

Mitigating capital gains tax - buying and selling French property through a foreign company

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The author explores investments in properties in France through efficient tax structures within the provisions of double tax treaties in the European Economic Area aimed at mitigating capital gains exposures of investors.

I. Introduction

As a general rule, when individuals sell property in France, they are liable for French capital gains tax on the gain regardless of their residency, albeit at different rates. French residents are subject to a fixed rate of 19 per cent tax on the gain plus social charges of 12.3 per cent. Non-residents pay tax at 19 per cent if they are resident in the EU, Iceland, Norway or Switzerland or $33\frac{1}{3}$ per cent if resident elsewhere, with no social charges to pay. Residents of 'black-listed' countries are charged at 50 per cent tax.

Individuals may be exempt from capital gains tax if the property sold is their main residence or if they have owned the property for 15 years or more. However, from an investor's point of view, owning a French property for 15 years to avoid capital gains tax will probably not be an attractive option.

In general, companies not resident in France are also liable to French tax at the rate of $33\frac{1}{3}$ per cent on the gains made on properties located in France. However, certain structures can be used within the provisions of double tax treaties which may assist investors to mitigate their capital gains tax exposures. This ar-

ticle explores some of these structures, and in particular, prospects of owning French property through a foreign company.

II. Buying and selling French property through an offshore company

Historically, France has had a number of double tax treaties which have allowed planning to mitigate capital gains tax liabilities. Some of its double tax treaties contain provisions that a company is only taxable in the country where it is resident, i.e. the country where it operates, or where its place of effective management is located and has its registered office. Whilst these treaties also contain provisions which stated that the profits from immovable property are taxable in the country where the property is located, older treaties took precedence to the provision which stated that the company was taxable in its country of residence. Consequently, if a non French resident company sold properties in France, the profit made by the company would be subject to tax only in the jurisdiction where the company is situated.

In order to make the most of such a structure one needs to set up the company in a low capital gains tax

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jurisdiction. More profitably, you could set up the company in a jurisdiction where the domestic law stipulates that the gains made on the disposal of a property situated abroad are only taxable in the country where the property is situated. This should result in no capital gains tax being payable anywhere.

By way of an example, Danish companies were often used for purchasing French properties because the Denmark-France double tax treaty contained a provision that the gains made by a Danish company were taxable only in Denmark. Danish domestic law provided that gains made on the disposal of immovable property were taxable in the country where the property was situated. As a result the Danish company was able to avoid capital gains tax entirely on the sale of its French properties. Many investors took advantage of the Danish company route until the France-Denmark treaty was revoked. Similarly, UK companies were also used in such structures until the UK-France treaty was replaced in 2010.

III. Points to consider

There are a few French tax treaties with some countries that remain in force having similar impact as above. Investors could take advantage of these double tax treaties when putting in place structures to mitigate their capital gains tax exposure. However, there are certain points which an investor should consider when contemplating such a structure.

Firstly, the company set up in the chosen jurisdiction must be a genuine vehicle in that jurisdiction. This means that the directors of the company must be local and must be resident in that country. Accordingly, one will need to trust the directors as they will ultimately have extensive power to deal with the assets of the company. One will also need to ensure that the company's place of effective management remains in that country. If the company is managed in another country, it can be treated as a resident in the other country under the terms of the treaty making it taxable in that country on all profits.

Domestic company laws will also need to be complied with and are likely to include preparing and filing company accounts. Whilst setting up a foreign company is relatively easy, the costs of running it as a genuine vehicle may be high. It is for this reason that

such structures are reserved for high net wealth individuals and high value properties.

Another point which an investor ought to consider while contemplating such a structure is the political stability of the country in which the company is proposed to be set up. Furthermore, there are certain jurisdictions which have stringent control over repatriation of funds, which ultimately mean the shareholders could have trouble accessing their money. Other tax consequences for the individual shareholders will also need to be considered in their relevant resident countries.

IV. Suitable jurisdiction

There are several jurisdictions with very helpful double tax treaties with France which have similar provisions to the former Danish and UK treaties exempting the gains from French taxation. These jurisdictions have low domestic corporation tax and as such are fiscally attractive to individuals making speculative purchases in France with a view to an early resale. There has for some years been a well established jurisdiction which has and continues to be used by sophisticated investors. It has had a history of instability though is currently stable. There is however also another jurisdiction, which has received no publicity, is politically stable and has a low rate of corporation tax. All the required professional services are readily available in this jurisdiction and it has a good banking system. This jurisdiction is likely to appeal in particular to Russian speculative buyers.

V. Summary

Whilst there may be several advantages of owning properties through an offshore company, they may also be some pitfalls. Careful consideration of the individual circumstances is necessary as well as consideration of the individual's future aims.

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