

## France issues comprehensive draft guidance on digital services tax

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### Executive summary

On 23 and 30 March 2020, the French Tax Authorities (FTA) issued new draft guidance with respect to the Digital Services Tax (DST). This draft guidance focuses on compliance issues and also includes the first guidance on the scope and computation of the DST. The draft guidance is subject to public consultation until 23 May 2020. Thus, there may be revisions before the guidance is issued in final form. However, the guidance is already binding on the FTA, so that a taxpayer that follows this draft guidance will not be subject to reassessment by the FTA.

This Alert summarizes the main features of the draft guidance.

### Detailed discussion

#### Background

France enacted its DST in July 2019.<sup>1</sup> The DST is imposed at a single rate of 3% levied on gross income derived from certain digital services (so-called "taxable services") for which the French Government deems user participation essential in creating value. Taxable services include targeted online advertising (including the sale of user data) and online digital intermediation services (i.e., platforms and marketplaces), whether they are provided in the context of a relationship between businesses (B to B), between businesses and consumers (B to C) or between consumers (C to C).

Only companies with worldwide revenue from taxable services of at least €750 million annually and with total taxable revenue from taxable services obtained in France exceeding €25 million annually are subject to the tax, based on an apportionment of French deemed services to be computed for each category of taxable services.

The FTA first published draft guidance with respect to the DST covering compliance issues (reporting and accounting obligations, collection, control and litigation) on 16 October 2019.

The draft guidance published on 23 and 30 March 2020 includes further development of that initial draft on compliance issues and also addresses the scope and computation of the DST.

## Scope of the tax

Imposition of the DST requires four cumulative conditions:

- ▶ Existence of a taxable service
- ▶ Location of the taxable service in France
- ▶ Receipt of income in return for the taxable service
- ▶ Satisfaction of the revenue thresholds for application of the DST, determined on the basis of all entities that are directly or indirectly affiliated based on control.

**Taxable services:** The guidance broadly defines the concept of digital interface as software that allows one or more users to both send and receive information. A digital interface can involve several types of software interacting with each other when they constitute a consistent whole characterized by a set of common functionalities and coordinated operations.

There are two categories of taxable services: digital intermediation and targeted advertising (which includes the sale of data for the purpose of targeted advertising). Each category is divided into two sub-categories. Establishing the sub-category in which a taxable service belongs is important because each sub-category has its own set of rules in terms of territoriality and computation of the ratio of French deemed services (the “French presence ratio”).

*Digital intermediation services* are services that allow users, through a digital interface, to interact with each other.

The first sub-category of digital intermediation services includes marketplaces providing a digital interface that enables users to conduct transactions between them (the supply of goods or services).

The second sub-category includes networking services allowing users to interact with each other without being able to proceed with transactions through the digital interface itself (e.g., social networks, services allowing users to play online together, services allowing users to meet each other).

The guidance also provides information on certain services that are excluded from the scope of digital intermediation.

The first exemption applies to digital interfaces where the main purpose is the supply of digital content (i.e., supplying digital content owned by the operator through the digital interface), to provide communication services to users (i.e., supplying software resources allowing users to exchange with pre-selected interlocutors) or to provide payment services to users.

To fall within this exemption, (i) the services must be provided directly by the operator of the digital interface; and (ii) digital intermediation must be ancillary to the supply of these services (i.e., interactions between users are only a means of benefiting from the principal service or benefiting from a better quality of service).

The second exemption applies to financial services as described below:

- i. Interbank settlement systems or systems for the settlement and delivery of financial instruments
- ii. Trading platforms and trading systems of “systematic internalisers”
- iii. Participating investment advisory activities and intermediation services in participatory finance
- iv. Other networking systems that are listed by decree (note that no decree was issued on 31 December 2019 for 2020).

The third exemption applies to the purchase or sale of services aimed at placing targeted advertising messages. In this situation, the digital interface makes placement possible or influences the way it is carried out, without necessarily leading directly to such placement (e.g., ad exchanges, supply-side and demand-side platforms, and ad servers). These services are not necessarily marketed to advertisers, but the exemption only applies in the case of targeted advertising (i.e., there is no exemption if the service involves non-targeted advertising messages).

