by the 1941 statute.
- Janfin: Art. L.64 of the LPF merely codifies a general principle of law and sets forth a special procedure.
- The 2008 Act, accomplished two ends. First, the revised statutory definition of abuse copies the 2006 *Janfin* judgment word for word. Second, the abuse of tax law procedure and penalties have been generalized to all taxes.



I. The GAAR: LPF, art. 64

- Fraude à la loi : the two branches
- Objective: violation of the spirit of the law

“searching to benefit from a textual application of texts or decisions against the objectives pursued by their authors”

- Subjective: taxpayer’s **exclusive** tax intention

“they [these acts] could not have been inspired **by any other motive** that than to avoid or attenuate (...) [taxes]”



I. The GAAR: LPF, art. 64

- Fraude à la loi : the subjective criterion

- The *Conseil Constitutionnel* (29 December 2013, n°2013-685 DC) struck down a legislative principal purpose test as conferring excessive discretionary power to the administration which, given the severe penalties attached to the abuse of law procedure, violated the constitutional objective of “intelligibility” of law and the principle of legality of criminal offenses and sanctions.

- Question : whether it is the principal purpose test that, in and of itself, is unconstitutional or it was considered so because it had been embedded in a special procedure triggering the application of penalties of a quasi-criminal nature.



I. The GAAR: LPF, art. 64

Fraude à la loi : the subjective criterion

- Exclusive tax motivation vs. economic motive
- “Wholly artificial arrangement” (ECJ 2006, Cadbury Schweppes)
- Economic substance
- *Substance* test for legal bodies while *motivation* test for *transactions* (even if the supporting structure has substance to it)
- Marginal non tax effect



I. The GAAR: LPF, art. 64

Fraude à la loi : the subjective criterion

- One of the most senior judges of Conseil d'Etat, specialized in tax law, OLIVIER FOUQUET, wrote that, in the eyes of the judge, there was an “abyss” between the “exclusive” and “principal” purpose tests.



I. The GAAR: LPF, art. 64

Fraude à la loi : what about the nature text abused

- Abuse of administrative interpretations?
- Abuse of tax treaties
- CE, 25 oct. 2017, Verdannet case:
 - L. 64 LPF applies to tax treaties even if they are no anti-abuse rules
 - Artificial arrangements are necessarily contrary to the intentions of the drafters of the treaty



II. MLI – Principal purpose test

MLI, Article 7

“Notwithstanding any provisions of a Covered Tax Agreement, a benefit under the Covered Tax Agreement shall not be granted in respect of an item of income or capital **if it is reasonable to conclude**, having regard to all relevant facts and circumstances, that obtaining that benefit was **one of the principal 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 the Covered Tax Agreement.”



II. MLI – Principal purpose test

A few questions:

- Articulation with the GAAR
 - Procedure?
 - Penalties?
 - Effect: recharacterization vs. denial of benefits
- Reading of the subjective criterion, different, similar ?
- Burden of proof, how can taxpayer defend himself ?
- Can a transaction with economic substance be deemed as necessarily dovetailing the object and purpose of the treaty (promote economic cooperation through eliminating double taxation)