Council of the
European Union

Brussels, 27 May 2019
(OR. en)

9652/19
ADD 2

FISC 274
ECOFIN 515

REPORT

From:	General Secretariat of the Council
To:	Permanent Representatives Committee/Council
Subject:	Code of Conduct Group (Business Taxation) – Report to the Council = Endorsement

France's new IP regime (FR054)

I/ AGREED DESCRIPTION

The following description was agreed by the Code of Conduct Group on 30 January 2019:

Country			France
1. Please provide below the basic information about your regime	a. Name of the regime		Reduced corporation tax rate on IP income
	b. Year of introduction/relevant legislation	Year	2019
		Please attach to this template (or provide a link to) the legislation which introduces your new IP regime (if in a language other than English or French, please provide a translation).)	Article 37 of the Finance Bill for 2019 abolishes the existing regime and introduces a new regime (cf. attached documents). Final legislation has been adopted by the French Parliament and confirmed by the French *Conseil constitutionnel*, which will take place before the end of 2018.

Country			France
	c. Benefits under your regime (e.g. a reduced rate or a deduction, an exception, or some other reduction in the taxable base)		The regime provides a lower corporation tax rate on relevant profits derived from qualifying IP assets.
	d. Effective tax rate under your regime		10%
	e. Statutory rate in your jurisdiction that would apply in the absence of the regime		33,1/3% (25% in 2022)
	f. Stated purpose of your regime		To create technical innovation by supporting the development of intellectual property (IP) rights and the location of R&D activities in France.
2. Please describe the scope of qualifying taxpayers under your regime.			All companies subject to corporate income tax or personal income tax in France (ie resident corporations and permanent establishments of non-resident corporations) which carry out R&D activities in France and derive IP income from such activities.
3. What types of IP assets can qualify for benefits under your regime?			- Patents and supplementary protection certificates, utility certificates, irrespective of whether they are granted by the French *Institut national de la propriété intellectuelle* (INPI) or under any equivalent foreign legislation. - Plant variety certificates - Softwares protected by copyright - Processes directly related to the patent - Patentable inventions (only for SMEs), cf. question 4
4. Third category of IP assets	a. Are you planning on allowing the third category of IP assets described in paragraph 37 of the Action 5 Report to qualify for benefits?	Yes/no	Yes.
		(i) Please describe how you will limit the taxpayers benefiting from the third category.	The only taxpayers that may qualify for such measure are those that have no more than EUR 50 million in global group-wide yearly turnover and that do not earn more than EUR 7.5 million per year in gross revenues from all IP assets, using a five-year average for both calculations.
		(ii) Please describe what IP assets will	The measure will apply to patentable inventions, ie inventions which have a level of patentability equivalent to that of

Country			France
		qualify under this category, and the reason why they will fit with the specific requirements in paragraph 37 of the Action 5 Report.	a patent or a utility certificate, the only difference being the absence of publication. It will thus concern non-obvious, useful and new inventions which will be certified by the INPI. Non-patented patentable inventions enjoy legal protection if they constitute a business secret. As such, anyone who breaches the secrecy of a patentable invention could be liable to civil liability (Article L. 152-1 of the French Commercial Code). Moreover, the triggering of a criminal action remains possible provided that it proves the existence of a criminal offense under common law (theft of secrecy, concealment, breach of trust, etc.). These inventions are substantially similar to the IP assets in the first two categories, and will be certified as such in a transparent certification process by a competent government agency that is independent from the tax administration (cf. iii)). The measure is thus in line with the requirements of the Action 5 Report.
		(iii) Please describe the transparent certification process (undertaken by a competent government agency that is independent from the tax administration) under your regime.	In order to certify their patentability, a certification process of patentability by the INPI, which constitutes a competent governmental body independent from the tax administration, will be implemented. Specifically, this certification could be issued in the course or in a process similar to that of a patent application procedure or a utility certificate application procedure interrupted before publication. The invention would then be considered non-obvious, useful and new for the claims validated by the INPI. As such, this new certification procedure would be as strong as the patent or utility certificate process, except the demand would not be made public.
		(iv) Please describe the procedures you have implemented to ensure annual reporting to the	In addition to the “standard” tracking and tracing system described under question 7, the taxpayer shall provide the tax administration with the following information on a yearly basis : - the list of non-patented patentable inventions benefiting from the regime,