*Targeted advertising* is characterized by three cumulative conditions: (i) services are marketed to advertisers or their agents; (ii) advertising messages are placed on a digital interface; and (iii) the messages are targeted based on users' data (either collected on the interface itself or collected/generated when users consult other digital interfaces).

The guidance provides the following specifications:

- i. An advertiser is the one who seeks to disseminate advertising messages.
- ii. Taxable services are those that allow or facilitate the placement of advertising messages on digital interfaces without directly ensuring the placement.
- iii. Targeted advertising messages are designed, at least partially, based on data from the user of the digital interface on which the message is placed. Such data, notably keywords in a search engine, identification username or password and personal or non-personal data, could have been collected on any digital interface. However, not taken into account are data not collected or generated via digital interfaces; data that have no influence on the recipient or the content of the advertising message; and data related to the digital interface itself but not specifically related to the user of the digital interface.

The first sub-category of targeted advertising includes user data transmission services for placing advertising messages that are limited to the transmission of user data for placing advertising messages.

The second sub-category includes advertising placement services that are not limited to such transmission, whether or not they include access to a database of users.

The guidance provides examples of taxable services in the programmatic sale of advertising: demand-side platforms (DSPs), trading desks (when not included in a DSP), ad servers (on the demand side), data management platforms (DMPs), and ad verification.

According to the guidance, services rendered outside the programmatic sale of advertising are also within the scope of the DST as online targeted advertising services that meet the conditions set out above, including:

- i. Websites comparing commercial offers, for goods or services, insofar they are paid for by the people promoting these offers and these offers are presented to the user of the digital interface based on information he or she has entered.

- ii. Advertising sites or directories, if they are remunerated by the persons publishing these advertisements or appearing in these directories and if these advertisements are presented to the user of the digital interface based on information that he or she has entered.
- iii. Any other service that is paid for by persons for the placement of internet links to the sites operated by such persons, provided that the links are presented to the user of the digital interface based on information that he or she has entered.

Taxable services provided between members of the same DST group are excluded from the scope of the tax. A DST group includes all related companies pursuant to article L233-16 of the French Commercial Code (FCC), which defines the concept of control as discussed in more detail below. The guidance specifies that this exemption is to be determined globally, without the potential of applying it, for a taxable service, to a fraction of the clientele.

**Location of taxable services:** The guidance provides information on how to determine if a user of a digital interface is located in France.

A user is deemed to be located in France when he or she accesses the digital interface from a terminal itself located in France. This terminal could be any device allowing access to the digital interface, such as computer, tablet or mobile phone.

The location of the terminal in France can be determined by any means, including IP address, geolocation data or information collected through various tracking and data collection devices. It is also possible to use a bundle of matching indicators to establish location with a high level of probability, such as data regarding a customer's account or usual place of residence.

With respect to the criteria of number of accounts opened for networking services and the computation of French deemed services/French presence ratio, the guidance specifies that the renewal, including tacit renewal, of an account is treated as the opening of an account.

The following taxable services are deemed to be provided in France during a tax year for:

- i. Marketplaces when, for at least one supply of goods or services for which the transaction is carried out through the digital interface, either the seller or the buyer is located in France (first sub-category of intermediation services).

- ii. Networking services when at least one of the users of the digital interface has an account that was opened, during that same year or a previous year, in France and that allowed him or her to access all or part of the functionalities of the digital interface during the tax year (second sub-category of intermediation services).
- iii. Placement services when at least one advertising message was placed on a digital interface through which a user was accessed by a terminal located in France (first sub-category of online targeted advertising services).
- iv. Data transmission services when all or part of the data is transmitted during that same year and at least one of the users to whom this data relates was located in France when the data was generated or collected (including when the data was generated or collected during a previous year) (second sub-category of online targeted advertising services).

**Receipt of income in return for a taxable service:** the guidance specifies that the fact that these amounts were only collected during a part of the year or from users not located in France is irrelevant.

**Threshold:** the guidance confirms that taxable amounts are calculated according to the same rules as for the calculation of the tax basis (discussed in more detail below), except that the calculation is made at the level of all taxable services. For the worldwide threshold (€750m of revenue from in-scope activities), the computation is made without applying the French presence ratio, while such ratio is applied in determining the French threshold of €25m of revenue derived from in-scope activities. The reference year for the taxable amounts considered is the year preceding the year for which the taxable amounts are paid for the taxable services (DST is assessed over a calendar year).

