Reflection for the implementation of an "anti-avoidance" tax in France

by

Boris Bouzol-Broitman¹ & Arnaud Iss²

¹ Political advisor in charge of economic issues at the European Parliament. Email: boris.bouzol@sciencespo.fr.
² Senior civil servant and magistrate. Email: arnaud.iss@gmail.com.

The Agenda 2030 Policy Briefs series mobilizes economists and practitioners to identify an economic and financial reform agenda to achieve the 2030 Agenda at the territorial, national and supranational levels. Contact: thomas.lagoardesegot@kedgebs.com.
I) Identified problem: the lack of fight against legal but abusive tax optimization

The term tax optimization can sometimes be confusing. There are in fact two types of tax optimization. One is illegal and consists of circumventing tax rules by going against the law. The cost to French public finances could reach 100 billion euros according to the Solidaires finances publiques union3. The other, legal, consists of playing with the tax rules in force, both in France and abroad, in order to pay as little tax as possible. This is by nature difficult to quantify, since the boundary between what is and is not optimization is subjective. This is particularly true for taxpayers who go abroad. How to define if a departure abroad was done in order to pay less tax or not? Sometimes it can be a mosaic of reasons, among which the fact of being able to pay less tax figures prominently.

It is therefore difficult today for the French tax authorities to recover the revenues that escape them as a result of this legal tax optimization abroad. However, this is made all the easier for French taxpayers as it can be done within the European Union itself, each country having its own tax rules, even though the movement of capital and people is free.

The negotiations underway at the OECD and G20 level, notably concerning the "BEPS" project, only concern corporate taxes and have been dragging on since 2012, due to the lack of international political consensus. We are therefore convinced that we should not wait for this type of international agreement before taking action. By creating a tool that can be implemented unilaterally by France, we can hope to act quickly to curb this phenomenon. Moreover, it would be in the interest of other States to imitate France and, little by little, we can reach an international consensus by example. It would then no longer be in the interest of any state to practice tax dumping. Tax harmonization from above would thus be a de facto process.

The objective is ambitious. However, this paper does not pretend to propose a turnkey solution to this scourge. It proposes a tool. But this tool will have to be the subject of a broad consultation, in particular with the tax authorities, in order to perfect it before it can be considered for implementation. The objective here is therefore to launch the reflection and the debate around what could be a simple and quick way to put an end to tax optimization abroad, which is certainly legal, but morally abusive as it reduces the tax paid by the wealthiest taxpayers.

II) Analysis and findings for France:

a) Our main national tools to fight against abusive tax optimization are "targeted" anti-abuse measures which, being too numerous and legally fragile, make the tax unreadable

As the law currently stands, we find that the French State is still insufficiently equipped to fight against legal but abusive tax optimization.

First, in broad terms, its main tool consists of specific tax modalities, namely "targeted" anti-abuse devices. And precisely, the current complexity of certain taxes (such as corporate income tax, income tax or VAT) can be explained by the successive layers of accumulated tax laws, each time intervening to fill legal uncertainties or to counter the inventiveness of tax lawyers, but very often after these loopholes have been exploited.

These particular tax mechanisms, which in each case have attempted to counter or limit abuses, are very often legally fragile and may thus contravene constitutional norms (equality before the tax, equality before public charges, etc.) or more often European Union law (in particular the "freedoms" of movement of capital and establishment).

Although useful and necessary, these particular anti-abuse measures nevertheless constitute a legal mosaic that makes taxes very difficult to read for taxpayers, especially since this mosaic is by nature evolving and legally fragile.

b) The existing "general" measures remain incomplete and do not aim to drastically limit tax optimization

The second main existing tool is the "general" anti-abuse provisions, which are mainly aimed at combating illegal tax evasion and avoidance and not at legal tax optimization. The most important one is the tax "abuse of right" (articles L. 64 and following of the book of tax procedures - LPF) which was set up as early as 1941, and then progressively strengthened, and which allows the administration to dismiss fictitious assets, seeking a literal application of the texts diverting their letter and spirit, if their sole purpose is to evade or reduce the tax normally due. Although this mechanism was recently reinforced (Finance Laws for 2019) by the creation of a "mini abuse of right" (article 64 A of the LPF) for abuses whose "main" (and not "exclusive" as the initial abuse of right of L. 64 LPF) purpose is to evade or reduce the tax due, these mechanisms alone remain insufficient and pose two main difficulties.

