

French taxation of pension fund lump sum payments

There has been no small amount of publicity about a recent change in French law which came into force on 1st January 2011 and on the face of it makes the previously tax free lump sum paid out by UK pensions wholly taxable in the hands of French residents. This means that people who have contributed to a UK pension fund would be heavily penalized if they moved to France before taking the lump sum.

In fact this is unlikely to be the case because of the provisions in the UK – France Tax Treaty which has been overlooked by many of the advisors and commentators.

French domestic law

Article 59 of the French Law of 29th December 2010, modified Article 79 of the French Tax Code to include as income taxable in France retirement payments made in the form of capital. Under French domestic law capital pension payments received by French residents from UK pension funds are clearly taxable even though not taxed in the UK.

Definition of a “pension” in the tax treaty

However things are not that simple. Article 18 of the UK – France tax treaty provides that pensions and similar remuneration paid to a French resident “in consideration of past employment” is taxable in France. This covers payments into a pension fund made by an employer but probably cannot cover employee contributions because there is no payment in respect of past consideration. The employee pays his own money in. It definitely cannot cover contributions made to a free standing scheme by a typically self employed person because he is not making the payment in consideration of past employment.

If not “pension” income – must be other income within UK – France tax treaty

This means you have to look at Article 23 of the treaty because the deemed lump sum income does not fit in anywhere else. This provides that any income which is not covered elsewhere in the treaty is taxed where the recipient is resident i.e. France but Article 23 expressly excludes income from trusts. Almost every pension fund is a trust. The wording of Article 23 could be interpreted as (1) the trust income is completely outside the treaty – very unlikely as the treaty is meant to be comprehensive (2) trust income can be taxed in both the UK and France – unlikely as why would it be excluded from French taxation exclusively (3) trust income not taxed in France – could be taxed in UK but in practice is not – this is the likely outcome.

Likely tax position

The likely legal position is that you have to ascertain whether the pension is an employer funded one or a private one. If employer funded then the lump sum needs to be divided into money from employers contributions, which is taxable in France, and the part from employees contributions which is not taxable because of the UK France Tax treaty.

If the pension is free standing and is not provided by an employer then it is not taxable in France because of Article 23 of the treaty. Similar considerations will apply to offshore pensions. The French Tax authority needs to be contacted urgently for a statement on how the UK France treaty will be applied.

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