Country			France
		FHTP and spontaneous exchange of information.	- the net income deriving from these assets. France will thus be able to provide the relevant information required to meet the obligation to report on its usage in line with the requirements outlined in the Action 5 Report (ie number of taxpayers benefiting from this category, aggregate amount of IP income arising from this category of IP assets that qualifies for the IP regime). France will also exchange information spontaneously about taxpayers benefiting from this category of IP assets.
5. What income will qualify for benefits? Please describe how you are ensuring that the amount of income is not equal to the gross income from IP assets.			There are two categories of qualifying income : - net proceeds from the alienation of qualifying IP assets between non-related parties and on the condition that the IP assets were not acquired within two years before their alienation, - net income consisting in any licence fee received under a licence agreement pertaining to a qualifying IP asset (or any appropriate grouping of qualifying IP assets). The net income for each qualifying IP asset (or any appropriate grouping of qualifying IP assets) is calculated by deducting from the gross income derived from such asset (or appropriate grouping) : - the total expenditures of the year incurred in relation to the IP asset (or appropriate grouping), which correspond tp the overall expenditure incurred to develop or acquire the IP asset as

Country			France
			defined for computing the nexus ratio's denominator, - the past total expenditures in relation to the IP asset (or appropriate grouping) recognized during the whole period for which election was made for the regime, - and any net losses in relation to the IP asset (or appropriate grouping) incurred in previous years during the whole period for which election was made for the regime (cf. question 8).
6. Embedded IP income	a. Does your regime allow embedded IP income to qualify for benefits?	Yes/No	No
	b. If yes, please describe how you are ensuring that non-IP income (e.g. marketing and manufacturing returns) does not also qualify for benefits.		-
7. Tracking and tracing	a. Have you designed tracking and tracing requirements to ensure that income that is not from qualifying IP assets or that is not qualifying IP income does not qualify for benefits?	Yes/No	Yes
	b. If yes, please describe your regime's tracking and tracing requirements.		The taxpayer shall provide on a yearly basis the calculations of the ratio and the net income for each qualifying asset (or appropriate grouping of qualifying assets) with respect to each tax year. The taxpayer shall also keep record of the following data for each qualifying asset (or type of product/service, or group

Country		France
		of product/service) : - a general description of the organization of the R&D activities of the company which sells one or more qualifying assets or derives royalties from one or more qualifying assets ; - specific information concerning the determination of the net income including: (A) a detailed list and description of each of the qualifying assets (or appropriate grouping of qualifying assets) ; (B) presentation of the ratio and corresponding tracking and tracing documentation for each qualifying assets (or appropriate grouping of qualifying assets); (C) presentation of the cost allocation method among the different qualifying assets (or appropriate grouping of qualifying assets).
		There is no initial restriction on the offset of those losses against standard rate profits, but losses associated with any qualifying IP asset (or appropriate grouping of qualifying IP assets) and incurred during the whole period for which election for the regime was made will be recaptured. This recapture mechanism consists in deducting previous losses associated with an IP asset (or appropriate grouping) from subsequent net income pertaining to the said IP asset (or appropriate grouping). Therefore, once election is made for the regime with respect to a qualifying IP asset (or