These measures are not intended to help in a generalized war against tax abuse, but are rather similar to surgical strikes that involve a significant workload and analysis for the administration, with the burden of proof resting on it. Above all, they do not target the majority of tax optimization that takes advantage of significant differences in taxation between two States, two distinct legal systems.

In addition, there is the limitation of another unfinished "general" mechanism, the "black lists" of tax havens (the list of uncooperative countries and territories for tax purposes of the European Union and France). These only concern a limited number of states (12 and 13 respectively in 2021) because inclusion on this list is not automatic, but results from a political decision - no European Union country in particular is included. Above all, this inclusion is the result of an anti-democratic process, since it is the "code of conduct" group, one of the most opaque groups in the European institutions, that is in charge of drawing up this list. This is so much so that the European Parliament has publicly indicated that it "questions the capacity of such an informal group to carry out this mission and the appropriateness of having entrusted it to it" in a resolution adopted by a large majority on 21 January 2021. Moreover, inclusion on this list does not necessarily imply the application of a drastic regime across the board (for example, for the European Union, defensive measures can be decided by the Council of Ministers; for France, this only has consequences for some taxes, such as corporate income tax).

---

4 MOTION FOR A RESOLUTION on the reform of the European Union's list of tax havens (europa.eu)
III) Proposed solution: an "anti-avoidance tax" in France

a) Brief description of this "anti-avoidance tax"

This proposal is based on the "targeted" anti-abuse measures for certain taxes that already exist in current law, in particular those detailed in articles 209 B and 283 A of the French General Tax Code, which we propose to generalize and extend to all taxes.

The aim is to limit tax optimization through a simplified and quasi-automated mechanism, without political intervention, in order to avoid the pitfalls of "black lists" of tax havens. This mechanism is based on a simple principle: "tax optimization abroad cannot exceed half the tax that could have been paid in France". As soon as a tax transaction involves a French individual or legal entity or takes place between France and another country, if the difference between the direct national taxes actually paid in the foreign country is excessively low compared to what would have been due in France (because the rate is very low or because the terms and conditions of the tax credit, for example, are disproportionately favorable), the taxpayer must pay the compensatory balance to the Treasury. The purpose of this system would be, in the short term, to limit this tax optimization within an acceptable margin, and then, in the long term and progressively, to put an end to all tax optimization outside France.

In concrete terms, the idea is to create a specific tax in French law (see proposed wording in Annex 1) with the aim of fighting tax optimization outside France in a transversal manner. This tax to control tax optimization would be equivalent to a general "safeguard clause" that would concern all national direct taxes due in France and their equivalents abroad.

The persons liable to this tax would be all individuals or legal entities domiciled in France, or of French nationality, as well as any individual or legal entity domiciled outside France carrying out commercial or financial transactions with it.

Finally, the legal and formal basis for this tax would be the difference in tax actually paid abroad compared to France for these taxes. However, in practice, this would consist of all legal, economic (in particular financial) or commercial transactions, which would constitute a taxable base in France under national direct taxes, and therefore could give rise to taxation there.

b) Benefits and expected effects

The expected benefits would be multiple. First, it would give the tax authorities a permanent and sustainable defensive mechanism to fight against tax evasion and optimization. This would allow them to reach tax arrangements that cannot be denounced as abuse of law, such as the departure of French taxpayers abroad in order to drastically reduce their income tax. This could concern, for example, cases that have been recently publicized:

- French personalities (Mulliez, Arnault, Depardieu) who have benefited from the many favorable Belgian tax regimes (inheritance tax more advantageous than in France, exemption of capital gains on shares)³;

³ Direct local taxes and indirect taxes would be excluded.
- the Portuguese "non-habitual resident" tax regime, which constitutes an optimization of income tax (flat rate of 20%). Its use has been denounced by the press, for example for the actress Isabelle Adjani in 2016.

