

## Using an SCI to avoid French Capital Gains Tax

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*Please note that international tax law is a complex subject and you should not rely on this article without professional advice on the facts of your case*

### **Introduction**

This article discusses a simple yet little known way of avoiding French capital gains tax on property sales. It applies whether or not you are a French resident. It is based on selling the shares in an SCI which have been owned for at least 15 years, rather than the property, regardless of how long the property has been owned.

Our view is that it may be better tax wise for investors to keep their SCI after a property sale and reuse it for other purchases. This is contrary to the commonly dispensed advice from notaires and accountants always to create a new SCI for each property venture.

### **French Capital gains tax**

France taxes capital gains in a different manner to the UK. Rather than basing the scope of the charge purely on residency, any individual or company who invests in French land is potentially within the charge to French CGT under French internal law. Most double tax treaties will give France the right to charge this tax.

It is important to note that companies whose assets are more than 50% French land are generally treated for French CGT purposes as French property companies. The shares in these companies are consequently treated as real estate in France and the sale of such shares is within French capital gains tax.

The rates of French CGT on property (including shares in property companies) sold by individuals is as follows:

- 19% for those in the EU, Iceland, Norway or Switzerland;
- 33 1/3% for individuals outside the countries mentioned above but not resident in black-listed countries; and
- 50% for individuals in 'black-listed' (i.e. tax haven) countries.

Where the property is owned by an individual taper relief applies. After 5 years, the gain is tapered by 10% per annum of holding, so no CGT is payable after 15 years of ownership.

### **SCIs**

There are companies which exist under French law specifically to own real estate. These are known as *Sociétés Civiles Immobilières* ("SCI"). So long as the SCI does not carry out any commercial activity (including rental of furnished property), it

remains tax transparent for income and capital gains tax. Therefore the shareholders are taxed in France on the underlying income and gains of the company.

When it comes to disposals, generally the SCI will sell the underlying property to the buyer although it is not uncommon for a sale of the shares to take place. As the companies are simple holding (non trading) structures, not requiring any annual filing, buyers do not need to conduct significant due diligence when purchasing such companies. Often non-resident buyers will be keen to purchase in this way as they can avoid issues of French forced heirship but can also avoid the costs of incorporating a company to do so. There is also the benefit that the transfer costs can be lower when a SCI is transferred and it is possible for such a transfer to take place without the involvement of a *notaire*.

The running of an SCI is straightforward as there are no annual filing requirements and anyone can act as the *gerant*. This means that an SCI can be maintained with little or no ongoing costs. It is also possible to set up SCIs in other jurisdictions including Monaco and Luxembourg which can take advantage of the same tax planning.

### **Tax Planning**

Because the SCI is treated as tax transparent, when it comes to sell its underlying property asset, it is the shareholders who are taxable on the gain. These individuals are able to take advantage of the taper relief provisions so that, if the SCI has owned the property for 15 years there will be no French capital gains tax due on the disposal.

The SCI is entitled to own other property and can be used again to own property in the future. If the SCI disposes of a property and acquires another property, there is a little known loophole which exists for the owners. If they have owned the shares in the SCI for 15 years they can again take advantage of the taper relief provisions mentioned above if they subsequently sell the shares in the SCI as the SCI shares are treated in the same way as a property in France. It would not matter if the SCI had not owned the underlying property at that time for the full 15 years. Of course on such a second sale if the property has not been owned for at least 15 years a share sale would be the only way to obtain a capital gains tax exemption.

### **As an example:**

Mr and Mrs X purchase a French property in 1995 creating a SCI to hold the property. In 2011 the SCI sells this first property and acquires a new property from the sale proceeds. No French capital gains tax is charged due to the property having been owned for 15 years. In 2013, Mr and Mrs X decide they want to sell the second property but they carry out the transfer by way of a share sale of the SCI. Again there is no French capital gains tax as the shares have been owned for at least 15 years (even though the property has only been owned for 2 years).

### **Possible line of attack**

Care will need to be taken in these circumstances as regular selling of property or of SCI shares runs the risk of you being classed as a 'property trader' in France. Your

capital gains are then chargeable to income tax at higher rates. To avoid this eventuality it is sensible to not make more than one sale per year. Ideally a number of years should pass between sales.

However it is clear that if you have purchased a property in France via a SCI it would be sensible to keep that SCI in place after the property has been sold on. This leaves you with the option of taking advantage of the above loophole and has little downside given that there are no costs of maintaining an SCI.

### **Going further**

More adventurous investors may wish to explore the possibilities further here including the use of shareholders of SCI's which have had the same shareholders for over 15 years. In general France will tax the legal owner of the shares (i.e. the person shown on the SCI's documentation as the shareholder) and so buyers may be able to benefit from simply acquiring the beneficial (rather than the legal) ownership of the SCI shares and then using the SCI as a vehicle for a new acquisition. Assuming the legal owner has owned the SCI shares for at least 15 years they are outside the charge to capital gains tax on a sale of the shares.

### **Our views**

There is no definitive view in France of tax transparent entities based in other countries such as limited liability partnerships in the UK.

In any case investors will also need to consider the position in their country of residency and in particular the UK where you are taxable on your worldwide gains. The position is also clouded in the UK by the fact that HMRC consider an SCI to be an opaque (i.e. non transparent) entity for tax purposes. However if the legal registered owners of the SCI declare that they are holding them on trust for the beneficiaries this may solve the problem. The structure is also helpful for non-domiciled people resident in the UK who should be able to avoid all taxation in this way so long as the net proceeds are not remitted to the UK.

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