Charles Hamer Financial Services
INDEPENDENT FINANCIAL ADVISERS

87 Park Street, Thame, Oxfordshire, OX9 3HX
Tel: 01844 218956 Fax: 01844 261886
www.charleshamer.co.uk
Partners: Jonathan Pawsey Dip PFS. Karen Ellis

THE FRENCH FINANCE ACTS OF DECEMBER 2012. THE MAIN PERSONAL TAX CHANGES PASSED INTO LAW.

After much heated debate which resulted in both 2013 Finance Bill and the 3rd 2012 Retroactive Finance Bill being taken to the Constitutional Counsel for final say, both bills were passed into Law in the final few hours of 2012.

Much of the initial proposals in both bills and summarised in our earlier bulletins have changed almost beyond recognition. The present bulletin therefore starts from scratch and summarises all the main outcomes as are likely to be relevant to the majority of our clients – namely those concerned by personal taxation as non active residents or non residents owning a French property.

This summary is by no means an exhaustive explanation of all the tax changes introduced. There are plenty more modifications that will affect the resident and non resident taxpayer according to their particular circumstances, whilst the explanations below are insufficiently detailed to be relied upon for a risk free DIY approach to be adopted when addressing French self assessment.

To find out more on how the following tax changes and others will impact your personal French tax bill, how your tax liabilities can be reduced and our French personal tax return compilation services, please contact either:

Our senior advising partner: **Jon Pawsey** at jon@charleshamer.co.uk

Or

Our head of department - client tax services: **Alex Romaine** at Alex@charleshamer.co.uk by phone on (00 44) (0)1844 218956

The summary of the main tax changes now follows:

1. Freezing of tax band thresholds and most allowances.

For the second year in a row the income tax band thresholds for assessment of 2012 income will be frozen at 2010 levels, rather than adopting the usual practice of revaluing the thresholds in line with inflation.

The same freeze in tax bands applies to Inheritance Tax, (whose nil rate bands were also reduced in certain cases by the second rectifying tax act of 2012).

The freeze is not across the board, however:

Age related income tax allowances, those with modest income, certain disabled taxpayers and the thresholds to qualify for Taxe Foncière and Taxe d'Habitation exemptions will see a 2% increase in their relevant limits for exemption or relief.

2. Introduction of a new higher rate 45% Income tax band but cancellation of the Gerard Depardieu tax!

A new higher rate income tax band has been introduced for 2012 income and beyond, set at 45% and applying to income exceeding €150.000 per taxable part.

This in turn bumps up the effective income tax rate for those households with taxable income above €500.000 per part to 49%, once we take into account the 4% "contribution exceptionnelle sur les hauts revenus", introduced in the 2011 Finance Act and remaining in place for as long as there is a govt. deficit.

This new tax band is not to be confused with the 75% effective tax rate which has so famously led – allegedly! - to Gerard Depardieu moving to Belgium and being invited to become a Russian citizen. Ironically, that particular proposal – to introduce a "contribution exceptionnelle de solidarité sur les très haut revenus d'activité " charged at 18% and which in any event was to only apply to earned income in excess of €1million - has subsequently been quashed by the Constitutional Counsel

We therefore end up with the following tax rates per taxable household part:

Table 1: French Progressive Rate Income Tax Table -2012 Income.

Taxable Income	Marginal Income Tax Rate
€0 - €5.963	0%
€5.964 - €11.896	5.5%
€11.897 - €26.420	14%
€26.421 - €70.830	30%
€70.831 - €150.000	41%
€150.001 - €250.000	45%
€250.001 - €500.000	48%
€500.001 +	49%

3. Tax Benefits Ceiling Reduced to €10.000

Currently – for 2012 income tax - each household can claim up to €18.000 per year, plus 4% of total taxable income, in tax credits and reductions related to a wide range of qualifying expenditure and investment, (e.g. renewable energy investment in the home). So, for example, a household with gross taxable income of €100.000 can reduce their tax bill by up to €22.000 in making use of these routes.

For 2014 tax assessment of 2013 income this ceiling, for the most part, is to be reduced to €10.000 with no proportionate uplift against total taxable income.

