

# TAX NEWS REVIEW

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This review of tax news focuses on the main case law decisions of recent months

## I. Subsidies paid by a private entity does not reduce the calculation basis for the research tax credit

CE, 9<sup>th</sup> ch. et 10<sup>th</sup> ch., July 12; 2023, n° 463363, FCBA, decision mentioned in the Recueil Lebon

As a reminder, industrial, commercial, or agricultural businesses can benefit from a research tax credit (*CIR* for *Crédit d'Impôt Recherche*) for their research and development expenses (French Tax Code, Article 244 quater B). However, public subsidies they have received for operations eligible for the *CIR* must be deducted from the calculation basis of this credit, whether they are definitively acquired or refundable (French Tax Code, Article 244 quater B, III).

In this case, an industrial technical center received subsidies from a non-profit association (1901 Law) with a public service mission. The tax authorities considered that these aids should be deducted from the *CIR* base. Arguing the opposite, the center asked the administrative Court to annul this administrative decision. As the request was rejected, it had filed an appeal.

The Administrative Court of Appeal had, on its part, considered that any aid paid for research projects, whether from the use of resources received mandatory and without compensation, coming from either a public authority or a private entity with a public service mission, should be regarded as constituting a public subsidy. In this case, it had thus ruled that the center should deduct the aids received from the association.

However, the French Administrative Supreme Court overturns this decision on the grounds that public subsidy is defined as any aid paid by a public legal entity for operations eligible for the tax credit.

Before this ruling, no definition had been proposed by case law or the authorities. Only a non-exhaustive list of aids to be deducted for the calculation of the *CIR* had been compiled by the Administration but it is no longer in force.

The Administrative Supreme Court finally settles the matter ruling that the aids paid in 2013 and 2014 for the financing of research operations by the association to the center are not public subsidies. Indeed, an association is a private entity. Therefore, the aids did not need to be deducted from the *CIR* calculation basis.

*Disputed claims on this subject may be filed in case such subsidies were wrongly deducted from the CIR base for the years 2020 to 2022.*

## **II. The concept of turnover includes the characteristic products of the company's economic model with regard to social contribution on corporate income tax (CIT)**

CE, 9<sup>th</sup> and 10<sup>th</sup> chambers, July 26, 2023, No. 466220, Mayapan, decision mentioned in the Recueil Lebon

French CIT is subject to a social contribution of 3.3% of the amount of this tax. However, SMEs whose capital meets certain conditions of release and ownership are exempt when their turnover is less than €7,630,000 (French Tax Code, Article 235 ter ZC). It should be noted that, from a tax perspective, companies must adhere to the definitions set forth in the accounting rules (codified in the General Accounting Plan), provided that these not incompatible with the rules applicable to the tax base (French Tax Code, Ann. III, Article 38 quater). Therefore, from an accounting standpoint, turnover corresponds to the amount of business conducted by the entity with third parties as part of its normal and customary professional activity (General Accounting Plan, Article 512-2). Generally, accounting practice has a restrictive interpretation of this notion and does not include financial income. However, some, such as the French Accounting Rules Authority (ANC for *Autorité des normes comptables*) in its draft regulation on revenue recognition, argue that a broader interpretation could be adopted, particularly with regard to the company's economic model.

In this case, it concerned a company whose sole activity was holding stakes in legal entities and providing these companies with interest-bearing loans. This company wanted to benefit from the exemption, arguing that this financial income did not increase its turnover. In this case, the French Tax Authority had adopted a broader definition of turnover, including financial income. Consequently, it had denied the exemption. The decision of the French Administrative Court of Appeal also supported this view, leading the company to file a cassation complaint.

In this decision, the French Administrative Supreme Court adopts a broad interpretation of turnover and states that, with regard to the social contribution on CIT, it refers to the amount of revenue derived from all operations carried out by the taxpayer in the course of its normal and customary professional activity, including, where applicable, in view of its economic model, financial income.

In this case, loans were one of the normal and customary ways of pursuing profit and characterized its economic model. Therefore, interest was part of the turnover, even though they were financial income. The company could not claim the exemption.

The Administrative Supreme court had previously relied on the economic model to include in the turnover the gains on the disposal of assets, with regard to the former exceptional contribution accompanying CIT (French Tax Code, Article 235 ter ZAA) (CE 10-7-2019 No. 412968).

However, beyond this specific case, the Tax Authority generally takes a rather restrictive view of turnover concerning the social contribution on CIT, considering that financial income should be excluded except in cases where specific regulations for certain sectors of activity provide otherwise (BOI-IS-AUT-10-10, No. 20). It also adopts the same definition for the reduced rate applicable to SMEs (BOI-IS-LIQ-20-10, No. 40).

*Therefore, the question of whether the Tax Authority's doctrine is opposable to it on the basis of Article L 80 A of the French Tax Procedures Book can reasonably be raised.*

### **III. Future revenue prospects can be considered to assess the commercial nature of an aid and its deductibility of taxable income**

CE, 9<sup>th</sup> and 10<sup>th</sup> chambers, July 26, 2023, No. 463846, Lamaï, decision mentioned in the Recueil Lebon

In the context of corporate income tax (CIT), financial aids are not deductible from the taxable income unless they are granted in the context of insolvency proceedings in some circumstances (French Tax Code, Article 39, 13). They are defined in opposition to commercial aids. According to case-law, an aid is considered commercial if it originates from commercial relationships and if it is granted to maintain market opportunities or preserve sources of supply.

In this case, a company deducted a debt waiver granted to a financially troubled subsidiary, and the French Tax Authority considered this aid to be of a financial nature and therefore not deductible.

The company argued that the waiver was motivated by a commercial relationship because there was an agreement under which it licensed its technology to its subsidiary and would become the owner of any improvements made to this technology by the subsidiary for reuse in one of its own activities. Therefore, it argued that it assisted its subsidiary out of commercial interest.

However, the Administrative Court of Appeal rejected these arguments on the grounds that, firstly, there was no consideration other than ownership of the improvements in favor of the granting parent company, which in itself demonstrated a lack of commercial relationship, and secondly, the activity for which the improvements were intended to be used had generated no revenue at the time the debt waiver was granted and only experienced development in subsequent years.

Nevertheless, the Administrative Supreme Court overturned the decision on the grounds that the fact that an aid is motivated by the development of an activity that, at the time the aid was granted, has not generated any revenue is nevertheless capable of giving the aid a commercial nature when the prospects for the development of this activity do not appear, at that same date, to be purely speculative. It was therefore necessary to determine whether, at the date of the debt waiver, there was a prospect for the granting parent company to generate revenue from the improvements made to its technology by its subsidiary licensee.

Finally, it decided the case on its merits, stating that even if the waiver might, in this case, have been partly motivated by financial considerations, it must be regarded as predominantly having a commercial nature and therefore as being deductible. Indeed, at the time of the waiver, the parent company's activity related to the licensed technology had become very important, and the prospects for commercial development of this technology appeared promising due to the improvements made by the subsidiary licensee. The latter had already marketed and sold products manufactured using it.

*Given the difference in tax treatment, companies are therefore well-advised to thoroughly document the factors that give a commercial nature to the aids they grant.*