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WILLS AND INHERITANCE
SHARED OWNERSHIP OF PROPERTY IN FRANCE

I. Your English will is not necessarily effective to dispose of French property. It may be ignored by the courts if it makes provisions which would be outlawed or ignored by French law, although in general a valid will made in English and in England (or here in France for that matter) will be acknowledged as formally valid in the absence of a French form will. The use of a French will may however save time, money and trouble for your executors and heirs, and we shall be pleased to advise as appropriate to your particular circumstances.

These notes are not and cannot be exhaustive; they are intended only for general guidance, and you should refer any queries to us. Please note that the rates of tax quoted may change.

It is a general principle of private international (or conflicts) law, recognised by both England and France, that real property is governed by the lex situs (ie: the law of the place where it is to be found). This also applies to all relevant tax matters under the double tax treaties. As a result, the inheritance position and estate duty matters relating to French real property are governed by French law, whatever your domicile at death. If you are resident in France on death (although you may have retained an English or other foreign domicile), then French law and French estate duty will apply to the whole of your estate worldwide.

French law contains compulsory provisions in favour of children. Where a person dies leaving one or more children, they are IN PRINCIPLE entitled to an irreducible share of the French estate, whatever any will may say. If no will is made, they inherit the whole estate in equal shares, and a surviving spouse may only at best, and without the assistance of a will or some other life-time gift, obtain an interest limited to one quarter of his or her late spouse's estate (plus a life-time right to continue in occupation of the matrimonial home, whether or not the survivor has any interest in the title).

The irreducible shares of the estate flowing to surviving children are:

- one child : one half of the estate;
- two children : two thirds;
- three or more children : three quarters (divided into equal shares between them).

Only the balance of the estate may be given to other persons (including the surviving spouse) by will or life-time gift, but either of these methods could grant the survivor a life-interest over the whole estate. A tontine or survivorship agreement can avoid these rules as may the use of a company in certain circumstances.

As of January 2007 however, under an amendment of the relevant Civil Code provisions, it is now possible for persons with a fixed entitlement to a share in a testator's estate (ie: children, grand-children or in their absence, surviving parents), to waive their entitlement in whole or in part in favour of other specified legatees. By way of example, if a testator domiciled in the UK owns French real property and wishes to leave it in whole to his surviving spouse inspite of having children with reserved rights, this is now possible by a "family arrangement". The testator would make such a legacy in favour of his or her spouse and the

children would execute a notarial deed whereby they waive their entitlement in the designated spouse's favour. This might be justified by reference to other assets gifted to them in the UK under the UK will of the testator, but such "justification" is not formally necessary. Such arrangements may also benefit other children or family members, or even third parties; they do not however alter the applicable estate duty, as to which see below.

It is also now possible to "skip" a generation leaving property to grand-children in spite of the intermediate generation of the testator's children still being alive at the time.

A final innovation is that an interest in property may now be entailed for one generation, that is to say that property may be left by a testator to a given person for life upon the condition that upon that person's death, full title then devolves on another legatee. This is an exception to the general rule that French law does not have a concept of trust; any such arrangement is already recognised as creating a fiduciary relationship between the intermediate beneficiary and the ultimate legatee. It is called a residual legacy; a variant available is referred to as a gradual legacy. The residual legacy leaves the intermediate beneficiary free to do as he/she wishes with the inheritance, the subsequent beneficiary receiving only what is left. The gradual legacy leaves the property to the subsequent beneficiary, the intermediate beneficiary not having the right to dispose of it.

These new rules do not only apply to real property. They may be applied to any asset subject to French law, such as the shares in a French company owned by a French resident. Shares are personalty, and thus dealt with by reference to the testator's "personal law": the personal law of a testator depends on his or her domicile on death, thus a British resident will only be affected by the new rules insofar as they apply to French real property, the remainder of his estate being dealt with under English law. However the rules apply to the whole estate of a British citizen who is a French resident on death.

If you purchasing or own property in France with other (particularly unrelated) persons, it may for various reasons be advisable to use a company as a vehicle for ownership. This should be referred to us in good time in order to ensure that completion is not delayed or a loan refused, because the company is not available or is otherwise not in a position to complete. There are advantages and disadvantages inherent in any choice of a corporate vehicle for the holding of property, and each case must be examined ad-hoc. However if you purchase the property in your own name, it is important to remember as aforesaid that French law always applies to real property situate in France, even though you may remain British domiciled on your death; your English will may not suffice to dispose of that property unless it does precisely what French law now allows; it may prove difficult to make a gift of the property outside your immediate family as any such gift will be expensive since estate duty is levied at the rate of 60%, without any allowance, on gifts and legacies between unrelated parties.

