



FEATURE: INTERNATIONAL PRACTICE

By **G. Warren Whitaker, Jean-Philippe Mabru** & **Matthew J. Woodbury**

French Tax Laws Affecting U.S. Citizens And Trusts

Recent amendments provide some clarification

France doesn't have trust laws; a trust can't be created under French law. However, French residents, including U.S. citizens residing in France, may create trusts under U.S. law or be beneficiaries of U.S. trusts. At one time, it was unclear how France would tax its residents who were settlors or beneficiaries of trusts. As of 2011, it became all too clear. Recent amendments have further clarified the negative treatment of trusts.

The French law enacted on July 29, 2011 affects trusts in any jurisdiction if: the settlor is French, any beneficiary is French or any trust assets are located in France (other than listed securities).

The cornerstone of this new tax system for trusts is reporting by the trustee of the existence of a trust subject to the law to the French tax authorities. This reporting is onerous, as described below, and is in itself a reason to consider terminating trusts that have French settlors or beneficiaries or excluding the French beneficiaries.

Subject trusts are those with: (1) at least one settlor, beneficiary treated as a settlor under French law (a deemed settlor-beneficiary) or beneficiary with a French fiscal domicile (citizenship is irrelevant), or (2) at least one piece of property or one right situated in France (other than French securities listed on a national exchange).

A report must be made to the French tax authorities

in the case of the creation, modification or termination (a reporting event) of a subject trust. The report is due within one month of the reporting event. A modification includes every distribution of principal or accumulated income from the trust. In addition, a similar yearly report must be made.

There's a flat fine of €20,000 for any failure to file a required report.

Contents of the Trustee's Report

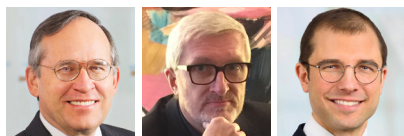
In the month following the creation, modification or termination of a trust, the trustee must make a declaration to the French Tax Service for Foreign Businesses.¹

Modification of a trust includes every change in: (1) the terms of the trust, (2) its functioning, (3) its settlors or beneficiaries deemed settlors, (4) beneficiaries, (5) trustees and administrators, (6) the death of any of the foregoing, (7) any transfer to or from the trust of property or rights, (8) any transfer or attribution of property, rights or income of the trust, and (9) generally any modification of any right or fact that could impact the economics or the functioning of the trust.²

The declaration must contain:

1. The identity of each settlor and deemed settlor-beneficiary, including name or company name, address and, as applicable, date and place of birth and, if deceased, of death.
2. The identity of each beneficiary, including name or company name, address and, as applicable, date and place of birth and, if deceased, of death.
3. The identity of the trustee of the trust, including name or company name and address.
4. The identity of the trust, including name and address.
5. The terms of the trust, including the terms of the instrument of trust and any other documents affecting governance of the trust, including, in

Left to right: **G. Warren Whitaker** is a partner at Day Pitney LLP in New York City, **Jean-Philippe Mabru** is the managing partner at Bonnard Lawson in Paris and **Matthew**



J. Woodbury is an associate at Day Pitney LLP in Boston



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particular, whether the trust is revocable or irrevocable, whether, how and to what extent it's discretionary and the rules governing beneficial ownership of the trust's assets, rights and income.

6. A description of the reporting event.
7. As applicable, a description of the trust assets and rights, including their value as of the date of the reporting event, and of any property, rights and income that were transferred, which vested (was attributed to a person) or which were distributed from the trust by reason of the reporting event.
8. For each piece of property and each right held in trust and mentioned in the declaration, the name or company name, address and, as applicable, the date and place of birth and, if deceased, of death of each person who placed the property or right in trust.

A U.S. citizen who becomes a resident of France is exempt from the IFI, except on French assets, for the first five years of residence.

9. For the property, rights and income transferred, vested (attributed) or distributed from the trust and constituting the reporting event, the name or company name, address and, as applicable, the date and place of birth and, if deceased, of death of each person to whom the property, rights and income were transmitted, attributed or distributed.

French fiscal domicile (that is, tax residency) for purposes of these reports is determined as of Jan. 1 of each year.

