Bloomberg Tax

Tax Management
International Journal™

Permanent Establishment: An Extensive Approach Adopted by the French Supreme Court

By Eric Meier, Ariane Calloud, and Hanna El-Rouah [*]
Baker & McKenzie AARPI
Paris, France

On December 11, 2020, the French Supreme Administrative Court (the ''Court''), sitting in tax ''plenary'' formation (the four chambers specialized in tax matters sit together when the Court rules on questions of principle, both complex and technical), issued a ruling in *Conversant/ValueClick*[1] The Court addressed whether an Irish company, ValueClick International, which operates in the digital sector and benefits from services rendered by ValueClick France, a local company in its group, has a permanent establishment in France for purposes of corporate income tax (CIT) and value-added tax (VAT).

While the debate on taxation of the digital economy continues at the national and international levels (compare the rise of unilateral digital services taxes with the OECD's efforts around Base Erosion and Profit Shifting (BEPS), Pillars 1 and 2, and implementation of multilateral instruments), the *Conversant/ValueClick* case relates to the application of traditional tax rules outside this debate.

The Court sets out principles that broadly interpret treaty provisions and take an innovative approach to European Union law regarding the characterization of fixed establishment for VAT purposes. While the Court's decision is less favorable than earlier decisions of French courts on PE matters, these cases highly depend on a case-by-case factual analysis.

[*]Eric Meier and Ariane Calloud are Partners in Baker McKenzie's Paris office. Hanna El Rouah is an Associate.

[1] Dec. 11, 2020, No. 420174, https://www.conseil-etat.fr/fr/arianeweb/CE/decision/2020-12-11/420174 (in French).

COURT OF APPEAL'S RULING REVERSED

The Paris Administrative Court of Appeal, following a detailed analysis of the circumstances of the case, ruled that ValueClick Int'l did not have a permanent establishment in France for both CIT and VAT purposes, considering that ValueClick France did not have sufficient resources to carry out the activity of the Irish company, nor the power to bind the former. The Court overturned the decision, in line with its Public Reporter's opinion, on the following main points.

Characterization of a Foreign Company's Dependent Agent in France

The Court ruled that ValueClick France shall be regarded as a dependent agent PE exercising powers enabling it to bind ValueClick Int'l in a commercial relationship relating to transactions constituting its own activity when it decides, in a usual manner, on transactions that the Irish company merely limits itself to endorsing and which, when so endorsed, bind the Irish company.

The fact that ValueClick France does not formally enter into contracts in the name of the Irish company proved to be irrelevant. The Court mentioned the Court of Appeal's finding that ValueClick Int'l sets the template contracts entered into with advertisers in order to give them the benefit of the services that it operates, as well as the general pricing conditions. However, the court notes that the choice of whether to enter into a contract with an advertiser and all the tasks necessary for its conclusion are the responsibility of ValueClick France's employees, with the Irish company merely validating the contract by means of a signature that is automatic in nature.

The Court noted that it considers this approach to be in line with OECD commentaries (in particular §32.1 and §33 of the commentaries on Article 5 of the Model Convention). It is important to emphasize, without taking a dynamic approach to the OECD commentaries, that the Court expressly refers to com-

ISSN 0090-4600

mentaries issued after the treaty between France and Ireland entered into force but prior to the facts.

This revises earlier French case law where commentaries issued after the conclusion of a tax treaty were not taken into account (for instance, *Andritz*[2]). Taking subsequent comments to a model document into account when interpreting specific international treaties may complicate the interpretation of international treaties.