4. Reduction In The Family Quotient Benefit Ceiling.

The French income tax system provides an income tax benefit for each member of the taxable household. Known as the "Quotient Familial" each member – depending on circumstances - is counted as between a one quarter or one whole unit when calculating the number of household units by which to divide total household income when calculating the tax due. For 2011 the maximum income tax benefit obtained by the Quotient Familial was €2.336 per half unit. In most instances, this is to be reduced to €2.000 for 2012 income.

Exceptions to the rule include those taxpayers who are disabled or who are widowed and with dependent household members.

5. Progressive Income Tax Rate on Investment Income.

The income tax rate applied to investment income received from 01/01/2013 is to be aligned with earned income.

Up to and including 2012, the taxpayer could elect for interest and dividends generated in France and dividends from abroad to be taxed at a flat rate, deducted at source, known as Prélèvement Libératoire, which represented full and final payment of all income tax due on that income.

From 01/01/2013 such income will be assessed at the progressive income tax rate by being added to other taxable income. When the tax continues to be deducted at source, (see items 6 and 8 below), such deduction will be credited against the total tax assessed and rebated when the tax arrived at under the progressive rate is lower than the flat rate of tax already paid.

One or two exceptions to this rule do remain however, including the election for Prélèvement Libératoire on profits attached to withdrawals from certain Assurances-Vie / EU based investment bonds, Bons de capitalisation, Plans d'Epargne en Actions and Bons Anonymes.

6. Dividends – Obligatory Taxation at Source.

For dividends and other company distributions received on or after 01/01/2013, a compulsory tax at source now applies to all individual French resident taxpayers, whether or not the dividends are French ***or sourced from overseas***. The tax at source is ***levied at 21%*** and constitutes payment of income tax on account.

If the tax so paid on account exceeds the overall income tax due then the excess is rebated on completion of the assessment for the year, (i.e. in late 2014 for 2013 income).

When the income is from abroad it is up to the taxpayer themselves to make the at source tax payment within the first two weeks of the month following receipt of dividend. When the dividend is from a company or organisation (e.g. OEIC or Unit Trust) based in the EEA (European Economic Area) the taxpayer can authorise the company to make the payment directly on their behalf, (in theory! – we are not confident that the company or investment manager concerned will regularly be so willing in practice).

Fortunately there is an exception to this new rule:

The taxpayer can request an opt-out from the arrangement if total taxable household income from all sources in the year two years prior to the year of income, (i.e. 2011 in respect to 2013 dividends), was less than €75.000 (or €50,000 in the case of a single taxpayer household).

This opt-out needs to be presented annually, prior to the 30th November of the tax year prior to the year of dividend payment, and ***prior to 31st March 2013*** in the case of 2013 dividend income.

A copy of the opt-out also needs to be presented to the organisation making the dividend payment.

Penalties for non co-operation:

a). For making a false claim to exemption: 10% of the tax at source otherwise payable plus late interest
b). Failure of any party making the dividend or distribution to supply a copy of the opt-out: €150
c). Failure to make the payment at source: 10% plus late interest

7. Dividends - Withdrawal of Income Tax Allowance.

Up to and including 2011 income, dividends enjoyed a category specific income tax exemption or allowance valued at €1.525, as applied to 60% of the gross dividend, increasing to €3.050 for married couples and civil partners. This was in addition to a general 40% income tax allowance applied to the gross dividend

For dividends received from 01/01/12 the €1.525 and €3.050 allowances are withdrawn, although the 40% of gross dividend allowance – as it applies to income tax – remains, (as does the ability to make use of the UK dividend tax credit against the overall tax due).

8. Interest – Obligatory Taxation at Source.

In a similar but not quite as extensive vein as the new rules applying to dividends, all taxable interest received with effect from 01/01/2013 ***is subject to tax at source levied at 24%.***

Again it will be credited against total tax due on assessment in the following year and rebated whenever the tax at source exceeds the resulting tax assessed.

Exceptions to the rule are:

- Interest from abroad is not subject to the tax at source levy if the household total taxable income from all sources in the year two years prior to the relevant tax year of income (i.e. 2011 for 2013 interest) does not exceed €25.000 (single taxpayer) or €50.000 (couples and civil partners).

