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**THE PURCHASE OF PROPERTIES IN FRANCE**

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## INTRODUCTION

Contrary to the situation in some other countries there is no standard solution for the acquisition of property in France. There are many factors to take into account when purchasing a French property, not least how best to structure the purchase and the taxes which are likely to be payable. The most efficient structure should be determined on a case by case basis by taking into account not only the personal circumstances but also the objectives of the purchaser.

## STRUCTURING THE PROPERTY PURCHASE

The conveyancing process will usually be set in motion by a “*notaire*”. The notaire will make a certain number of enquiries, complete the documentation and register the purchase. As a general rule, he will be instructed by both parties of the transaction and he will not expect to advise on how the purchase should be structured to suit the buyer’s individual needs. It is consequently essential for the purchaser to be represented by a lawyer who will represent his interests exclusively.

- **French Succession Law**

The correct structuring of the property purchase is of crucial importance to a non-resident buyer, not least because it will affect how the property will pass on death. Property situated in France is subject to French inheritance law, even if owned by a non-French resident. Here we come across a significant difference between U.S. and French law. Whilst in the United States a person may leave his or her property to whomever he or she wishes by will, French law contains a set of rules (known as “forced heirship” rules) under which fixed percentages of an estate must pass to the person’s children, or if there are no children, to grandchildren, failing which to surviving parents, and so on.

For example, if there are two children, they are entitled to two-thirds of the French property and the owner is only free to dispose of the remaining one-third as he or she wishes (e.g. to a surviving spouse). This can cause problems if the children are less than eighteen, because French property cannot usually be sold, mortgaged or let until the children reach eighteen without the consent of the court and obtaining consent is a slow and expensive process. In addition, children of any previous marriage must also benefit under the forced heirship rules, which can cause difficulties.

Forced heirship rules will apply if a house is purchased jointly by a couple “*en indivision*”, the type of joint ownership which notaires tend to assume will be required. There are, however, several ways to structure the purchase so as to mitigate the forced heirship rules and, for example, postpone children receiving French property. It is advisable to decide how the property purchase should be structured at the outset, as it will sometimes not be possible to change the way it is owned at a later stage. The suitability of each structure will depend upon the personal circumstances of the buyer. Some possible structures are set out below and their suitability outlined for a married couple purchasing a property, but some will also be suitable for purchasers who are unmarried.

- **Purchasing “en tontine”**

If a “tontine” clause is inserted into the French conveyance, on the first death the surviving spouse will receive the whole of the house and the forced heirship rules will not apply at this stage. The effect is therefore similar to “joint tenancy”. On the other hand, this structure is not without its own problems and may not be suitable for high value properties.

- **Change of Matrimonial Regime**

Strange as it sounds, it is possible for a married couple to avoid French inheritance laws by changing their matrimonial regime. A normal U.S. marriage is treated in France as though the couple had adopted the regime known as “*séparation de biens*” (“separate estates”). As a result, any property registered in the name of one spouse belongs to that spouse. A couple who are married under the separate estates regime (provided that they do not have children by a previous relationship) may form a French “community of property” marriage contract (“*communauté universelle*”) in relation to the French property. As a result, when one spouse dies, the French house will pass into the sole ownership of the surviving spouse, free of French inheritance tax.

- **Ownership via a company**

Unlike some other civil law countries, France does split the estate into *movable* and *immovable* properties. When a person dies domiciled for succession purposes outside of France, French inheritance law will only apply to *immovable* property in France (that is, land and buildings). Movable property (such as bank accounts and shares) will be subject to the inheritance law of the country of residence. If a non-resident holds a French property via a company, he or she will own the shares of the company and will be treated as owning *movable* property, which will not be subject to French law and can be left by will outright to a surviving spouse.

Different types of company may be used to own French property, and each will have different tax consequences:

***A non-French company***

It is essential that a French property is not owned via a company situated in a “tax haven”, with which France has no double tax treaty. This is because the French authorities discourage the use of such companies by charging the company a 3% tax each year on the market value of the French property. Ownership by means of a company resident in a country which has a double tax treaty with France will avoid the 3% annual tax (provided that the identity of the ultimate owners of the ownership structure is divulged), but the company will be subject to French corporation tax.