Characterization of a French PE for VAT Purposes

With regard to VAT, the Court of Justice of the European Union (CJEU) typically considers that the most appropriate, and thus the primary, point of reference for determining the place of supply of services for tax purposes is the place where the taxable person has established his business. It is only if that place of business does not lead to a rational result or creates a conflict with another Member State that another establishment may come into consideration.[3]

More recently, in a case related to digital services, the CJEU stated that:

> [T]he place where the taxable person has established his business as primary point of reference appears to be a criterion that is objective, simple and practical and offers great legal certainty, being easier to verify than, for example, the existence of a fixed establishment (. . .). Furthermore, the place of business is mentioned in the first sentence of Article 44 of the VAT Directive, whereas the fixed establishment is mentioned only in the following sentence. That sentence, introduced by the adverb 'however', can only be understood as creating an exception to the general rule set out in the previous sentence.[4]

Despite this case law, the Court considers that as long as the services can be connected to a fixed establishment there is no need to investigate whether this reference is fiscally more rational than a reference to the provider's place of business.

Consequently, the Court's decision leads to a *de facto* approximation of CIT and VAT with respect to the qualification of permanent establishments, although the rules applicable to each are different. Interestingly the Court decided to start with CIT contrary to the order followed before lower jurisdictions.

For VAT purposes, the Court noted that the reality of the human resources required to carry out the company's marketing solutions is indeed located in France. In particular the human resources that enable ValueClick France to make the decision to enter into a contract with an advertiser that allows it to benefit from the services operated by ValueClick International. The fact that ValueClick France could not decide on its own to put the marketing services online was of little importance for the Court.

In addition, the Court did not adopt the principles set out by the CJEU in *Welmory*, regarding the technical means necessary for the provision of services. In that case related to services carried out in the field of online commerce, the CJEU ruled that a Cypriot company did not have a fixed establishment in Poland because the computer servers, software and IT services were located outside Poland.

Hence, the Court ruled that ValueClick France's employees shall be regarded as having the appropriate technical resources to provide ValueClick International's services autonomously, even though no technical infrastructure (including software and data center used for the execution of the IT linking functionalities) is located in France. Indeed, the Court determined that ValueClick France's employees defined the parameters of the advertising campaigns and managed the customer accounts in a manner that effectively opened up ValueClick France's access to functionalities without any necessary intervention from another company in the group, while noting that ValueClick Int'l was responsible for the development and maintenance of the software as well as the operation of the servers.

CASE REMANDED

The Court left some issues unaddressed. It did not rule on the question of the existence of a fixed place of business of ValueClick Int'l in France, which is another approach that makes it possible to characterize a permanent establishment for tax treaty purposes. This approach was adopted in this case both by the French Tax Authorities and by the Court's Public Reporter in his opinion.

The Court also did not address the question of profit attribution. The Public Reporter however emphasized that in a situation such as this the French Tax Authorities should be able to choose the basis of tax reassessments by placing itself either in the field of transfer pricing by increasing the remuneration of the French company or by characterizing a permanent establishment in France of a foreign entity.

While the amounts of the tax reassessments shall in principle be the same, the consequences of each of these two bases are not the same. First, the taxpayers subject to the reassessments are different. Transfer pricing reassessments for insufficient remuneration would have related to ValueClick France; whereas reassessments on the ground of the permanent establishment relate to ValueClick International. Moreover, unless the conditions of the ''right to make a mistake'' are met, reassessments made on the ground of the permanent establishment generally lead the French Tax Authorities to allege a concealed activity, leading to an extended statute of limitations and an automatic 80% penalty. Cases on which such level of penalty is

---

[2] French Supreme Administrative Court, Dec. 30, 2003, No. 233894.

[3] CJEU, *Berkholz,* July 4, 1985, No. 168/84.

[4] CJEU, *Welmory*, Oct. 16, 2014, No. C-605/12, https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:62012CJ0605&from=FR.

ISSN 0090-4600

applied since the entry into force of the fight against fraud on October 23, 2018 must be referred to the Public Prosecutor.

The Court has referred *Conversant/ValueClick* back to the Paris Administrative Court of Appeal, which will have to apply the above-mentioned principles in its decision to be rendered again on the merits of the case.

ISSN 0090-4600