With respect to the DST group, the guidance confirms that the taxable amounts of each member of the group must be added and that the determination of the control relationship, as defined by article L233-16 of the FCC, is made on the date of the triggering event (i.e., 31 December of the calendar year in which taxable services were supplied).

With respect to the concept of control provided in article L233-16 of the FCC, the guidance specifies the following:

One company controls another when it has, directly or indirectly:

- i. More than 50% of the voting rights of another company

- ii. The power to appoint, over two successive financial years, more than half of the members of the administrative, management or supervisory bodies of another company (this is notably the case when the company has held, directly or indirectly, more than 40% of the voting rights during this period and no other partner or shareholder held, directly or indirectly, a greater percentage of such rights)
- iii. The right to exercise a dominant influence over the other by virtue of an agreement or statutory clauses, where permitted by applicable law

Several companies jointly control another company if one of these three conditions is likely to be fulfilled as a result of the joint action of those companies, irrespective of whether such joint action actually takes place.

A company is linked in a controlling relationship with:

- i. Companies that it controls, directly or indirectly (daughters, granddaughters and other descendants)
- ii. Companies that control it, directly or indirectly (parents, grandparents and other relatives in the ascending line)
- iii. Companies controlled, directly or indirectly, by the companies described in (ii) (cousins of any degree).
- iv. Companies controlled, directly or indirectly, jointly by two or more of the following companies: the companies in question and the companies described in (i), (ii) or (iii), or companies falling within the scope of this provision.

Two companies linked to a third company are linked to each other and therefore deemed to belong to the same group.

All such related companies together constitute a group referred to as the DST group.

### Computation of the tax

The triggering event for the tax is 31 December of the year during which amounts were received as consideration for the supply in France of a taxable service, referred to as the "tax year."

However, amounts considered in the calculation of the tax due for a tax year are amounts for the supply of a taxable service in France during the year preceding the tax year.

**Taxpayer:** The person liable for the tax is the person that collects the sums paid as consideration for taxable services, and the liability to pay the tax occurs at the same time as the triggering event (i.e., 31 December).

When the same taxable service is operated successively by several persons during the same tax year, each is liable for the amounts it has received.

**Formula:** the guidance confirms that the amount of tax to be paid, calculated for each category of taxable services, is equal to the worldwide taxable amounts of each member of the DST group, multiplied by the French presence ratio of the taxable service considered. The tax basis obtained through this formula is subject to the 3% levy.

**Taxable amounts:** the guidance specifies for each category of taxable services, the amounts to be considered for the computation of the tax. First and foremost, the guidance specifies that the determination of taxable amounts and the calculation of the French presence ratio are made at the level of each taxable service.

The guidance provides that amounts refunded by the taxpayer to its users for a taxable service are deducted from the amounts received in the tax year in which the refund is made.

If the taxable amounts are paid in a foreign currency, the taxpayer must convert them using the exchange rate published in the *Official Journal of the European Union* on the first day of the month in which the amounts were paid.

When the taxpayer uses several currencies and converts all of them into the same currency for purposes of its accounts, the conversion carried out for the DST may be made from this same currency.

For all in-scope/taxable services, all revenues received by the taxpayer from users for taxable services are taxed, regardless of the billing method and even if the transaction was not carried out via the interface. However, amounts received by the taxpayer as an intermediary of a payment are not taxable (e.g., if payment for the service/sale is made through the marketplace/platform, which only keeps a portion for its intermediation service, only such portion is taxable from a DST perspective).

Amounts received from users for economically independent services are excluded from taxable amounts. The guidance specifies that a service is not independent if: (i) the use of the digital interface and the supply of the service are strictly linked; and (ii) the service constitutes a means for using the digital interface. Also, assessment is made at the level of customers based on objective criteria. The guidance provides several examples.

Mixed services are defined as services that could be analyzed as both digital intermediation services and targeted advertising services. In this case, taxable amounts received by the taxpayer are taxed as digital intermediation services if targeted advertising services constitute a means for using the digital interface; if not, amounts are taxed as targeted advertising services.