A form is available for trustees to use for declarations made by reason of a reporting event but it isn't mandatory. The report may be made in any form.³

The Trustee's Annual Report

The trustee or administrator must make an annual declaration by June 15 of each year to the French Tax Service for Foreign Businesses containing:

1. The first five pieces of information included in the declaration for a reporting event (as noted in the previous subsection), except that the terms of the trust needn't be described if a complete description was previously submitted in a declaration related to a reporting event.
2. If at least one of each settlor, deemed settlor-beneficiary or beneficiary has his fiscal domicile in France, an inventory of all the trust's assets, rights and income, whether situated in or outside of France, and their fair market value (FMV) as of Jan. 1 of that year.
3. If no settlor, deemed settlor-beneficiary or beneficiary has his fiscal domicile in France, an inventory of the trust's assets, rights and income situated in France and their FMV as of Jan. 1 of that year. For this purpose, financial investments (such as publicly traded securities) are generally excluded, except: (1) investments (direct or indirect) relating to French real property or real property rights, and (2) companies or assets controlled by family members owning French real property or real property rights.

As discussed more fully below, the declaration must be accompanied by any required payment of the amount of any wealth tax on the value of French real property (the new *impôt sur la fortune immobilière* or IFI) held in the trust due for that year.⁴

Fiscal domicile for purposes of these reports is determined as of Jan. 1 of each year.

A form is available for trustees to use for the annual declaration but it isn't obligatory.⁵ The report may be made in any form.

The MTG Tax

France has a tax on gratuitous transfers (the MTG tax)⁶ by reason of gift or inheritance. The tax is generally payable by the recipient, who's also responsible for filing a return.

Tax rates are based on the type of relationship between the transferor and transferee. Transfers to direct descendants, spouses and domestic partners are taxed at lower rates (at graduated rates from 5 percent to 45 percent, depending on the net taxable value) than transfers to brothers and sisters (at 35 percent or 45 percent), to other family members up to the fourth degree of relationship (at 55 percent) and to



more remote family members and non-relatives (at 60 percent).⁷

All worldwide assets are generally fully subject to French MTG tax if: (1) the donor or decedent has his fiscal domicile in France,⁸ or (2) the inheritor, donee or legatee has his fiscal domicile in France and has had his fiscal domicile in France for at least six of the 10 years preceding the year of the transfer. (However, under Article 8 of the U.S.-France Succession and Gift Tax Treaty, if the donor, deceased or settlor is a resident of the United States, the French donee, heir or trust beneficiary isn't taxed except on French situs real estate, tangibles and business property.)

The MTG tax applies in the normal way if the transfer from the trust is considered to be a transfer by gift or succession under French law. Assets of a trust are subject to the MTG tax, without regard to whether a gift has technically been completed under the laws of a common law jurisdiction:

1. on transmission or at the death of the settlor or deemed settlor-beneficiary; or
2. if the beneficiary of a trust, as defined in the Code général des impôts (CGI), has his fiscal domicile in France⁹ (except as provided otherwise by a tax treaty).

It's the position of the French tax administration that a transfer from a trust will be considered a transfer by way of a gift or a succession only if a distribution is made to the beneficiary during the lifetime of the settlor (other than an income distribution) or at the settlor's death.

If, however, a transfer isn't considered a transfer by gift or by succession under French law, then those trust assets that are retained in trust are subject to the MTG tax in a different manner (*sui generis* taxation):

1. Any identifiable share of the trust assets attributable to a single named or identified beneficiary at the settlor's death is taxed according to the relationship between that beneficiary and the settlor (that is, at the rates for descendants, graduated from 5 percent to 45 percent depending on net taxable value).
2. Any identifiable share of the trust assets attributable to the settlor's descendants collectively (that is, a pot trust for direct descendants) is subject to the MTG tax at the highest rate applicable to transfers to direct

descendants, 45 percent.

3. Any other share is taxed at the rate of 60 percent.¹⁰

These rules are overridden if the trustee is subject to the laws of a state deemed "non-cooperative" under the French tax code or if the trust was created after May 11, 2011 by a settlor fiscally domiciled in France, and the assets aren't distributed to the beneficiaries at the time of his death. In such a case, all MTG taxes are paid at the rate of 60 percent.

