



Recent developments on French Capital gains tax on the sale of French Real Estate

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On 7 September 2011 the French Assembly adopted a new proposal from the French Government regarding the reform of French capital gains tax ("CGT") in respect of secondary residences. The CGT rates would not change but the way capital gains are computed would be profoundly modified.

Regarding the CGT rates, we are familiar with the benefits of the "Biso" case to certain foreigners living in Monaco who can escape taxation under Article 164 C of the French Tax Code (income tax on three times the letting value of any property available in France) by invoking the non discrimination provisions contained in a Double Tax Treaty signed between France and the country of their citizenship. We will see that these principles can also apply in respect of French CGT.

1/ New proposed Capital gains tax regime

Currently, the taxable gain is reduced by 10% for each year of ownership after the fifth year, so that the gain is totally exempt after 15 years of ownership. Under the proposed new law, the reduction would apply as follows: 2% per year between 6 and 16 years (10 years = 20%); 4% per year between 17 and 24 years (8 years = 32%) and 8% between 25 and 30 years (6 years = 48%) so that the gain is totally exempt after a lengthy period of 30 years of ownership.

The very good news is that the new law will apply to sales completed as of 1 February 2012 (and not 25 August 2011 as initially proposed). We can

expect that a lot of properties will come on to the market fairly quickly to capture the old regime therefore.

However, to avoid tax planning strategies being implemented prior to the introduction of these new rules, the new law will apply as of 25 August 2011 in certain cases of family ownership restructurings. In this respect, and interestingly, the new law only refers to contributions of properties or rights over properties to a company and not strictly speaking to a mere sale of a property or rights to a company. If the intention is only to avoid contributions, **this drafting would open the door to the possibility of other forms of restructuring before 1 February 2012 to benefit from the current exemption and purge latent capital gains.**

To become law the text must now be approved by the French Senate. Further developments will follow...

2/ Non discrimination provisions and application of the reduced French Capital gains tax

Non French tax residents are subject to French CGT on the sale of French real estate at different rates depending on where they are resident:

- 19% if they are resident in an EU State or Iceland, Norway and Liechtenstein (the rate of 19% applies as of 1 January 2011, previously the rate was 16%). Although Switzerland is not an EU State, in a case dated 20 May 2010, the Paris Court of Appeal held that Swiss residents should

benefit from the 19% rate. However, this is only due to a particular provision contained in the Double Tax Treaty signed between France and Switzerland;

- 33.33% if they are resident in a country other than those mentioned above;
- 50% if they are resident in a country seen by France as an "uncooperative State or territory".

Monaco is not an EU State and is not considered as an "uncooperative State or territory". Residents of Monaco are therefore prima facie subject to the rate of 33.33% on any capital gains made on the sale of French real estate, unless the "Biso" case principles can apply to them. The "Biso" case does not provide an argument under European law (see further developments below) but rather by an extension of application of non discrimination provisions contained in certain Double Tax Treaties signed by France.

How we can help

Under the "Biso" case principles, certain nationals living in Monaco (except French and Monegasque nationals) can invoke the non-discrimination provisions provided by the Double Tax Treaty signed by France with the country of their citizenship to claim the reduced rate of CGT if they have already paid the higher rate on a past sale. We say "certain" because not all the foreigners living in Monaco are able to invoke an appropriate Double Tax Treaty (ie a "good" Double Tax Treaty for these purposes).

Residents of Monaco who sold French property in the past (not before 1 January 2009 if CGT was paid before this date) and paid CGT at the higher rate of 33.33% and who, unbeknown to them at the time, were in the position to benefit from the reduced rate by application of the relevant Double Tax Treaty, might still be able to make a claim to the French tax authorities to ask for a refund of the extra CGT paid, plus payment of interest.

We can assist with the preparation of the claim to the French Tax Authorities. However, before doing so, please note that an analysis of the Double Tax Treaty applicable is required first to determine whether or not non discrimination provisions can apply. The nationality of the Monegasque resident taxpayer becomes a crucial element.

In respect of French CGT, a claim can be made up to 31 December of the second year following the tax year during which the CGT was paid. For instance, we have until 31 December 2011 to make claims in respect of CGT paid during the 2009 tax year (ie in respect of sales occurring during 2009). In France, the tax year is the calendar year. As of 1 January 2012 no claim for a refund would be possible in respect of 2009.

Having said this, and for future sales, foreigners in Monaco who can invoke an appropriate Double Tax Treaty are also in a position to benefit from the reduced CGT rate when the sale occurs, provided that they can convince the Notary (if any) and more importantly, the fiscal representative to apply the reduced rate. In such a case no subsequent claim needs to be made. We can also advise and assist during the sale process to ensure that the seller pays the right CGT rate at the outset.

Future developments under European law...

In three recent cases dated 25 February 2011, the Tribunal of Montreuil opened the door to further tax benefits regarding the application of the reduced CGT rate to non EU residents. In these cases, the Tribunal considered that the difference in tax treatment (CGT rates) between residents of an EU State and non residents of an EU State was discriminatory and constituted a restriction on the freedom of movement of capital under European Law. The Tribunal agreed to apply the lower CGT rate to residents outside the EU regardless of the nationality of the taxpayers so that these principles would apply even to a non EU citizen.

The importance we can attribute to these decisions is relatively small however given that these are lower Court decisions that have been appealed by the French Tax Authorities. However, should they be confirmed by the Court of Appeal and subsequently by the Supreme Court they would then open other wider perspectives for any nationals resident outside the EU including residents of Monaco who cannot currently benefit from the "Biso" case argument and a "good" Double Tax Treaty.

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These notes are for general information only and are not intended to provide legal advice.