- The taxpayer can request an opt out against all interest income, both sourced in France and abroad, if the €25.000 and €50.000 thresholds referred to above are not exceeded. The procedure and deadlines for exercising the opt-out are the same as for the tax at source on dividends, (notice to tax office by **31st March 2013** for 2013 income and 30th November of the prior year for subsequent years).

When total gross interest received for the year does not exceed €2.000:

The taxpayer can elect for the 24% tax paid at source to be treated as full and final payment of tax due on that income, irrespective of the marginal rate of income tax otherwise applicable under the default progressive rate – as described in item 5 above. Such an election is made at the time of submitting annual tax returns.

Table 2: Summary of Household Income Limits Permitting Opt Out of Taxation at Source of Interest, Dividends and Other Distributions

Income Type	**Household Status**	
	Taxable Income Threshold in Year n-2	
	Single / Divorced / Widowed	**Married / Civil Partnership / PACS**
Interest	€50.000	€75.000
Dividends	€25.000	€50.000

9. French Capital Gains Tax on Shares and Collective Investments.

Rules have been substantially altered by the 2013 Finance Act and the present outcome varies according to when the gains are realised (2012 or 2013) and whether or not they refer to business or simply investment / private assets. This summary limits its explanation to private investment assets.

Investment / private assets

The following rules apply to the taxation of OEICS, ISAs and Unit Trusts, SICAVS and FCPs, as well as direct shareholdings.

Gains realised in 2012 continue to be taxed at a flat rate, although this has increased from 19%, (as was applied to gains made up to and including 2011) to 24%. Of course, Prélèvements Sociaux charged at 15.5% will be added to this, so bringing up the total tax rate on gains (excluding any CMU possibilities) realised in 2012 to **39.5%**

Gains realised in 2013 and beyond will – in the main - be assessed at the **marginal rate of income tax**. However, to mitigate the impact, the gross gain will be reduced by taper relief for the purposes of income tax but not Prélèvements Sociaux.

The relevant holding period for taper relief will, subject to the occasional exception, be from the date of acquisition. Therefore current holdings could benefit from taper relief if sold in 2013, depending on when they were initially acquired.

Table 3: Taper relief on Movable Intangible Investment / Private assets (applicable to disposals on or after 01/01/2013

Holding Period (from the date of acquisition, not from 01/01/13)	**Income Tax Taper Relief**
0 – 2 years	0%
2 – 4 years	20%
4 – 6 years	30%
6 + years	40%

Furthermore, it is the gross gain, rather than the tapered gain, which is used to determine the "Revenu Fiscal de Reference" in the year of disposal. Whilst not directly relevant to the actual capital gains tax payable, this rule will impact on any contributions to CMU (Couverture Maladie Universelle) or claims to exemption or relief from ISF, (Impôt de

Solidarité sur la Fortune / Wealthtax), Taxe Foncière and Taxe d'Habitation, or any other benefits dependent on the Revenu Fiscal de Reference figure.

Business Assets.

It is not within the scope of this bulletin to explain what qualifies a share as a business asset, but it suffices to say that when the criteria are met, more generous capital gains tax reliefs apply depending on the circumstances of the disposal, (e.g. retirement relief, or business roll over relief).

10. French Capital Gains Tax on the Disposal of Land and Buildings, (and in shares in companies whose balance sheet is dominated by French land and buildings).

Capital gains tax on sale of French property is a particularly complex area, encompassing a number of technical issues which – without prior planning well before making the intended disposal - can otherwise give rise to quite a nasty shock when the tax is finally arrived at a day or so before the sale is to take place.

2012 saw quite a few changes to the French Capital Gains Tax treatment of property, particularly for the non resident owner.

We therefore strongly advise you to visit our web pages for more details of these general technical issues, potential exemptions and wholesale changes, which also incorporate the modifications described below. Please visit:

http://www.charleshamer.co.uk/French_capital_gains_tax.aspx

The **3rd Retroactive Finance Act 2012** has introduced a capital gains tax surcharge on all taxable gains realised on disposals made on or after 01/01/2013 unless the sale relates to a Promesse de Vente (or Sous seing privé) registered before 7th December 2012 or a Compromis de Vente drawn up by a notaire and signed before the same 7th December date.