In this way, French taxpayers would be discouraged from moving their operations to very favorable tax jurisdictions, which would mechanically increase French tax revenues. In addition, in the event of significant effective tax evasion, this new tax would in any case allow the recovery of these tax revenues.

If it works in France, it could encourage the main developed countries that do not engage in tax dumping to develop similar defensive instruments. If this solution gradually spreads, countries offering aggressive tax optimization opportunities would be discouraged from doing so, as this strategy would no longer "pay off".

**b) Main obstacles identified and overcome by this proposal :**

<table>
<thead>
<tr>
<th>Obstacles:</th>
<th>Our proposal:</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Readability and simplicity</strong></td>
<td><em>An &quot;anti-avoidance tax&quot;</em> complementing other French taxes, with a simple principle: &quot;tax optimization abroad cannot exceed half the tax that could have been paid in France&quot;.</td>
</tr>
<tr>
<td><strong>Political - diplomatic risk</strong></td>
<td><em>A depoliticized administrative management:</em> no &quot;name and shame&quot;, the administration only has to check if the tax optimization remains within the authorized limits, and if necessary to adjust. It is not the foreign states that are at fault, but their tax systems that are too favorable;</td>
</tr>
<tr>
<td><strong>Political - taxpayers' concern</strong></td>
<td><em>Possibility of a threshold:</em> in order to focus the system on the taxpayers who are the quickest to optimize their tax situation, a threshold of tax due (tens of thousands of euros for individuals, hundreds of thousands for companies, for example).</td>
</tr>
</tbody>
</table>

---

**Legal - Bilateral treaties**: any reform of a tax affected by the numerous bilateral tax treaties (aimed at avoiding double taxation) to which France is a party would imply that these treaties be renegotiated; this would imply an immense workload for the administration;

**Legal - with regard to European Union law**: risk of hindering the free movement of capital and the freedom of establishment, with invalidation of the system by the Court of Justice of the European Union.

**Legal - a fiscal big bang?** A new generalized anti-abuse mechanism could imply the modification of numerous articles of law (general tax code, book of tax procedures).

**This additional tax would be:**

- **outside the scope of bilateral treaties**: it is not a question of modifying the terms of all French taxes that can be subject to tax optimization, but of creating a new, complementary tax that concerns a scope not covered by international treaties;

- **in conformity with EU law**: the perimeter of taxpayers proposed in the first analysis does not constitute an obstacle to the freedoms of movement of capital and establishment, uniformly tightening the regime regardless of the nationality of the individual or legal entity considered. *(At the very least, if there is a risk of contradiction, it could be due to the absence of sufficiently justified derogations to these "freedoms" at the EU level).*

- **no change to the rest of the tax law**: no need to amend the rest of the existing tax law.

**c) Additional elements and implementation modalities:**

- **The proposed margin of tolerance would be at least 50%**. That is, when the tax actually paid in a foreign state is less than half of what should have been paid in France, then the balance between what was paid and what would have been paid in France must be paid to the French Treasury.

This margin of tolerance can also be differentiated according to the states involved. For example, developing countries may have inherently lower tax rates than rich countries. It could be envisaged that automatically, if a country has a GDP/capita that makes it a developed country, even if it is considered as developing by the UN (UNDP), then the margin of "tolerance" would no longer be 50% but 33 1/3% or 25% for example.

