2012 French supplementary budget: how this may affect non-residents

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Amongst several changes announced by the French Parliament in its supplementary budget, the ones affecting non-residents who have investments and other financial interests in France have generated much interest and Patrick Delas explores the issues surrounding wealth and inheritance taxes among others in the ensuing article.

I. Background

The 2012 supplementary budget (LFR 2012) passed by the French Parliament on August 16, 2012[1] contains substantial changes to the level of taxation applicable to individuals and is expected to raise EUR 7.2 billion in 2012 and EUR 14 billion in 2013.[2]

Amongst various provisions regarding VAT, financial services or the president's and prime minister's own wages, the following is relevant to non-residents owning a second home in France.

Hopefully, the position is now settled from a political perspective and the rules have been set up for the next five years. Uncertainties remain, however, in particular with regard to the submission of non residents to social security contributions and its compatibility with EU law.

II. Wealth tax (ISF)

An "exceptional contribution" will be payable by November 15, 2012.[3]

The contribution will be calculated by reference to the pre-2011 schedule of six bands below (Table I) that will replace in 2013 the current slab system of 0.25 per cent if between EUR 1.3 million and EUR 3 million and 0.50 per cent if above EUR 3 million.

Table I

Net wealth (EUR)	Rate
Not exceeding 800,000	0.00 percent
Between 800,000 and 1,310,000	0.55 percent
Between 1,310,000 and 2,570,000	0.75 percent
Between 2,570,000 and 4,040,000	1.00 percent
Between 4,040,000 and 7,710,000	1.30 percent
Between 7,710,000 and 16,790,000	1.65 percent
Above 16,790,000	1.80 percent

The pre-2011 position is however not entirely restored since the EUR 1.3 million threshold resulting from LFR 2011 is maintained.

For a net worth of EUR 1.5 million, the contribution in addition to the ISF already paid will represent an increase of 12.8 per cent compared to last year.

For a net worth of EUR 3.5 million, the increase will be 23 per cent and for a net worth of EUR 10 million, the increase will be of 125 per cent compared to what was expected at the beginning of this year.

III. Lifetime gifts / Inheritance

The current nil-rate band of EUR 159,325 available per parent and per child every 10 years (i.e. EUR

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637,300 for a couple with two children) is reduced to EUR 100,000 every 15 years (i.e. EUR 400,000 for a couple with two children).[4]

The current nil-rate band of EUR 80,724 on lifetime gifts between spouses/civil partners remains available but the period is here again increased from 10 to 15 years. Spouse/civil partner exemption still applies on death.

Therefore, the position may now be summarised as follows:

A. Relationship: parents and issue

Each child/parent has a EUR 100,000 nil-rate band from each child/parent;

Each grandchild has a EUR 31,865 nil-rate band from each grandparent;

Each great grandchild has a EUR 5,310 nil-rate band from each great grandparent, then as per Table II below:

Table II

Estate	Percent	EUR
Not exceeding 8,072	5	403
Between 8,072 and 12,109	10	403
Between 12,109 and 15,932	15	573
Between 15,932 and 552,324	20	107,278
Between 552,324 and 902,838	30	105,154
Between 902,838 and 1,805,677	40	361,135
Above 1,805,677	45	

B. Relationship: spouses/civil partners (French "PACS" or foreign equivalent)

1. Inheritance tax

The surviving spouse/civil partner benefits from a total exemption of inheritance tax.

2. Lifetime gifts

Each spouse/civil partner has a nil-rate band of EUR 80,724, then as per Table III below

Table III

Estate	Percent	EUR
Not exceeding 8,072	5	403
Between 8,072 and 15,932	10	786
Between 15,932 and 31,865	15	2,389
Between 31,865 and 552,324	20	104,091
Between 552,324 and 902,838	30	105,154
Between 902,838 and 1,805,677	40	361,135
Above 1,805,677	45	

C. Relationship: siblings

Each sibling has a nil-rate band of EUR 15,932, then as per Table IV below:

Table IV

Estate	Percent	EUR
Not exceeding 24,430	35	8,550
Above 24,430	45	

Note: cohabiting siblings may benefit from a total exemption under certain conditions.

D. Relationship: others

Each nephew and niece has a nil-rate band of EUR 7,967. All other beneficiaries have a nil rate band of EUR 1,594, then as per Table V below:

Table V

Relatives to 4th degree	55 percent
Others	60 percent

IV. Social security contributions - CSG/CRDS on income and capital gains

A. The position prior to August 1, 2012

Subject to double tax treaties, non-residents are, in principle, subject to French income tax on the revenue derived from their French situated property (rental income or capital gain).

In addition, French residents have been subjected since the 1990's to a series of social security contributions (*contribution sociale généralisée-CSG, contribution au remboursement de la dette sociale-CRDS, prélèvement social, contribution additionnelle "solidarité autonomie" contribution additionnelle "revenu de solidarité active – RSA"*) representing an additional 15.5 per cent[5].

Traditionally, non-residents covered by their own national insurance scheme were exempted from social security contributions and only subjected to a 19 per cent (EU residents) or 33 1/3 per cent (non-EU residents) tax on capital gains and 20 per cent tax on rental income.