Country			France
			appropriate grouping), only IP profits exceeding previous losses in relation to the said asset (or appropriate grouping) will benefit from the reduced tax rate. The regime also includes an additional safeguard to ensure that a taxpayer may not elect out and then opt into the regime again to avoid recapture of previous losses. Indeed, if after having elected for the regime with respect to a qualifying IP asset (or appropriate grouping of qualifying IP assets) the taxpayer then opts out of the regime, he will not be allowed to re-enter the regime. This ensures that any previous loss remains to be recaptured when the regime applies.
9. If you are not a Member State of the European Union, have you designed your regime to be consistent with footnotes 16 and 19 on page 42 of the Action 5 Report?			Not applicable
10. Related-party outsourcing	a. Does your regime limit benefits based on outsourcing to related parties?	Yes/No	Yes
	b. If yes, please explain how your regime limits benefits based on outsourcing to related parties.		The eligible income (ie the income to be subject to the reduced tax rate available under the regime) is obtained after multiplying the net income by the nexus ratio. The nexus ratio includes costs associated with related party outsourcing expenditures in the denominator (and not in the numerator). In doing so, related party outsourcing expenditures will reduce the amount of benefit available when the nexus ratio is

Country			France
			applied to the net income. In addition, related party outsourcing expenditures are also deducted from the gross income in calculating the net income before application of the nexus ratio (see answer to question 5: net income is calculated by deducting from the gross income the expenditures of the year corresponding to the nexus ratio's denominator). This is in line with the requirements outlined in the Action 5 Report.
11. Acquisitions of an IP asset	a. Does your regime limit benefits based on acquisitions?	Yes/No	Yes
	b. If yes, please explain how your regime limits benefits based on acquisitions. Following this question, please proceed to Question 13.		The eligible income (ie the income to be subject to the reduced tax rate available under the regime) is obtained after multiplying the net income by the nexus ratio. The nexus ratio includes acquisitions costs in the denominator (and not in the numerator). In doing so, acquisition costs will reduce the amount of benefit available when the nexus ratio is applied to the net income. In addition, acquisitions costs are also deducted from the gross income in calculating the net income before application of the nexus ratio (see answer to question 5). This is in line with the requirements outlined in the Action 5 Report.

Country			France
12. Related-party outsourcing and acquisition of an IP asset in line with footnotes 16 and 19 on page 42 of the Action 5 report	a. Does your regime limit benefits based on the location of the R&D activities in the case of related-party outsourcing and acquisitions?	Yes/No	No
	b. If yes, please explain how your regime limits benefits based on the location of R&D activities.		--
13. Rebuttable presumption	a. Does your regime treat the nexus ratio as a rebuttable presumption?	Yes/No	Yes
	b. If yes, please answer to the following questions (i) through (iii)	(i) Please describe how departures from the application of the nexus ratio will be limited to the exceptional circumstances described in paragraph 48 of the Action 5 Report.	The taxpayer may, due to exceptional circumstances and after prior authorization granted by the tax administration, replace the nexus ratio with a replacement ratio representing the proportion of the value of the qualifying asset that would actually be attributable to the R&D activities that it carries out directly or indirectly by non-related companies. The proportion of the value mentioned in the first paragraph corresponds to the proportion recognized to them by non-related persons, who, under similar conditions, undertake R&D activities. The authorization mentioned in the first paragraph is granted when: (A) the nexus ratio is greater than 32.5%

Country			France
			(ie 25% with the 30% uplift, equivalent to 25% without the uplift) ; (B) the replacement ratio is significantly greater than the nexus ratio because of exceptional circumstances beyond the control of the taxpayer.
		(ii) Please provide examples of situations where your jurisdiction expects taxpayers to rebut the presumption.	The law does not provide any examples of the situations where taxpayers are expected to rebut the presumption. In line with the Action 5 Report, the regime provides for the conditions to be met in order to access the rebuttable presumption, but cases where an exceptional circumstance arises will be reviewed on a case by case basis. However, the write down of an acquisition may be one instance in which the use of the rebuttable presumption could be authorised as stated in the Action 5 Report. It is also important to note that in order to rebut the presumption, the taxpayer will have to establish that, where a situation is deemed “exceptional”, there must be a causal link between those exceptional circumstances and the replacement ratio being significantly higher that the nexus ratio.
		(iii) Please describe the procedures you have implemented to ensure annual reporting to the FHTP and spontaneous exchange of	The prior authorization to rebut the presumption is valid for a five-year period, provided that the above-mentioned conditions A and B (see Question 13 (i)) continue to be met by the end of each tax year. Those prior authorizations will be notified