Precisely, this margin of tolerance should not be absolute, and the objective should be set that, in the long run, international taxation between equivalent countries should be harmonized. For example, for 10 years this margin of tolerance would be a maximum of 50%, then 33 1/3% or 25% for the following 10 years, before there is no more margin of tolerance after 30 years. At the end of this period, this would mean that any difference in taxation compared to the French rates would have to be paid back to the French Treasury by the taxpayer. If most countries set up such systems, then any country practising tax dumping would not only no longer be attractive - the taxpayer would have to pay the same amount of tax as in a "normal" tax country anyway - but it could even be seen as a defect, as it would lead to a certain administrative complexity (declaration in the country of residence and in the country of origin, etc.) in order to ultimately pay the same amount of tax.
- **Tax threshold**: To prevent this mechanism from falling on small taxpayers, a tax threshold could be set at a tax theoretically due in France greater than or equal to thresholds - here purely indicative - of 50,000 euros (individuals) or 100,000 euros (legal entities) per tax year, in order to target the top end of the taxpayer spectrum.

- The **burden of proof rests with the taxpayer (remote declarations)**: if the taxpayer carries out a transaction which could have given rise to taxation in France, but is taxed in another State, then he must calculate the tax which would be due in France and the tax due in that foreign State, and justify that the difference is less than or equal to the margin of tolerance in force. If taxpayers do not comply with their reporting and regularization obligations, they may be subject to tax investigations, with penalties for non-reporting.

**Conclusion and closing remarks:**

Aggressive tax optimization is a real scourge. In addition to burdening public revenues with the tax thus evaded, it pushes governments to reduce taxes more and more, in the name of international tax competition. In addition, it drastically reduces the willingness to pay taxes of the majority of the population paying taxes in France, who no longer see why they should pay taxes when those who have more means than they do manage to avoid them.

The objective of this paper is therefore to launch the reflection around a tool that could allow to drastically limit the tax optimization abroad, legal but morally abusive as it reduces the tax paid by the wealthiest taxpayers. Many legal obstacles will have to be removed, the main one being the potential conflict with European law. Moreover, only practice will make it possible to put in place the limits with regard to constitutional and European standards of the broad definition of the taxable base that we propose. However, in view of the problem raised, it seems legitimate to launch this legislative project.
APPENDIX 1:

Proposed wording:

Create an Article 1 AA in the General Tax Code:

"Preliminary Title: Combating tax evasion and abusive tax optimization

Article 1 AA

The anti-avoidance tax corresponds to the difference, for direct taxes whose rate is fixed by law at the national level, between the tax actually paid in a privileged tax regime for the transactions mentioned in the second paragraph and at least half of the tax that would have been paid for them under the conditions of ordinary law in France.

Any legal or economic transaction, in particular financial or commercial, which could give rise to taxation of any kind in France, carried out by any individual or legal entity domiciled in France, or of French nationality, as well as any individual or legal entity domiciled outside of France carrying out commercial or financial transactions with it, is only allowed if the actual or potential debtor provides proof that this transaction has been or is subject to taxation outside of France, and if the amount of tax actually paid outside of France in relation to this transaction is not less than the amount of tax paid in a privileged tax regime. If this proof is not provided, these transactions are considered as taxable under the anti-avoidance tax.

For the application of the first paragraph, such persons shall be deemed to be subject to a privileged tax regime in the State or territory concerned if they are not taxable there or if the amount of tax actually paid to which they are subject for the transaction or transactions in question is less than at least 50% of the amount of tax or taxes for which they would have been liable under the conditions of ordinary law in France. The threshold mentioned in the previous paragraph is raised to 66 ⅔% or 75% for States whose level of development implies a tax convergence with the French level of taxation, by a list set at least annually by decree of the Council of State.

For the application of the second paragraph, these persons must transmit each year to the tax authorities a summary of these operations, of their taxable or non-taxable nature abroad, as well as the amount of tax paid outside France, as well as the amount of tax to which they would have been subject if these operations had been taxed in France. Failure to declare before December 31 of the year following the completion of these transactions gives rise to a surcharge under the conditions provided for in Article 1728 of the General Tax Code.

By way of derogation from the second paragraph, individuals and legal entities shall not be subject to the anti-avoidance tax if the annual amount of tax or taxes that could have been paid in France, in respect of the above-mentioned transactions, is less than an amount set by order of the Minister of the Budget and which may not be less than 50,000 euros for individuals and 100,000 euros for legal entities."

8