**French presence ratio:** the ratio represents the proportion of French users for each sub-category of services. The assessment is made at the level of each taxable service, so that each taxable service has its own ratio. The criteria used are the same as for determining the location of services described above.

For marketplaces (first sub-category of intermediation services), the ratio is determined based on the proportion of supplies of goods and services made through the marketplace during the tax year for which one of the users of the service is located in France.

For networking services (second sub-category of intermediation services), the ratio is determined based on the proportion of users who have an account that was opened in France, including prior to the tax year, and who used the intermediation service during the tax year.

For placement services (first sub-category of online targeted advertising services), the ratio is determined according to the proportion of advertising messages that have been targeted, during the tax year, to a user located in France.

For data transmission services (second sub-category of online targeted advertising services), the ratio is determined according to the proportion of users for whom all or part of the data transmitted was generated or collected when consulting a digital interface in France.

The guidance notes that if a taxable service is successively supplied by different taxpayers during the year, the ratio is assessed for the whole year for each taxpayer, unless the taxpayer demonstrates that he cannot obtain the necessary information on the periods during which the service is provided by a different taxpayer.

## Compliance

**Taxpayers must provide to the FTA upon its request all documents detailing sums collected by sub-category of taxable services:** the guidance published on 16 October 2019 provides details of the information to be retained, for

each month of the tax year and for each sub-category of service. The new guidance published on 23 and 30 March 2020 adds a new category of information to be retained relating to economically independent services.

The below table summarizes information to be retained:

Category of item to be retained	Sub-category of taxable services			
	Marketplaces	Networking services	Placement services	Transmission of data services
Amounts taxed and collected	When the same service is remunerated in different ways, each is distinguished as follows			
	Distinction is made between amounts paid by user-buyers and amounts paid by seller-users of the digital interface	No specification	No specification	No specification
Amounts excluded as economically independent services	Supplies of goods and services provided to users of the digital interface that are independent of access to or use of the digital interface shall be identified. The relevant amounts shall be distinguished for each commercial offer.		Non-applicable	
Quantitative items related to the French presence ratio	The method used to locate users of the digital interface shall be specified and the data on which it is based shall be retained. Where, for the same service, different methods are implemented, the following elements shall be distinguished for each of them.			
	Total number of transactions carried out for which: <ul style="list-style-type: none"> <li>▶ the buyer is located in France but not the seller</li> <li>▶ the seller is located in France but not the buyer</li> <li>▶ both the buyer and the seller are located in France</li> <li>▶ neither the buyer nor the seller is located in France</li> </ul>	Total number of accounts that: <ul style="list-style-type: none"> <li>▶ were opened from France</li> <li>▶ were not opened from France</li> <li>▶ In both cases, a distinction is made between accounts used to use the interface since the beginning of the year and other accounts</li> </ul>	Total number of advertising impressions made: <ul style="list-style-type: none"> <li>▶ for which the Internet user is located in France</li> <li>▶ for which the Internet user is not located in France</li> </ul>	Total number of users whose data have been sold: <ul style="list-style-type: none"> <li>▶ for which all or part of the data was generated or collected from France</li> <li>▶ for which none of the data was generated or collected from France</li> </ul>
Amounts excluded as products	Amounts having a direct and inseparable link to the consumption of: <ul style="list-style-type: none"> <li>▶ energy products or electricity</li> <li>▶ alcohol and alcoholic beverages</li> <li>▶ manufactured tobacco products</li> </ul>	Non-applicable	Non-applicable	Non-applicable

**Filing obligation:** the guidance confirms that the DST is declared according to the same procedures as are applicable to French Value-Added Tax (VAT), subject to some adjustments depending on the taxable regime applicable as indicated in

the law (i.e., with the VAT return of March or of the first trimester of the year following the year of taxation for the normal regime and with the annual VAT return of the year following the year of taxation for the simplified regime).

**Payment:** as indicated in the law, the guidance confirms that the tax is paid by two advance payments for the ongoing year of taxation (calendar year), each of which amounts to at least 50% of the amount of the DST due the preceding year. Each installment is paid with the filing of the VAT return in April and October of the year, and the balance of the payment is due in April of the following year with the filing of the DST return.