Country			France
		information.	to the FHTP and exchanged spontaneously. In addition to the “standard” tracking and tracing reporting system described under question 7, the taxpayer shall provide on a yearly basis the following information to the tax administration : - the list of assets benefiting from the regime, - the net income deriving from these assets. France will thus be able to report, as required under the Action 5 Report, the overall number of companies benefiting from the regime, the number of cases in which the rebuttable presumption is used, the number of such cases in which France spontaneously exchanged information, the aggregated value of income receiving benefits under the IP regime and a list of the exceptional circumstances that permitted taxpayers to rebut the nexus ratio in each case.

REGIME SELF-REVIEW TEMPLATE

Jurisdiction: France	
Regime: Reduced corporation tax rate on IP income	
Description of regime:	
Part A: Preliminary factors	
A1: The regime has been previously reviewed and there have been no subsequent changes to the regime.	No
Comments: The existing regime was previously reviewed in 2016 but is abolished as of 1st January 2019.	
A2: The regime has been abolished. *(Where a regime has been abolished and replaced by a new regime, the new regime should be considered on a separate Template.)*	No
Comments: Under the Finance Act for 2019, the existing regime is abolished as of 1st January 2019. A new regime will enter into force as for 1st January 2019. It is described in separate templates (1st and 2nd questionnaires).	
A3: The regime falls outside the scope of the work of the Forum on Harmful Tax Practices. *(The scope of this work focuses on geographically mobile activities, such as financial and service activities, including the provision of intangibles. It excludes regimes designed to attract investment in plant, building and equipment.)*	No
Where a regime falls outside the scope of the work of the Forum, please provide a full and detailed explanation as to why this is the case:	
If the response to any of A1-A3 is 'Yes', there is no requirement to complete Parts B-D	
Part B: Key factors in identifying harmful preferential tax regimes	
B1: No or low effective tax rates *(this factor is the gateway criterion to further assessment)* [See 1998 Report, paragraph 61]	Yes
Comments: The existing regime as well as the new regime provide for a lower corporation tax rate on relevant profits (royalties and proceeds from the alienation of IP assets). Under the existing regime the tax rate is 15%, under the new one the tax rate is 10%, whereas the statutory tax rate is	

33,1/3 %.	
B2: Ring-fencing of regime from the domestic economy [See 1998 Report, paragraph 62; and Consolidated Application Note, chapter III]	**No**
Comments:	
B3: Lack of transparency of the regime *(for example, the details of the regime or its application are not apparent, or there is inadequate regulatory supervision or financial disclosure)* [See 1998 Report, paragraph 63; and 2015 Action 5 Report, chapter 5]	**No**
Comments: **All details of the new regime are laid down in the law, which is published in the official gazette and publicly available on the Internet (see: www.legifrance.gouv.fr).**	
B4: Lack of effective exchange of information with respect to the regime [See 1998 Report, paragraphs 64-67]	**No**
Comments:	
B5: The regime encourages purely tax-driven operations or arrangements that involve no substantial activities [See 1998 Report, paragraph 79; 2015 Action 5 Report, chapter 4; and 2017 Progress Report, annex D]	**No**
Comments: **The new regime relies on the nexus approach which requires substantial activities.**	
Part C: Other factors in identifying harmful preferential tax regimes	
C1: An artificial definition of the tax base [See 1998 Report, paragraphs 69-70]	**No**
Comments:	
C2: Failure to adhere to international transfer pricing principles [See 1998 Report, paragraphs 71-72]	**No**
Comments:	
C3: Foreign source income is exempt from residence country taxation [See 1998 Report, paragraph 73]	**No**
Comments:	
C4: Negotiable tax rate or tax base [See 1998 Report, paragraph 74]	**No**