If you immigrate to France, with no intention of returning to the U.K., you would from a general English law point of view, lose your British domicile, which might very well invalidate any wills you have currently made, and thought would then in any event, need to be given to drawing up new French wills to cater to your personal wishes and changed circumstances. It is usually adviseable in the event of a change of domicile to use the tax holiday which may arise between the old and new tax domiciles, to reorganise one's liquid assets so that trusts and other tax reducing mechanisms can be set up in a tax-neutral environment. France will usually regard persons ordinarily resident here (ie: holding a current resident's card, and/or spending most of their time here) as being tax resident for the purposes of estate duty.

II. France does not have Inheritance tax. Inter vivos gifts and bequests on death are taxed to **estate duty**. The effective rates of estate duty in direct line of descent or ascent are generally favourable as compared to Inheritance Tax, since duty is levied on each recipient of a part of the estate, rather than on the estate as a whole.

As of and from 22nd August 2007 (ie: in respect of deaths occuring on or after that date), the whole of the surviving spouse's share in the deceased's estate is now completely **exempt** duty, whatever the value of the estate. This exemption also applies to partners in a PACS (a registered civil partnership or similar). Inter vivos gifts between married or PACSed persons are dutiable above a threshold of €80,724.

The deceased's children are each entitled to a duty-free allowance of €159,325 (death occuring on or after 1st January 2011) against the value of their share in the estate.

A married couple may therefore between them now leave a total of € 320,000 free of estate duty to EACH of their (common) children.

Grandchildren each obtain a duty free allowance of €31,865.

However, rates of estate duty are much higher (and the duty-free allowances much smaller - in most cases limited to €1,594 per share inherited) where the beneficiary of any gift or bequest is outside the deceased's immediate family. The rates and allowances are reviewed fairly regularly but do not in general keep pace with inflation.

The deceased's world wide estate is (subject to any relevant double tax relief) taxable to French estate duty where he or she was regarded as an ordinary tax resident of France on death.

Whatever the domicile of the deceased at death, his or her **real property** situate in FRANCE will as aforesaid devolve according to French rules and will be taxed to French estate duty at the following rates, subject to the various allowances aforsaid which vary according to the year of taxation and the person inheriting :-

- in direct line: rate varies according to value of share inherited, between 5% - 40% (on the dutiable slice above the €159,325 individual allowance for children);
- between brothers and sisters: 35% - 45% (each such beneficiary obtaining a €15,932 reduction on the dutiable value of his or her share, although where the beneficiary is aged 50 or more, is unmarried and lived with the deceased, his or her share of the estate is exempt estate duty);
- other relations to the 4th. degree: 55% (subject to a €7,967 reduction on the dutiable value of each share);
- others beyond the 4th. degree of family relationship: 60% .

Absolute INTER VIVOS gifts in general give rise to payment of the same rates of duty subject to a reduction in the amount of duty payable of 50% if the donor is aged 69 or less, and 30% if aged 70 to 79. Such a gift may (depending on the dutiable value) exhaust the allowance in favour of the relevant beneficiary in whole or in part, however where the donor survives at least six years after making the gift, a further gift to the same beneficiary may be made with a new allowance applying to reduce the duty payable.

In addition, gifts made subject to a life interest retained by the donor, reduce the taxable value by a percentage dependent on the age of the donor (35% in general reducing to 10% where the donor is aged between 71 and 79).

Thus a property valued at for instance € 150,000 gifted in whole (with no life interest retained by the donor) to a child of the donor, is currently only dutiable as to half that value, which dutiable portion would also be subject to the ordinary allowance applicable in direct line of €50,000.

A straight-forward gift of cash not exceeding €31,865 per recipient is also duty free (once only) in the hands of children or grandchildren (subject to the donor being aged less than 65 and the recipient being aged 18 or more).

III. Where husband and wife or other partners for whatever reason intend to make a joint purchase of real property, care must be taken to ensure that they own the proper shares in that property, and that in the event of sale, death or other event where the owners change, the resulting financial or other rights are as desired by the parties.