***Société Civile Immobilière (“SCI”)***

The use of a French SCI will avoid the French inheritance rules if the owner is not domiciled in France. In most cases, the SCI will not be subject to the taxes mentioned above for non-French companies (except for the 3% tax). However, the structure is not suitable for properties which are to be let furnished.

- **Ownership via Trusts**

Contrary to popular belief, trusts can be used as a means of avoiding French succession law and French succession taxes. Whilst a French property cannot be directly owned by a trust, the shares of a company owning the property can be held in trust. However, as the concept is alien to French law the use of trusts to hold French assets may give rise to difficulties in tax terms and detailed advice is essential before using a structure that involves a trust.

## **TAX CONSIDERATIONS**

The way in which the property is owned will have tax consequences and it is important that expert advice be obtained in order to ensure that the structure of the property purchase is suitable taking all relevant factors into account.

A non-French resident will not be exempt from French taxes payable in respect of French property. Some of the taxes payable on the purchase, during ownership, when the property is sold and on the death of the owner are outlined below.

- **Taxes payable on the purchase**

Apart from the notaire's fees (which will generally be 2% of the purchase price) and the estate agent's fees, VAT may be payable on the purchase of a property less than 5 years old. Otherwise, transfer duties comprising "*droits d'enregistrement*" and regional taxes will be payable. The total amount varies depending on where the property is situated, but it can be up to 6.5% of the value of the property.

- **Taxes payable during ownership**

Local property taxes will be payable each year.

Wealth tax ("*impôt de solidarité sur la fortune*") is payable on French assets which in total exceed a certain level (currently 720,000 €). The tax is payable on a sliding scale according to the value of the assets, ranging from 0.55 to 1.8%. It may be possible to structure the purchase of a property to reduce this tax.

If the property is rented out, the rent received will be subject to French income tax.

- **Tax payable on a sale of the property**

Capital gains tax will be payable at 1/3 of the net gain on the sale of a French property by a non-resident. For individuals the net gain is calculated by taking the difference between the sale and the index-linked purchase price. There is a special reduction in the tax payable if a property is held for more than 3 years. If it has been owned for 22 years, no capital gains tax will be payable.

- **Tax payable on a gift of the property**

Gift tax will be payable in France when a French property is given away to another person. Gift tax is normally payable at the same rate as French inheritance tax.

However, special rules apply to reduce the tax where the donor is less than 75 years old.

- **Taxes on death**

Inheritance tax will be payable as a general rule on the death of the owner of a property situated in France. Whereas in the USA, inheritance tax is payable by the deceased's estate and a surviving spouse enjoys in most cases complete exemption from inheritance tax, in France tax is payable by the beneficiary and the surviving spouse has an exemption of only 76,000 €. The rate of tax will depend on the degree of blood relationship between the beneficiary and the deceased and can vary from 5% to 40%. For direct family members and between spouses. They increase to 60% when there is no family relationship. Certain ways of structuring the property ownership will mitigate or avoid inheritance tax.

### ***Treaties***

Treaties with individual countries may alter some of these rules. France has concluded approximately 35 estate treaties including one with the United States but not with Canada. It is worth mentioning that the tax treaty between France and the United States is one of the very few which covers not only inheritance tax but also gift tax.

In some cases, tax will be potentially payable by a non-resident on the same property both in France and his or her country of residence (for example income tax on rent, capital gains tax on any gain on the sale and inheritance tax). However, the double tax treaties generally result in credit being given in one country for tax paid in another, so that there will not be a charge to tax in both countries. It is important to seek specialist advice on obtaining relief under the treaties.

### **CONCLUSION**

The acquisition of real estate property in France is attractive to a large number of foreigners. Because of the numerous legal and tax hurdles of making such an investment, many pre-packaged solutions are proposed which unfortunately, prove largely to be at best ineffective, if not dangerous. Potential purchasers should be aware that in the event of challenge to a structure, the French tax authorities are entitled to put a charge on the property until either the tax claimed is paid or the appeal against it is won. However, this does not mean that for the well-advised buyer solutions do not exist, provided that they are tailor made and have sufficient substance.