Comments:	
C5: Existence of secrecy provisions [See 1998 Report, paragraph 75]	**No**
Comments:	
C6: Access to a wide network of tax treaties [See 1998 Report, paragraphs 76-77]	**Yes**
Comments: **France has a wide network of instruments (DTCs and TIEAs) in force and is a Party of the OECD Multilateral Convention as amended by the 2010 Protocol. The total number of exchange of information partners is 148 in 2018.**	
C7: The regime is promoted as a tax minimisation vehicle [See 1998 Report, paragraph 78]	**No**
Comments:	
Part D: Conclusion of self-review	
D1: In light of the above and other factors, does your jurisdiction believe the tax regime may be potentially harmful?	**No**
Comments: (Include any assessment of the likely impact of the regime on other countries)	
D2: What measures are proposed to remove any features considered harmful?	
Comments:	
D3: Further observations or comments	
Comments:	

II / FINAL ASSESSMENT

The following assessment was agreed by the Code of Conduct Group on 30 January 2019:

	1a	1b	2a	2b	3	4	5	OA
FR – Reduced Corporation Tax Rate on IP Income (FR054)	X	?	X	?	X	X	X	X

In accordance with the 24 November 2016 report of the Code of Conduct Group to the Council, the following assessment has been prepared with regard to paragraphs 1 to 5 of the Code, based on the OECD description (hereafter referred to as "agreed description"[1]) provided by the French authorities in December 2018. The measure was assessed against all Code criteria and on the basis of the modified nexus approach.

Explanation

Significantly lower level of taxation:

"Within the scope specified in paragraph A, tax measures which provide for a significantly lower effective level of taxation, including zero taxation, than those levels which generally apply in the Member State in question are to be regarded as potentially harmful and therefore covered by this code"

The Reduced Corporation Tax Rate on IP Income ("IP regime") entered into force as of 1 January 2019. It provides for a lower rate for income and gains derived from certain IP rights.

The agreed description mentions that a lower corporation tax rate of **10%** on relevant profits (royalties and proceeds from the alienation of IP assets) is applied compared to the current French company tax rate of **33.33**% [25% as of 2022] .

This rate is significantly lower than the rate generally applying. **It is therefore potentially harmful within the meaning of paragraph A of the Code.**

Criterion 1:

"whether advantages are accorded only to non-residents or in respect of transactions carried

[1] For this particular exercise, the Member State's reply to the OECD questionnaire for FHTP.

out with non-residents”
Criterion 1 contains two elements. The first element is whether the measure is exclusively available to non-residents or transactions with non-residents (criterion 1a). The second element is whether it is only or mainly used by non-residents or for transactions with non-residents (criterion 1b). 1a) Criterion 1a concerns the *de jure* application of the measure. Both French resident companies and French permanent establishments (PEs) of non-resident companies subject to French corporate income tax which carry out R&D activities in France and derive IP income from such activities can benefit from the IP regime. There seem to be no provisions restricting the benefits to transactions with non-residents. 1b) Criterion 1b is used to complement the assessment under criterion 1a which only looks at the literal interpretation of the measure. It takes account of the *de facto* effect of the measure. Where the majority of taxpayers (or counterparties to transactions) benefitting from the measure are in fact non-residents the measure will fall foul of criterion 1b. In light of the recent introduction of the IP regime, it is unlikely that statistical or impact data is either available at this stage, or representative enough to reflect the comprehensive effects of the newly IP regime. Moreover, the agreed description in the format used lacks such data. This is a horizontal issue for almost all assessments. To the extent that our draft assessment is based on currently available information [or lack of] on statistics, we suggest that the group reserves the possibility of a potentially different outcome of a future assessment based on more complete information.

Criterion 2: “whether advantages are ring-fenced from the domestic market, so they do not affect the national tax base”
As regards criterion 2 the division between criteria 2a and 2b is done in the same way as in the case of criterion 1 (i.e. *de jure* interpretation and *de facto* analysis). In general, a measure is caught by criterion 2 if the advantages are ring-fenced from the domestic market so that they do not affect the national tax base. In most cases, the evaluation against criterion 2 follows closely that of criterion 1. 2a) What has been written under criterion 1a applies analogously to criterion 2a. There are no rules preventing domestic taxpayers from benefiting from the IP regime or to exclude domestic transactions. 2b) On the basis of the explanations provided above and the marking under criterion 1b, the evaluation of criterion 2b follows the same reasoning. In light of the recent introduction of the IP regime, it is unlikely that statistical or impact data is either available at this stage, or representative enough to reflect the comprehensive

effects of the newly IP regime. Moreover, the agreed description in the format used lacks such data.