If no other agreement is made between the parties at the time of purchase (and reflected in the conveyance), then they will own the property in equal but separate or "divided" shares, which is the equivalent of an English law tenancy in common. This means that whilst each owner is fully entitled to use and enjoy the property without restriction, each share is distinct and there is no automatic entitlement for either party to inherit the other's share(s).

In the case of separated shares, a will could gift the shares to the other joint owner(s), but such a will might not be effective in French law (eg: between spouses or unrelated parties, where there are children entitled to irreducible shares in their parent's estate).

An advantage of such divided shares however is that they do not necessarily have to be equal and the conveyance on purchase may therefore reflect the differing contributions of each party. In the event of a sale, each party recovers what he or she has brought in by way of financial contribution, and the shares may also be varied to reflect the intended unequal contributions to loan repayments or to the cost or effort involved in building or renovation work. Furthermore, a certain freedom to leave the share to someone other than the remaining joint owner(s) may also be seen as an advantage in certain cases.

Such a method of ownership is referred to as an "indivision" in French law; no-one may be forced to remain in such a situation unless he or she has otherwise agreed by contract (the duration of which may not exceed five years). Thus a sale may as a final recourse be forced by any of the owners (eg: in the event of a divorce), and to some extent this position may be compared with an English law bare trust for sale, although it should not be forgotten that French law does not contain equitable doctrines and remedies.

Where the parties do however wish to provide that the whole title is to revert to the survivor on the death of any joint owner (eg: between spouses, to cement the surviving spouse's rights and avoid the compulsory inheritance provisions of French law, at least on the first death), it is possible to arrange this by including a "tontine" or lottery clause in the title. This gives the survivor rights equivalent to those of a joint tenant in English law. It is not possible to amend the title later to arrive at the same result and so this should be dealt with on purchase.

This sort of arrangement is however difficult, if not impossible, to amend or sever subsequently, and therefore careful thought should be given to the parties' rights and desires before it is included in the title. A subsequent divorce or separation would not for instance alter the survivor's rights, and we would therefore recommend that the method of ownership be discussed with us prior to any final instructions being given to the notary dealing with your purchase. Where unrelated parties are involved, the French estate duty on a gift between them (even under a tontine arrangement) remains 60%, and the tax aspect thus also needs careful attention.

The French courts are likely to ignore British legal considerations in the event of a dispute as to title over the French property. However the English courts could (in a dispute concerning British domiciled parties) take the French shares (or allocation of rights to the French estate) into account when determining whether overall the position is equitable. Compensatory adjustments in relation to British assets, could be ordered were the French position found to be inequitable.

Each case needs individual attention, and we shall of course be pleased to be of further assistance.

If none of the above is wholly satisfactory to your case or wishes, and if you intend to take up residence in France, it may be possible or desirable to arrange matters otherwise through a marital contract

to be adopted between the spouses. One of the French matrimonial régimes which may be adopted is that of universal commonality of all assets, the effect of which is to leave all marital property to the survivor of the spouses on the first death, deferring the children's or other heir interests to the second death.

Whatever solution (matrimonial contract, tontine or testamentary disposition) is adopted, the benefit to the surviving spouse on death is now exempt any estate duty. However this exemption from duty should not be taken to mean that any of the solutions may be adopted; only a matrimonial contract (universal commonality – see below) allows the whole estate to flow to the surviving spouse. The tontine only affects the property concerned. A will cannot reduce the legal minimum entitlements of the children of the deceased.

IV. Thus the best solution in general (particulary where the property has already been purchased and the conveyance does not incluse a tontine clause) is for British spouses to adopt a French marital contract or settlement, whether in relation to their French property alone (most appropriate where thay continue to be UK domiciled) or of general effect (where they become French residents). Such contracts can be of varied effect: they may make provision for property to be owned in all circumstances in separate (or severed shares), or for all property to be owned jointly, with the survivor of the couple inheriting everything. Various shades between these extremes may also be adopted.

The marriage contract known as “communauté universelle des biens” (universal common ownership of all property), is the contract which puts all property (or certain designated assets) into common ownership, with the survivor taking all. The major advantage of this type of marriage contract is that on the first death, the title to the property flows to the survivor automatically and with no payment of estate duty; estate duty will only be payable on the second death, which may be slightly disadvantageous to children as they will only obtain the benefit of one duty-free slice against their parents’ joint estate (instead of two, the first on the first death and another on the second), but in most cases the saving on the first death more than outweighs this consideration.