In the case of trust property taxed under (2) and (3) above, the tax is payable by the trustee, and not the recipient, within six months from the settlor's death, if he died in France, or otherwise within a year of death.¹¹ However, if the trustee doesn't pay or if the trust is governed by the law of a state either considered "non-coop-

On the death of a U.S. citizen who resides in France, French succession tax applies to all his worldwide assets, including assets in any trust of which he's the settlor.

erative" or that hasn't ratified a tax evasion convention with France, the beneficiaries of the trust are jointly responsible for payment of the tax.

Whether the trust is revocable or irrevocable, and when it was created, aren't relevant. The law makes no distinction between revocable and irrevocable trusts. There's no such thing in France as a "completed gift" to a trust.

There is, however, a better result for U.S. residents (and perhaps the residents of other countries with an applicable tax treaty): All these tax rules are subject to the U.S.-France Estate Tax Treaty. If the settlor is a U.S. resident under the treaty at the time of his death and the trust assets don't include any French real property owned directly by the trust, or indirectly



through a company, no tax will be levied in France on any French beneficiaries.

French Income Taxation

Income received from a trust by a French resident is taxed with estimated tax of 30 percent due on the 15th of the following month and total tax rate rising to 45 percent.

Original principal isn't taxed as income on a distribution to a beneficiary.

It's important that the deemed owner himself declare the property on an IFI return and pay the tax because the highest rate of tax will be levied for property taxed to a trust and not declared by the deemed owner.

Income that's built up inside a trust without being distributed typically isn't subject to French income tax but may be subject to French inheritance or gift tax.

Applicability to U.S. Citizens

A U.S. citizen who becomes a resident of France is exempt from the IFI, except on French assets, for the first five years of residence.

Special rules also apply for U.S.-source passive income (deductible tax credit in France equal to the French income tax). These rules are applicable to trust distributions.

However, a trust of which the U.S. citizen is the settlor must still be reported and the exemption claimed for purposes of the IFI.

After five years, the U.S. citizen residing in France will be fully taxed by France on all his worldwide

real properties, including trust assets, for wealth tax purposes.

Succession Tax—U.S. Citizens

On the death of a U.S. citizen who resides in France, French succession tax applies to all his worldwide assets, including assets in any trust of which he's the settlor.

Assets that pass to a trust for a single beneficiary will be taxed as part of the decedent's worldwide estate, under the rules described above.

Assets passing to discretionary trusts at the settlor's death will be taxed at a 60 percent rate.

A U.S. citizen fiscally domiciled in France is subject to U.S. tax (income, gift and estate taxes). Under the U.S.-France Estate Tax Treaty, a U.S. citizen residing in France who leaves his assets outright to his French citizen spouse will obtain a \$11.18 million marital deduction in addition to the unified credit of \$11.18 million.

Thus, a U.S. citizen may leave a total of \$22.36 million outright to his French spouse.¹² That is, a U.S. citizen who passes property to his French citizen spouse won't need to use a qualified domestic trust for property valued less than or equal to that amount.¹³

Transfers between spouses at death are exempt from tax in France.

U.S. Citizen Trust Beneficiary

A U.S. citizen living in France who's the beneficiary of a U.S. trust will be treated as the owner of the trust if the original settlor isn't living (that is, as a deemed settlor-beneficiary).

He'll be subject to the IFI on distributions to French gift tax if the distribution is made to other beneficiaries and on death to French succession tax.

There will be no credit for U.S. estate tax because no tax will be payable in the United States.

Trusts Created by French Citizens

Generally, there's no tax advantage to a French individual creating a trust. There will be substantial reporting requirements, and the tax effect will be the same as if the property were owned outright, possibly worse.

However, because trusts aren't available under French law, a French person may want to create a trust for long-term management and control of assets if the French law regime of the fiducie is inadequate, recognizing that



there will be reporting requirements and no tax advantage, but no disadvantage if it's done properly.

The settlor, however, must not be a French resident at the time of the creation of the trust or at the time of his death, if assets are to remain in trust post-mortem. Otherwise the transfer of the trust assets to the beneficiaries, whoever they are, will be subject to a 60 percent tax in France.