B. The position since August 1, 2012

The socialist government resulting from the general elections of June 2012 regarded this exemption as "unjustified" and LFR 2012 now provides that non-residents should be fully subjected to social security contributions.[6]

This raises the level of taxation of capital gains to 34.5 percent in total for EU residents and 48.83 per cent for non-EU residents.

V. UK position / double tax treaty

The application of particular French double tax treaties on income tax may override a charge to French tax in particular circumstances and needs to be carefully considered.[7]

Under Article 2 of the double tax treaty between France and the United Kingdom of June 19, 2008 (effective from January 1, 2010):

"1. The taxes which are the subject of this Convention are:

. . ..

. . ..

(b) in the case of France, all taxes imposed on behalf of the State or of its local authorities irrespective of the manner in which they are levied on total income, or on elements of income, including taxes on gains from the alienation of movable or immovable prop-

erty, taxes on the total amount of wages or salaries paid by enterprises, as well as taxes on capital appreciation; those taxes are in particular:

(i) the income tax (*l'impôt sur le revenu*);

(ii) the corporation tax (*l'impôt sur les sociétés*);

(iii) the social contribution on corporation tax (*la contribution sociale sur l'impôt sur les sociétés*);

(iv) the tax on salaries (*la taxe sur les salaires*);

(v) the "*contributions sociales généralisées*";

(vi) the "*contributions pour le remboursement de la dette sociale*";

(hereinafter referred to as "French tax")."

Under Article 14 of the treaty:

"1. Gains derived from the alienation of immovable property referred to in Article 6 and situated in a Contracting State may be taxed in that State.

2. Gains derived from the alienation of:

(a) shares, other than those regularly traded on an approved Stock Exchange, or rights deriving their value or the greater part of their value directly or indirectly from immovable property referred to in Article 6 and situated in a Contracting State;

. . ..

. . . .

May be taxed in the State in which the immovable property is situated."

Whereas Article 24 provides that:

"1. Subject to the provisions of the law of the United Kingdom regarding the allowance as a credit against United Kingdom tax of tax payable in a territory outside the United Kingdom (which shall not affect the principle hereof):

a) French tax payable under the laws of France and in accordance with this convention, whether directly or by deduction, on profits, income or chargeable gains from sources within France (excluding in the case of a dividend, tax payable in respect of the profits out of which the dividend is paid) shall be allowed as a credit against any United Kingdom tax computed by reference to the same on profits, income or chargeable gains by reference to which French tax is computed;"

However,

"2. For the purposes of paragraph 1:

c) the taxes referred to in clauses (i) to (iv) of sub-paragraph (b) of paragraph 1 of Article 2 and, in respect of the taxes mentioned in those clauses, in paragraph 2 of Article 2, shall be considered French tax.".

Therefore, as under most double tax treaties, France retains the right to apply tax to the sale of French situated property under its own domestic rules. If taxation also applies under UK domestic rules (i.e. the vendor is UK domiciled and resident), double taxation is avoided on the basis of a credit available in the United Kingdom. However, only taxes referred to in clauses (i) to (iv) of sub-paragraph (b) of paragraph 1 of Article 2 are regarded as "French taxes" which excludes CSG/CRDS.

Until 2012, since in most cases taxation in the United Kingdom was at a higher rate than in France (28 per cent against 19 per cent) French capital gains tax even as increased by LFR 2011 was of limited impact.

The situation is now different since LFR 2012 where 15.5 per cent payable in France cannot be claimed against any tax in the UK possibly resulting in a double taxation (28 CGT in UK + 15.5 CSG/CRDS in France = 43.5 per cent total).

VI. Constitutionality / Compatibility with EU Law

The various social security contributions were progressively introduced since the 1990s in order to reduce the deficit France's *sécurité sociale* which, until then, was exclusively funded by contributions on wages and self employed profits. Their legal nature (tax or social security charge) has never ceased to be debated.

The issue went as far as the European Court of Justice on two occasions. The ECJ initially ruled in the case of *Commission of the European Communities v France*, February 15, 2000[8] that with regard to its purpose (namely funding a national insurance scheme), the CSG/CRDS should be regarded as a social security contribution and not as a tax. However, the position was apparently overruled by *Philippe Derouin v Urssaf Paris, 3 April 2008*[9] which implies that the CSG/CRDS is actually a tax subject to double tax treaties. The ECJ position is however not exactly clear.

In any event, by the decision 2012-654 DC of August 9, 2012, the *Conseil Constitutionnel* has approved the provisions of LFR 2012 in this respect but interestingly, comments that it is not competent to judge the compliance of this with EU regulations and international treaties, but only with the Constitution of France. In other words, the *Conseil* says that it is for the taxpayers to take it to the ordinary courts if they wish to challenge the provision.

Conclusion

France has been through a turbulent political and tax period and the ambition of LFR 2012 is to end up with the Sarkozy period and set up the rules for the next five years. Uncertainties remain however and matters may not be as settled as they seem.

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NOTES

[1] Loi n° 2012-958 of 16 août 2012 de finances rectificative pour 2012

[2] http://www.assemblee-nationale.fr/14/projets/pl0071.asp

[3] Art 4 LFR 2012

[4] Art. 5 of LFR 2012

[5] Since July 1, 2012

[6] Art. 29 of LFR 2012

[7] French tax treaties are available at: http://www.impots.gouv.fr.

[8] C-169/98 and C 34/98

[9] C-103/06