



## **THE FRENCH SCI – PROPERTY HOLDING COMPANY**

When purchasing residential real estate in France, foreign residents are often interested in the idea of owning the property through a holding company. The principal reason for doing so is due to the restrictive nature of certain French succession law provisions.

We have set out below a brief view of the relevant succession provisions and the effect of holding property through an SCI. We have also looked briefly at the other main advantages and disadvantages of forming and managing such an entity.

### **1. French succession law**

#### **1.1 Applicability**

When considering whether or not French law is likely to apply to a particular probate situation, it is important to draw a distinction between tax law and other civil law provisions. The rules governing their application are not the same.

From a general civil law point of view and as may seem obvious, French inheritance rules only apply to assets within the deceased's estate, the administration of which upon death is governed French law. Real estate situated in France falls within this category, however this is not the case for "moveable" assets, which are governed by the succession laws of the country of the deceased's last fixed domicile.

Unfortunately, French inheritance tax rules do not make the same distinction and apply to both movables and immovables. For example, inheritance tax would therefore be due on the value of the furniture, vehicles and other assets situated in France at the time of the death.

The major effect of this rule is that shares in a property holding company therefore escape the application of French succession law (see below), but are nevertheless subject to French inheritance tax.

Finally, it should be noted that these rules obviously do not apply for real estate or moveable assets situated outside of France.

#### **1.2 Effect**

There are certain restrictions implied by French law which overrule the terms of a contrary will, in order to ensure that it is impossible to disinherit certain categories of beneficiary. Such rules only apply to that part of the estate governed by French succession law (see above).

A certain part of the estate of a deceased individual ("la réserve") must pass to certain specified individuals due to their close family link (the "réservataires").

These enforced heirship provisions are not encountered in many other legal systems and often shock those unfamiliar with the French legal context.

### **2. Effect of a French property holding company (S.C.I.)**

## 2.1 Avoidance of enforced heirship provisions

The principal reason for foreign residents to own a property through an SCI is that for civil law purposes (not unfortunately for tax purposes – see above) shares in an SCI are treated as moveables and therefore do not fall under the French succession law regime. Instead, their transfer upon succession is governed by the law of the deceased's domicile at the date of death. Holding shares in a property company rather than owning the property directly therefore helps to avoid the French enforced heirship laws and other restrictions on testamentary freedom.

## 2.2 Simplifies Co-ownership

The use of an SCI provides for maximum flexibility and stability if it is intended that a property should be bought by several individuals compared to purchasing as joint owners "*en indivision*"

Indeed the "indivision" regime is known to be disadvantageous for the following reasons :

- There is no obligation for the co-owners to keep their rights of ownership and to remain in the "indivision". In the case of a dispute between any of the co-owners, the others might be forced to sell the whole property or at least to buy back the other(s) "share". Of course the resale of the property will require the agreement of everyone and any objection could bring the situation to a standstill.

The "indivision regime" might also be a disadvantage when one of the owners dies. Indeed, according to French inheritance law the heirs and beneficiaries (including the surviving spouse) would receive the deceased's part of ownership. The former owners would then have to share the right of ownership with these heirs and beneficiaries.

## 2.3 Tax transparency

For tax purposes (for example, income tax on rent) an SCI is totally transparent and therefore tax is charged on the underlying shareholders as if they held the property directly.

It is important to consider the type of rental that will be carried out by the SCI.

Setting up a French property owning company is not adapted to renting out **furnished property** because French law considers that this is a business (and not a civil) activity. Any income would become subject to corporation tax, not individual income tax. If you remain UK resident, the French rental income will also be liable to UK income tax, wherever the money is deposited or paid to you even if the money is never brought into the UK.

Any French tax paid is deductible against the UK tax liability, in accordance with the UK/France Double Tax Treaty.

## 3. Creation and management of an SCI

An SCI can be created very simply and the share capital will generally be a small amount, for example 1.000 euros.

Our charges, taxes, costs and disbursements for setting up the company and dealing with the initial registration formalities would be :

- fees = 1700 euros
- VAT on fees = 333 euros
- Disbursement (companies registrar, legal advert...) = 500 €

**Total = 2550 euros**

As for the management of the company, this is relatively simple. Although there is no specific text stipulating that maintaining accounts is a legal requirement, in practice, it is highly recommended. These accounts can be maintained at a minimal level.

#### 4 Transfer of the ownership of French property to a French SCI

Should a decision be made to transfer a property to an SCI after the property has been acquired (as opposed to acquiring the property directly through the SCI), the following should be kept in mind :

##### 4.1 Cost

#### REGISTRATION TAX AND TRANSFER TAXES

The transfer of real estate to an SCI is treated as a contribution to the capital of the company and is taxed according to the nature of the contribution, namely whether it is in return purely for shares or also for another consideration such as the repayment of a loan attached to a property.

If the contribution is of the full value of the property (i.e. no outstanding loan) the tax payable on the transfer would be limited to our fees of around 0,5 % (including VAT) of the value of the property, and land registry fees of 0.1% of the same value.

However, if the contribution includes the company taking on the outstanding liability of a loan over the property, that part of the value is taxed at the same rate as an ordinary sale of the property, namely around 5% .

#### CAPITAL GAINS TAX

The transfer of the property to an SCI will also be considered as a chargeable disposal of the property for capital gains tax purposes. The charge to capital gains tax will depend upon the increased value in the property since its acquisition and a number of other conditions, which require further details (see our note on CGT).

#### 4.2 Other consequences

#### RIGHT OF PRE-EMPTION

The transfer of the property will be considered as a proper transfer which would entitle the local authority to exercise its right of pre-emption should it wish to do so. This is unlikely, but it should be kept in mind

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