



Agency permanent establishment – the Zimmer case

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Facts

- Before 1995, Zimmer SAS (France) acts as a distributor in France for products made by Zimmer Ltd (UK), a related company
- In 1995, Zimmer SAS becomes a commissionnaire for Zimmer Ltd (signs commission contract with Zimmer Ltd, sells facilities and stock of products to Zimmer Ltd)
- Under the commission contract:
 - Zimmer SAS is charged with the sale in France of the products of Zimmer Ltd in its own name (not in the name of Zimmer Ltd), but for the account of and at the risk of Zimmer Ltd
 - Zimmer SAS may accept orders, display quotes and documents in tender offers, negotiate prices, grant discounts or terms of payment with current or new customers and conclude sales contracts on behalf of Zimmer Ltd without its prior approval
- French tax administration: Zimmer Ltd has a PE in France under the dependent agent provision of France-UK treaty (signed in 1968)

Outcome

- *Conseil d'Etat* (31 March 2010) quashes decision made by Administrative Court of Appeals of Paris and decides there is no agency PE
- *Conseil d'Etat*:
Under the France-UK treaty (equivalent to Art. 5(5) and 5(6) OECD and identical to 1963 OECD Model), « a company resident in France which is controlled by a company resident in the UK can only constitute a PE of the latter if it cannot be considered as an independent agent of the company resident in the UK and if it habitually exercises in France authority permitting it to bind that company in a commercial relationship with respect to the operations which constitute that company's own activities »

Outcome

According to the terms of Art. L 132–1 of the French Commercial Code:

“A *commissionnaire* is a person who acts in his own name or under a business name for the account of a principal (“*commettant*”) ...”

“It follows from these provisions [as interpreted by French case law] that contracts concluded by a *commissionnaire*, even though they are concluded for the account of its principal, do not bind the latter directly vis-à-vis the counterparties of the *commissionnaire*.”

“...unless it appears either from the express terms of the contract of commission, or from other factual elements relating to the arrangement, that despite the ‘commission’ title given by the parties to the contract between them, the principal is personally bound by the contracts concluded with third parties by his *commissionnaire* who must, therefore, for this reason, be regarded as his representative and constitute a permanent establishment.”

Issue: combination of 5(5) and 5(6)

- In the French text, Art. 5(6) excludes « **commissionnaires** ». Is the debate closed?
 - No: Although the **examples** of 5(6) may seem unnecessary for commissionnaires (because of 5(5), the **general rule** of 5(6) excludes independent agents
 - Therefore the real test, for dependent persons, is the authority to conclude contracts in the name of an enterprise (5(5))
 - In the Zimmer case, the dependent character of Zimmer SAS was not even in dispute. The *Conseil d'Etat* applies the test in 5(5)

Issue: Literal and juridical interpretation of 5(5) ?

- *Conseil d'Etat*: « in the name of » means legally binding
- In 5(5) the distinction between « pour le compte de » / « on behalf of » and « au nom de » / « in the name of » seems to be borrowed from French legal concepts, which may be explained by the history of the drafting of the OECD Model
- Opinion of *Rapporteur public*:
 - 1963 OECD Commentaries confirm that view
 - § 32.1 of later OECD Commentaries do not affect the outcome (later Commentaries + designed to solve specific problem in the UK)
 - Purpose of PE rule: tax the non-resident company in the source country for its own activity in this country

Issue: Why not a factual, economic approach ?

- There is tax planning going on: should courts step in and interpret 5(5) to prevent tax schemes ?
- Legally, does a « economically binding » test make sense ?
- Difficult to find a manageable economic test that would not create great legal uncertainty
 - commissionnaire automatically triggers economic activity by principal? But what of other distribution arrangements ?
 - commissionnaire has no risk because no stock? But in some situations other distributors may not run many risks.
 - in the Zimmer case, the practical elements put forward by the French tax administration were not uncommon for a commissionnaire
- Do not mix the issue of the existence of a PE and the issue of transfer pricing

Issue: Potential recharacterization

- Zimmer decision mentions a potential recharacterization of a commissionnaire agreement as binding the principal, deriving from the express terms of the contract of commission, or from other factual elements relating to the arrangement
- Not necessarily abuse of law
- Back to usual civil law interpretation methods:
 - The title of a contract may be disregarded if the actual provisions do not match
 - A contract may be interpreted using surrounding agreements that clarify its meaning
 - The actual behavior of the parties can reveal the true nature of a contract
- The test remains: is the principal legally bound vis-à-vis the customers ?