Such a marriage contract may be freely adopted by most British couples, by their registering a marriage settlement with a notary; certain circumstances may however militate against this solution (such as children from first marriages, whom the parents do not wish to disinherit), or in exceptional circumstances, the place of the marriage or of the first matrimonial home. In general however, a couple with children only from their marriage who married in the UK and made their first matrimonial home there, can adopt such a contract without any restriction.

Marriage contracts and the advantages which may flow from adopting one or from amending a pre-existing arrangement, only apply to married couples. PACSed couples must deal with property matters in their “pact” which should therefore be drafted carefully by a competent lawyer.

V. Whilst an English will often does not suffice to dispose of French real property, it can be used to dispose of shares in a company which are deemed to be personalty, and thus governed by the deceased's personal law (i.e. that of his domicile), rather than by the law of the place where the property is situate.

Another method of ensuring that the property is handled in accordance with one's wishes rather than by compulsory French legal provisions, is thus prior to conveyance, to place a company between the owners and the title to the property. (A subsequent re-conveyance to a company will be as costly as the original purchase and may give rise to capital gains tax liability).

A French law S.C.I. (most nearly equivalent to an English law partnership) can be used to avoid the difficulties referred to above, particularly if associated with trust arrangements made in England (it should be noticed than French law does not pro tem recognize a trust). However without trust arrangements, the use of an S.C.I. will not avoid French estate duty, and the case law shows that such a company may not in all

circumstances remove the question of the rules of succession from the jurisdiction of French law to that of English law.

A previously purchased property may be reconveyed to an SCI at a cost of between 2 and 3% of its market value, being 1% duty and registration fees and the balance the notary's fees and land registry charges.

The use of an English limited liability company registered with dormant status, if it has no activity (in particular no income), removes all questions relating to ownership in the hands of the "joint-owners" from French law to English law, since the company owns the title to the French freehold, whereas the "joint-owners" own shares in that company.

Where it is possible to use a English company, all difficulties arising between shareholders are effectively within only the jurisdiction of the English Court. Additionally in the event of a death, only English law would apply to gifts or legacies of any shares, and French estate duty would be wholly avoided, leaving any transfer to be taxed as appropriate only under English rules.

The other main tax advantage of the use of a U.K. company, is that rather than selling title to the property, the shareholders have the option of selling the company's shares in which event no French duty is paid, nor is the transmission subject to capital gains tax in France.

The disadvantages of the use of a U.K. company are :

1/ During the time in which the company owns title to the French property, it must make an annual return to the French tax authority, although it is in fact exempt from any tax provided it has no French taxable income. This does not normally apply to an SCI, although it would have to make an ordinary income tax return on behalf of its members, even though there may be nil income.

2/ Notwithstanding that the company may be dormant, the directors must make an annual return to Companies House in the U.K.. This of course does not apply either to a French SCI, which is exempt any requirement for an annual return in France.

3/ The French rules as to capital gains tax are favorable to individuals, but not to companies. Thus were the company to sell the property (rather than the shareholders selling their shares), the whole athematical capital gain would be taxable in France without any index linking of the historic base cost, and without any of the annual allowances otherwise available. Additionally, since the beginning of 1994, a foreign registered company owning French real estate is deemed to have made a depreciation charge of 2% p.a. for each year of ownership, and thus the historic cost of the property reduces by 2% p.a. thereby increasing the taxable slice of the proceeds of sale.

On the other hand, the use of an SCI which is for tax purposes regarded as transparent, allows the shareholders to take full advantage of the French capital gains tax rules.

4/ The British Inland Revenue will regard the directors'/shareholders' use of the French property as being a UK taxable benefit in kind made available through the UK company. It is theoretically possible for the French tax administration to do the same, thereby creating a nominal annual charge to income tax for the beneficiary directors. The British government has also recently decided to tax English companies whose only activity is to hold land abroad, rather heavily, and this route is now of doubtful usefulness.

(Only for British tax residents) Please also note that special consideration needs to be given to your position in the UK (and that of the surviving spouse) if you have a personal pension scheme (including a SIPS) and intend to use it to finance an acquisition in France or to continue to draw on it after becoming

French resident. You should so inform us and take specific UK tax advice on the subject BEFORE investing/moving.

Rates and rules up to date as of 01/2011, but may vary.