This is a horizontal issue for almost all assessments. To the extent that our draft assessment is based on currently available information [or lack of] on statistics, we suggest that the group reserves the possibility of a potentially different outcome of a future assessment based on more complete information.

Criterion 3: “whether advantages are granted even without any real economic activity and substantial economic presence within the Member State offering such tax advantages”
In November 2014 the Group agreed, in co-ordination with developments at the OECD, on the modified nexus approach as the appropriate method to ensure that patent boxes require sufficient substance. Therefore, under this agreed approach, criterion 3 for the Code is to be interpreted in line with the modified nexus approach. The key elements of the modified nexus approach are: Scope (qualifying IP assets), Nexus ratio, Tracking and tracing, Rebuttable presumption and Treatment of losses. **<u>1. Scope</u>**: *<u>Qualifying IP assets</u>: Income benefiting from an IP regime has to come from a qualifying asset, comprised in one of the three categories 1) patents and functionally equivalent assets including utility models, protection granted to plants and genetic material, orphan drug designations and extensions of patent protection; 2) copyrighted software, and 3) assets that share the features of patents and are substantially similar to the two previous categories and are certified as such by a competent government agency in the State*[2]. The French IP regime comprises: 1° patents, utility certificates and supplementary protection certificates, irrespective if they are granted by the French *Institut national de la propriété intellectuelle* (INPI) or under any equivalent foreign legislation; 2° Plant variety certificates; 3° Software protected by copyright; 4° Industrial processes directly related to the patent, resulting from R&D activities and object of the same unique exploitation licence as the main patent; and 5° Patentable inventions (only for SMEs as defined[3]), all of which capitalized as a fixed asset. The French IP regime includes therefore also the third category of IP assets for small and medium size enterprises[4]. The scope covers patentable, but not patented, inventions, for which the patentability is certified by the French INPI [i.e. inventions which have a level of patentability equivalent to that of a patent or a utility certificate, the only difference being the

[2] Category limited to companies which are not part of a group with more than €50m turnover and gross revenues of €7.5m from all IP assets.

[3] The only taxpayers that may qualify for such measure are those that have no more than EUR 50 million in global group wide yearly turnover and that do not earn more than EUR 7.5 million per year in gross revenues from all IP assets, using a five-year average for both calculations.

[4] Given that such inventions are substantially similar to the IP assets in the first two categories, they should be certified in a transparent certification process by a competent government agency that is independent from the tax administration.

absence of publication].

The agreed description indicates that both royalties[5] from licensing an IP right, and capital gains[6] on the sale/transfer of qualifying IP rights between unrelated parties fall under the FR IP regime; embedded royalties are excluded.

2. Nexus ratio:

The tax advantage granted under the FR IP regime is a reduced tax rate.

Such reduced rate applies on the relevant qualifying net[7] IP income. The portion of income qualified for the reduced rate is calculated under the modified nexus formula: [QE (+30% uplift) / OE x OI]:

- QE being qualifying expenditure excluding outsourcing to related parties and acquisition costs;

- OE being overall expenditure, including outsourcing to related parties and acquisition costs;

- OI being overall income calculated as a net income and including royalties and capital gains (with a transfer pricing method).

3. Tracking and tracing:

MS must require companies to track expenditure, IP assets and income. When such tracking would be unrealistic and require arbitrary judgements, MS may allow the application of the nexus approach so that the nexus may be between expenditure, products arising from IP assets and income (product-based approach). It requires tracking of all QE and OE at the level of the product.

The FR law sets specific provisions regarding the tracking and tracing requirements under the IP regime. The entity shall keep any accounting record needed to determine direct and indirect income and expenses related to the IP assets involved, so tracking and tracing is ensured.

