

Buying a house in France

Essential points for first time buyers of French residential property and their advisers



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Introduction

Realising the dream of owning a second home in France is, in essence, no more or less difficult than buying in England. Freedom of mobility and movement of capital around Europe now mean that there is no obstacle to Britons buying holiday flats and substantial secondary houses in France, our nearest and biggest neighbour.

But the thoughtful buyer will look before he leaps. He will reflect on the fact that France is a civil law country whose laws on taxation and succession, in particular, are entirely foreign to him. He will realise that he could make some costly mistakes through failure to take proper advice before he commits himself.

This Dixon Wilson update, prepared by our Paris office, aims to serve as an aide-mémoire to the essential French issues that need to be addressed by a typical UK resident buyer.

Who shall own the property?

As a rule, personal ownership of a second home in France is to be preferred to ownership by a company, be it a French or a foreign one, or by trustees. This is because the French tax system intentionally discriminates against the long term holding of property, either anonymously or in such a way as to circumvent death duties once in each generation. Succession planning needs to be thought about at the outset, as splitting ownership of a property or giving it away to children later on is certain to incur capital taxation which could otherwise have been avoided.

The French way

A vehicle with no equivalent in English law, the société civile immobilière, or civil property company, provides a convenient means whereby several people, be they members of the immediate family or not, may own a house in precise shares. The so-called "SCI" is not a taxpaying company, but is more akin to a partnership. It is easily set up. Although it has minimal compulsory annual compliance burdens these must be carefully adhered to in order to avoid the possibility of the company's being regarded as a sham by the tax authorities. For all practical purposes, when viewed from the perspective of an English resident in France, the SCI is treated in the same way as if the house were in the buyer's own name. Moreover, it will allow the property to pass in accordance with his English will, rather than under the French rules of compulsory succession.

Draft UK legislation, still to be enacted, was published following the 2007 Budget the purpose of which is to remove the possibility of an income tax charge on a benefit in kind arising from the use of overseas homes owned through companies.

You need to be aware of the possibility of splitting the ownership of your house into two interests: the "usufruit" and the "nue-propriété". These, respectively, mean the right to enjoy or occupy the property, and the bare ownership or legal title. An election for "community of assets", a particular type of marriage contract was, until the Sarkozy reforms of August 2007, a means of eliminating taxation on the first of a couple to die. The new law has, however, exempted from French death duties transfers between spouses and Pacs'd couples. A tontine clause may be inserted in the deed of conveyance to create an equivalent to a UK joint tenancy. This will allow the property to pass wholly into the estate of the survivor and bypass potential claims under French forced heirship rules.

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The rôle of the notary

Having identified your house or château, probably through an estate agent, your next port of call will be the notary. The notary's function is to transfer title to the property and handle the receipts and payments of money. All notaries in France, wherever they are physically located, have equal standing. The notary's fees are fixed nationally by law and there is no price competition between them. It is common for buyer and seller to use the same notary for smaller transactions. Having your own notary, however, gives you more chance of receiving useful advice directed at your personal circumstances. There is no additional cost to you as the two notaries will share a single fee. Note, however, that tax planning is not the notary's central concern or duty and you should seek separate advice on tax issues.

The purchase transaction

A sale proceeds in two phases. In the typical case the *compromis de vente* (an undertaking to buy and to sell) binds both parties to the deal, subject to proof of title, to conditional clauses based on the outcome of structural surveys, town planning searches and the like and to a seven day cooling off period in certain circumstances. It is important to ensure that your own "worry points" are built in when this document is being drawn up by your notary. It will be too late once you have signed it and paid over your deposit, usually 10%.

The signed *compromis* allows you, the buyer, to insist upon completion of the sale even if the seller changes his mind. It prevents gazumping. Conversely, it allows the seller to claim your deposit in the event that you decide to pull out for reasons other than those mentioned in the conditional clauses.

Once the searches are complete, you and the seller will meet at the notary's office to pay the balance of the purchase price and then sign the *acte de vente* (sale deed) by which the house becomes legally yours. Notice that at both points in the process, *compromis* and *acte de vente*, it is open to you to appoint a local person, usually one of the notary's clerks, to sign on your behalf if this suits your travel plans better.

Typically, the interval between initial signing and completion of a deal will be around eight weeks, but you may agree upon a longer period.

As soon as the final sale deed is signed you are responsible for insuring the property.

Agent's commission and registration duty

The price of the house usually, but not invariably, includes the estate agent's commission and this will be paid over to him by the notary. You, the buyer, will have to pay registration duties totalling 5.09% of the price plus notarial fees and taxes, bringing the total up to some 7%. If it is either a new house, or less than five years old, or a substantially restored old house, then VAT at 19.6% is payable and not registration duty. The VAT is included in the asking price of the property and is not an additional cost to you, the buyer. Buyer's costs on a new property will come to some 2% of the price.

Wealth tax

Non-French resident individuals must pay wealth tax if the combined French assets of husband and wife exceed €770,000 on 1 January each year. Loans secured on the property are deductible in computing the taxable value. It is up to you to declare your wealth and pay the tax rather than wait to be discovered. The taxman has up to six years to require returns in the event that none have been made. Penalties and interest will be in point in such cases, at rates high enough to make the paying of the tax on time much the cheapest option. Your wealth tax valuations will be reviewed by the French tax authorities as a matter of routine at the time of a subsequent disposal of the property - and uplifts made where appropriate.

The wealth tax bands as at 1 January 2008 are as follows :

Taxable amount	Rate %
€0 - 770,000	0
€770,000 - 1,240,000	0.55
€1,240,000 - 2,450,000	0.75
€2,450,000 - 3,850,000	1.00
€3,850,000 - 7,360,000	1.30
€7,360,000 - 16,020,000	1.65
Excess	1.80

These wealth tax bands are increased annually in line with inflation.