The supplementary charge applies to the whole of the post tapered gain, at the rate shown in the following table:

Table 4: Supplementary Capital Gains Tax: Basic Rates and Transitional Reliefs

Post Tapered Gain	Supplementary Tax Rate on the Taxable Gain (TG)	Transitional relief
€0 - €50.000	0%	€0
€50.001 - €60.000	2%	(TG-€60.000) x 5%
€60.001 - €100.000	2%	€0
€100.001 - €110.000	3%	(TG-€110.000) x 10%
€110.001 - €150.000	3%	€0
€150.001 - €160.000	4%	(TG-€160.000) x 15%
€160.001 - €200.000	4%	€0
€200.001 - €210.000	5%	(TG-€210.000) x 20%
€210.001 - €250.000	5%	€0
€250.001 - €260.000	6%	(TG-€260.000) x 25%
€260.001 +	6%	€0

Important Note:

The provision made by article 15 of the 2013 Finance Bill to allow a 20% additional allowance against the post tapered gain for both the standard rate income tax of 19% and the above supplementary tax **was withdrawn** following a decision by the Constitutional Court to quash article 15 in full as a result of the tax burden arising from other sections of this same article being found to be too burdensome and thus unconstitutional. A classic example of the baby being thrown out with the bath water!

For an EU resident making a taxable disposal of their French property the French tax rate can therefore now amount to **40.5%** as a result of the latest modifications.

This is substantially higher than the UK income tax rate of 28% that a higher tax payer UK tax resident might face. There is thus a strong incentive to explore all avenues for bringing the French taxable gain to a minimum.

Visit http://www.charleshamer.co.uk/French_Capital_Gains_Tax_savings.aspx for some examples of where we have been able to help clients reduce their French CGT.

11. ISF – Wealthtax.

The 2013 Finance Act introduced a wide ranging reform of ISF, the result of which is to bring it more closely into line with the position prior to the changes introduced in 2012

ISF will now apply whenever the taxable estate exceeds €1.3million but in such circumstances will then be assessed at progressive rates of tax on the net estate exceeding €800.000, as follows:

Table 5: French Progressive Rate ISF -2013 Assets.

Net Taxable Estate	Marginal Tax Rate
€0 - €800.000	0%
€800.001 - €1.300.000	0.5%
€1.300.001 - €2.570.000	0.7%
€2.570.001 - €5.000.000	1.0%
€5.000.001 - €10.000.000	1.25%
€10.000.001 +	1.50%

There are a couple of reliefs against the gross tax arrived at in the above table:

Décote:

Transitional relief will be available for those estates with taxable estates between €1.3million and €1.4million. The relief amounts to: €17.500 – (taxable estate x 1.25%).

Payment ceiling

Limited to French tax residents, total ISF, Income tax (French and foreign) and Prélèvements Sociaux cannot exceed 75% of relevant income. When this is the case, ISF is reduced accordingly to the above ceiling. Relevant income comprises all income and gains realised – taxable and non taxable – for the previous tax year.

Impact of the ISF changes on Trusts and Trustee obligations

Since last year Trustees and/or their beneficiaries or settlors have been required to disclose details of the Trust and trust assets whenever the Trust has assets located or a beneficiary or settlor resident, in France.

When the French resident beneficiary or settlor would otherwise be liable to ISF and fails to include trust assets in their personal ISF declaration and/or the Trustees fail to make proper disclosure of such assets, a stand alone tax equating to the highest marginal rate of ISF is payable.

Previously, the highest marginal rate stood at 0.5%. As a consequence of the above changes to ISF rates, this tax charge therefore rises to **1.5%.**

Bearing in mind that if such assets were properly disclosed, the corresponding ISF in most instances would fall well below the 1.5% level or may be exempt altogether, this 1.5% effective tax penalty acts as quite an incentive to bring Trust affairs into order whenever there is a French connection.

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