4. Rebuttable presumption[8]:

---

[5] Net income consisting in any licence fee received under a licence agreement pertaining to a qualifying IP asset (or any grouping of qualifying IP assets).

[6] Net proceeds from the alienation of qualifying IP assets.

[7] Calculated by deducting from the gross IP income derived for each qualifying IP asset (or any appropriate grouping of qualifying IP assets):

- the total expenditures of the year incurred in relation to the IP asset (or appropriate grouping), which correspond to the overall expenditure incurred to develop or acquire the IP asset as defined for computing the nexus ratio's denominator,

- the past total expenditures in relation to the IP asset (or appropriate grouping) recognized during the whole period for which election was made for the regime,

- and any net losses in relation to the IP asset (or appropriate grouping) incurred in previous years during the whole period for which election was made for the regime.

[8] Jurisdictions could treat the nexus ratio as a rebuttable presumption but would need to limit to exceptional situations where the ratio could be rebutted to those that meet at minimum the following requirements: the taxpayer should first

The FR IP regime does have a rebuttable presumption provision for exceptional circumstances and after prior authorization.

This works by replacing the nexus ratio with a replacement ratio representing the proportion of the value of the qualifying asset that would actually be attributable to the R&D activities that it carries out directly or indirectly by unrelated companies. The proportion of the value aforementioned corresponds to the proportion recognized to them by unrelated persons, who, under similar conditions, undertake R&D activities. The authorization is thus granted when: i) the nexus ratio is higher than 32.5%[9]; and ii) the replacement ratio is significantly higher than the nexus ratio because of exceptional circumstances beyond the control of the taxpayer. Cases where an exceptional circumstance arises will be reviewed on a case-by-case basis.

The taxpayer will have to establish that, where a situation is deemed "exceptional", there must be a causal link between those exceptional circumstances and the replacement ratio being significantly higher that the nexus ratio.

The prior authorization to rebut the presumption is valid for a five-year period, provided that the relevant conditions continue to be met by the end of each tax year. Such prior authorization will be exchanged spontaneously with MS.

5. Treatment of losses[10]:

There is no initial restriction on the offset of those losses against standard rate profits, but losses associated with any qualifying IP asset (or appropriate grouping of qualifying IP assets) and incurred during the whole period for which election for the regime was made will be recaptured. This recapture mechanism consists in deducting previous losses associated with an IP asset from subsequent net income pertaining to the said IP asset. Therefore, once election is made for the regime with respect to a qualifying IP asset, only IP profits exceeding previous losses in relation to the said asset will benefit from the reduced tax rate.

As an additional safeguard ensuring that a taxpayer may not opt out and then opt into the regime again to avoid recapture of previous losses, a taxpayer opting out of the regime after having elected for the regime with respect to a qualifying IP asset, will not be allowed to re-enter the regime. This ensures that any previous loss remains to be recaptured when the regime applies.

Criterion 4:

"whether the rules for profit determination in respect of activities within a multinational group

use the nexus ratio to establish the presumed amount of income that could qualify for benefits; the nexus ratio (excluding the up-lift) should equal or exceed 25%; the taxpayer should demonstrate that because of exceptional circumstances, the application of the nexus ratio would result in an outcome inconsistent with the nexus approach (burden of proof on the taxpayer).

[9] ie 25% with the 30% uplift, equivalent to 25% without the uplift.

[10] Note 14 to Action 5 Report: Jurisdictions should also use any tax losses associated with the IP income in a manner that is consistent with domestic legislation and that does not allow the diversion of those losses against income that is taxed at the ordinary rate.

of companies departs from internationally accepted principles, notably the rules agreed upon within the OECD”

- General transfer pricing rules:

France applies the arm's length principle (article 57 of the General Tax Code) and its administrative regulations make reference to the OECD Transfer Pricing Guidelines.

The arm's length principle is relevant to the following features of a patent box: the reduction of the tax base by a fixed percentage, if any; the calculation of royalty profits; the application of safe harbour rules; the asymmetrical treatment of losses (if any).