Local taxes

Two local taxes are payable on French houses: the *taxes foncières*, levied on the owner and the *taxe d'habitation*, payable by the occupier. These are the equivalent of Council Tax. The local tax office will send these out with no action required from you.

Income tax on non-residents

Non-French residents pay income tax only on their French source income, such as holiday lets. For furnished lettings, you receive a flat rate deduction of 71% in lieu of expenses and, as a non resident, pay tax at a minimum rate of 20% on the balance. Alternatively, you can opt to prepare full accounts and thereby create a loss for offset against future income. The expenses deductible include all normal business-related expenditure and depreciation on the initial cost of the building (but not the land element) and on subsequent capital expenditure. Accountancy costs will be minimised by opting for the flat rate deduction method, although this cannot give rise to a loss.

Capital gains tax

Citizens of the European Union who sell their French houses at a profit are liable to capital gains tax at 16%. (Unless they are trading in property, in which case full business tax rules apply). Non-EU citizens are taxed at 33 1/3 %. You may have to appoint a tax guarantor in France for CGT purposes. Current or past residents of France will be eligible for the main residence exemption, similar to that in the UK provided they own the property in their own names, i.e. not through an SCI.

Property gains made by individuals are reduced by 10% per year after the first five years of ownership, giving 100% exemption after 15 years. Even though a gain on sale has been reported in France, and French tax paid, the gain will still be assessable in the UK, computed according to UK rules, if you are a UK tax resident.

Capital gains made on properties owned through limited liability companies (i.e. not SCIs), are taxed much more heavily. This is because the system of exemption after 15 years' ownership does not apply to companies. In addition, the base cost of the house (but not of the land) is reduced by 2% per annum of ownership by a company (because a trading company would normally be claiming this as deductible depreciation each year). For these reasons we discourage the use of limited companies for private property ownership.

The tax at 3% on property companies

A tax which has no direct equivalent in the English system exists so as to discourage the use of tax haven companies as ownership vehicles. All companies, French or foreign, unless they can (and do) claim exemption under one of the specific heads available, are *prima facie* liable to pay a tax equal to 3% of the market value of the property at 1 January each year. Loans, whether or not charged on the property, are not deductible for this purpose. Companies incorporated in countries which have concluded double taxation treaties with France (e.g. Great Britain) can claim exemption by declaring the identities of their shareholders. This then passes the structure into the wealth tax and succession duty regime. Tax haven companies, with no treaty protection, are not eligible for exemption from the 3% tax even if they are willing to declare the identities of their shareholders.

A recent case brought before the European Court of Justice called into question France's right to require EU incorporated companies to meet stricter disclosure criteria than French companies when filing for exemption from 3% tax. The French authorities have responded by harmonising the disclosure requirements for all eligible companies.

If our clients have any French properties still owned by such tax haven entities, we recommend unscrambling the ownership as soon as possible. Although the coast may appear to be clear, in fact penalties and interest will be accruing on a daily basis (unless, of course, the 3% tax has been regularly paid each year).

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Death: the need for a will dealing with your French assets

If you die domiciled in England (note that this is different from merely resident in the country) then French death duty will be payable only on your French house and contents, after deducting loans secured on it. The tax payable will depend on how many children you have. The respective rights of children and spouses over the property and its eventual sale proceeds will be a matter of French law and you do not have the same freedom to dispose by your will as you do in England. It is nevertheless desirable to make a will, or a codicil to your existing English will, in respect of your French moveable and immoveable assets as soon as you become the owner of the property. If you make a French will, you should check with your solicitor that it does not revoke your English will and vice versa.

One recognised way of avoiding French forced heirship rules on the first to die of a husband and wife is for the couple to elect jointly for the French marital regime of "community of property". The election for community of property can be made at any time and must be done through a notary. The effect is that on the first death all the property subject to the community (i.e. the house in France) is deemed to belong to the surviving spouse. No tax is payable at that stage by virtue of the exemption for transfers between spouses. However, it is not binding upon children from previous marriages, who can claim their share of the property under the forced heirship rules. Very often the house will have been sold before the second death occurs and the proceeds repatriated to England, thereby avoiding French succession duty on the second death as well.

Two important caveats need to be made where the property has been bought with a usufruct in favour of a parent. Firstly, tax on the death of the parent will only be avoided if it can be demonstrated that the bare owners (normally the children), bought their interests using funds other than gifts from their parents. This needs to be documented at the time of purchase, which may be many years before the death of the parent occurs. Secondly, some UK inspectors of taxes are known to treat a French usufruct as similar in tax terms to an English life interest. The implication is that, even if French tax is avoided on the death of the parent, English inheritance tax may still be in point.

Current rates of succession duty are as follows:

Taxable amounts To direct descendants	Rate %
€0 - 7,699	5
€7,699 - 11,548	10
€11,548 - 15,195	15
€15,195 - 526,762	20
€526,762 - 861,053	30
€861,053 - 1,722,105	35
Excess	40

Other tax rates apply in the following circumstances:

Between married couples and partners under Pacs (French civil partnership) Exempt

Between siblings

0 - €23,299	35%
Excess	45%

Between non-family members

Remoter relatives	55-60%
Third parties	60%

The above rates apply to each of the inheritors after deducting exempt bands as follows:

Children/parents (each)	€151,950
Siblings (each)	fully exempt

but only if single, five years cohabitation with the deceased and sibling over 50;

otherwise	€15,195
Other (each)	€1,520

This update is for information only and does not constitute professional advice. For advice on your particular circumstances or for further information, advice or assistance in relation to any matters raised above, please contact the author James Howes or your usual Dixon Wilson partner.

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