For 2020 only, the guidance published on 23 and 30 March confirms the previous official statement from the FTA<sup>2</sup> that taxpayers may postpone the payment of the two installments due for 2020 into a single payment in December 2020. The taxpayer will not face penalties or late payment interest. This postponement is related to the ongoing discussions at the Organisation for Economic Co-operation and Development (OECD) on the project on addressing the tax challenges of the digitalization of the economy.

With respect to the amount of the advance payments, the guidance provides that: (i) the taxpayer may either suspend payment or reduce the amount where it is able to establish that the trend in its revenue justifies such suspension or reduction; or (ii) where the amount of the advance payments is higher than the amount of tax, the excess will be deducted from the following year's advance payments or reimbursed if such amounts are not enough.

If the amount of the balance of the payment of DST is 20% greater than the amount of the installments paid, late payment interest (0.20% per month) and a 5% penalty are applicable to the amounts whose payment has been deferred pursuant to the procedure described above. These penalties also apply to the entire value of the first installment where the taxpayer has failed to pay it, even if the resulting shortfall is less than 20%.

**Tax audit and tax litigation:** as indicated in the law, the guidance restates that the DST is subject to the same procedures as are applicable to French VAT, except for the statute of limitations which is six years for the DST instead of three years for VAT.

**DST consolidated group:** related companies under article L233-16 of the FCC may constitute a DST consolidated group. Among the controlled companies, one is designated to

be the sole party responsible for the DST filing requirements and payment obligations on behalf of all the companies belonging to the DST group as described above.

All related companies must agree to the election of the DST consolidated group. The designated company of the DST consolidated group must then send evidence of this agreement to the FTA. However, the guidance specifies that one company controlling another may give consent on its behalf. The guidance provides that a list of group members and the consent of each member is to be attached to the election.

According to the law, the election applies for a minimum period of three years and each new related company is considered to have agreed to the existing election unless it expressly disagrees. The guidance specifies that in this specific case the group ceases to exist even if the minimum three-year period for the election is not reached.

Any member of the DST consolidated group may renounce the election after the minimum three-year period. The guidance specifies that the renunciation results in the termination of the DST group.

However, when a member no longer meets the conditions of control it ceases to belong to that consolidated group and the group continues to exist. In that case, advance payments already paid for that member will be deducted at the time of the tax determination of the following year.

The draft guidance published on 16 October 2019 stated that members of the DST consolidated group that are not established in France but whose designated company is established in France do not need to appoint a fiscal representative in France. However, that provision has been eliminated because the draft guidance published on 23 and 30 March 2020 provides for the contrary.

## Implications

The rules provided in the guidance pertaining to the French DST are complicated and must be applied carefully. Taxpayers should use the additional information provided by the FTA in the draft guidance to review their initial assessments of the application of the DST. This includes in particular the information regarding the group concept as broadly defined by article L. 233-16 of the FCC.

Taxpayers also should continue to monitor developments with respect to the French DST, including the possibility of further revisions before the draft guidance is finalized.

## Endnotes

1. See EY Global Tax Alert, [France's Parliamentary Commission agrees on Digital Services Tax](#), dated 3 July 2019.
2. See EY Global Tax Alert, [French tax authorities confirm postponement of Digital Services Tax payments for 2020, but 2019 payments remain due](#), dated 11 February 2020.

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For additional information with respect to this Alert, please contact the following:

### Ernst & Young Société d'Avocats, Paris

- ▶ Jean-Pierre Lieb      [jean.pierre.lieb@ey-avocats.com](mailto:jean.pierre.lieb@ey-avocats.com)
- ▶ Morgan Vail          [morgan.vail@ey-avocats.com](mailto:morgan.vail@ey-avocats.com)

### Ernst & Young LLP (United States), French Tax Desk, New York

- ▶ Frederic Vallat      [frederic.vallat@ey.com](mailto:frederic.vallat@ey.com)
- ▶ Mathieu Pinon        [mathieu.pinon1@ey.com](mailto:mathieu.pinon1@ey.com)

### Ernst & Young LLP (United States), Washington, DC

- ▶ Barbara M. Angus     [barbara.angus@ey.com](mailto:barbara.angus@ey.com)

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