Wealth Tax

France formerly had a wealth tax (the *impôt de solidarité sur la fortune* or ISF) that could be applied to trust assets under the 2011 trust law. This wealth tax was repealed effective Jan. 1, 2018 and replaced by a tax on French real estate, regardless of how it's held (the IFI). An individual is subject to the IFI if he has applicable French real property with a net value exceeding €1.3 million. The tax is levied at graduated rates ranging from 0.5 percent to 1.5 percent. The first €800,000 of value isn't taxed. The 0.5 percent rate applies to the taxable value from €800,000 to €1.3 million, and the top rate of 1.5 percent applies to taxable value in excess of €10 million.

Under French law and for the purpose of the IFI, real property held by a trust is deemed owned by the settlor or by a deemed settlor-beneficiary.¹⁴ Accordingly, all real property of a trust will be subject to the IFI if the deemed owner of the trust is a French fiscal domiciliary (except foreign real estate exempt under an applicable income tax treaty), while only French real property will be subject to the IFI if the deemed owner isn't a French fiscal domiciliary.¹⁵ It's important that the deemed owner himself declare the property on an IFI return and pay the tax because the highest rate of tax will be levied for property taxed to a trust and not declared by the deemed owner.¹⁶

In addition, a trust with French real property is subject to the reporting requirements described above, aimed at revealing the trust's subject real property and the identity of the deemed owners responsible for paying the tax.

As noted above, that annual trust declaration must be accompanied by any required payment of the amount of any IFI on the value of real property due for that year. If the real property wasn't duly reported as owned by the deemed owners, the required tax wasn't paid by them.¹⁷ Again, we stress that the tax

will be levied at the 1.5 percentage rate when a trustee pays the tax, rather than the deemed owners. 

Endnotes

1. Decree No. 2012-1050 for the reporting obligations of trustees is found at "Décret n° 2012-1050 du 14 septembre 2012 relatif aux obligations déclaratives des administrateurs de trusts," www.legifrance.gouv.fr/eli/decret/2012/9/14/EFIE1229648D/jo/texte.
2. Code général des impôts (CGI) Art. 344 G sexies.
3. The form is available at www.impots.gouv.fr/portail/files/formulaires/2181-trust1/2017/2181-trust1_1200.pdf.
4. CGI art. 990 J.
5. The form is available at www.impots.gouv.fr/portail/files/formulaires/2181-trust2/2017/2181-trust2_1209.pdf.
6. The tax on "mutations à titre gratuit," CGI art. 750 ter et seq.
7. CGI art. 777.
8. CGI art. 750 ter.
9. CGI art. 750 ter.
10. CGI art. 792-0 bis.
11. See CGI art. 792-0 bis and CGI art. 641.
12. The marital deduction under the treaty applies if at the time of the decedent's death: (1) the decedent was domiciled in either France or the United States or was a citizen of the United States; (2) the decedent's surviving spouse was domiciled in either the United States or France; if both the decedent and the decedent's surviving spouse were domiciled in the United States at the time of the decedent's death, (3) one or both was a citizen of France; and (4) the executor of the decedent's estate elects the benefits of the treaty provision and irrevocably waives the benefits of any other estate tax marital deduction that would be allowed under the law of the United States on a U.S. federal estate tax return for the decedent's estate by the date on which a qualified domestic trust election could have been. See Protocol Amending the 1978 U.S.-France Estate Tax Treaty (Dec. 8, 2004), Art. VI, para. 3. Note that the unified credit against the U.S. estate and gift taxes was recently doubled from \$5 million to \$10 million (plus an inflation adjustment) under the Tax Cuts and Jobs Act of 2017. Public Law No. 115-97 (Dec. 22, 2017).
13. Under U.S. law, the unlimited marital deduction is only applicable in the case of a U.S.-citizen spouse, unless the property passes to a qualified domestic trust (QDOT). See Internal Revenue Code Sections 2056(d) and 2056A. Estate tax with respect to the decedent's estate is imposed on property of the QDOT on distributions during the surviving spouse's lifetime and on his death. IRC Section 2056A(b).
14. CGI art. 792-0 bis and 970.
15. See CGI art. 965. The veil is pierced also for corporations and certain other entities.
16. CGI art. 990 J.
17. CGI art. 990 J.