- Reduction of the tax base by a fixed percentage: *in principle, reducing a company's arm's length profits by a fixed amount means that the final result does not reflect the arm's length principle. This is a question about the circumstances in which fixed reductions of the tax are acceptable and is therefore part of the overall assessment that the Group need to make.*

The tax benefit under the French IP regime is granted through a reduced tax rate and not a reduction in the tax base. Therefore, the amount of the basis of income is not modified in the IP regime in a way that would not reflect the arm's length principle.

- Calculation of royalty profit (embedded royalties): *where transfer pricing rules exist, the profits that go into a patent box will reflect the arm's length principle because they are just a part of the company's total profit. In principle this applies both to royalties and embedded royalties. If the IP regime covers also the latter category, its identification within the sale price of a product should rely on transfer pricing principles.*

Embedded royalties are excluded from the French IP regime.

- Safe harbour rules: *adoption of safe harbours is not in accordance with internationally agreed principles; safe harbours are not recommended in the Transfer Pricing Guidelines.*[11]

The French IP Regime does not seem to provide for such safe harbour rules.

- Asymmetrical treatment of losses: *where the profits from particular IP assets are taxed at a lower rate in a patent box then the losses should be treated in the same way and not deducted outside the box at a higher rate.*

What has been written under criterion 3 above on losses applies analogously to criterion 4.

Criterion 5:

“whether the tax measures lack transparency, including where legal provisions are relaxed at administrative level in a non-transparent way”

[11] *Transfer Pricing Guidelines*, p167.

All preconditions necessary for the granting of a tax benefit should be clearly laid down in publicly available laws, decrees, regulations *etc*. before a measure can be considered transparent.

The nexus approach contains commitments to additional transparency in three areas. These concern the third category of qualifying assets, new entrants to existing IP regimes after 6 February 2015 and the rebuttable presumption rule. Commitments regarding new entrants to pre-existing regimes are not subject to the present assessment and are part of a separate monitoring process. The commitments in the 2015 Report cover both the report of certain information to the Forum on Harmful Tax Practices and the spontaneous exchange of information between competent authorities.

Third category of qualifying assets:

First, the 3rd category of assets must be certified as such in a transparent certification process by a competent government agency that is independent from the tax administration. In order to certify their patentability, the French authorities will implement a certification process of patentability by the INPI. Specifically, this certification could be issued in the course or in a process similar to that of a patent application procedure or a utility certificate application procedure interrupted before publication. The invention would then be considered non-obvious, useful and new for the claims validated by the INPI. As such, the certification procedure is meant to be as rigorous as the patent or utility certificate process, except the demand would not be made public. We do not have any information for the moment whether such rules on the certification procedure have already been adopted, nor have they been communicated to us.

Second, in order to ensure the annual reporting and spontaneous exchange of information, the taxpayer shall provide the tax administration with the relevant information on a yearly basis. This will allow France to provide the relevant information required to meet the reporting obligation. France will also exchange information spontaneously about taxpayers benefiting from this category of IP assets.

Rebuttable presumption:

Under the FR IP regime, the nexus ratio can be treated as a rebuttable presumption. However, there is a requirement that the conditions for continuing applying the presumption are met at the end of each year. The prior authorization to rebut the presumption is valid for a five-year period, provided that the relevant conditions continue to be met at the end of each tax year. Such prior authorization will be exchanged spontaneously.

In addition to the “standard” tracking and tracing reporting system the taxpayer must provide on a yearly basis the following information to the tax administration: - the list of assets benefiting from the regime, - the net income deriving from these assets. France will thus be able to collect, report and exchange the relevant information.

Overall assessment:

In light of the assessment made under all Code criteria, the French IP regime is considered as **not harmful** from a CoC point of view.

Overall the FR IP regime is in line with the modified nexus approach. Similar to other recently introduced or amended measures, question marks remain in the grids in relation to criteria 1b and 2b.

In summary, the Group's overall assessment is that this measure is **not harmful**.