OVERSEAS CHAMBERS OF PETER HARRIS

E: oc@overseaschambers.com
T: +44 (0)1534 625 879
F: +44 (0)1534 491 195
www.overseaschambers.com

Chestnut Farm
Mont du Ouaisne
St Brelade
Jersey, JE3 8AW

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Information correct as at 24th October, 2012

Overview of the French Trust tax *Instructions*

The French trust taxation instructions are now published, as of 16th October, 2012.

As indicated, the non-compulsory declarations for the French Trust declarations were published on the French administration's website on 20th September, without any form of administrative commentary or instruction.

It is difficult to post a serious and objective commentary on this piece of regulatory intervention without becoming irate at the inadequacy of the process. I am endeavouring to restrain my natural tendency for sharp humour in so doing.

The filing date for the levy declaration was postponed in the decree of 15th September to 30th September, 2012, a Sunday, and without mentioning that the dominical respite was also available to non-residents. In effect that the non-resident trustee could in fact produce the declaration by midnight on Monday 1st October. The postmark is generally being admitted as proof of posting and therefore of filing.

What is pernicious is the entire lack of administrative definition of the terms used in the legislation which define liability, in particular what a trust is, or at least is considered to be, what a beneficiary/bénéficiare is and lastly, any confirmation as to the ambiguity in the decree which could have meant that trusts in existence before 31st July, 2011 might be required to file the declaration of existence, modification or extinction of a trust by 30th September, rather than the 31st December, 2012. The fact that the explanatory instruction appeared after the deadline in itself constitutes a means of retorsion by the taxpayer if threatened with penalties for non- or incomplete declaration.

In short this is the least effective implementation of a tax that has ever seen the French regulatory book. Never has such an important international initiative been introduced in such an inefficient and slovenly manner by an administration that generally prides itself upon its effectiveness and efficiency; and whose Minister was attempting to sell French administrative machinery to the world as being an effective model of management and fairness. The only reason why the Minister, and the administration, have escaped political censure so far is that trustees, being foreigners, have no vote, and no right of representation beyond the scant rights given to taxpayer in general under

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the principle of equality before the law. The French political system has therefore failed, in that the uneducated and biased cries of trusts being no more than a form of formal tax evasion from the rabid left in France has simply enabled the administration to brave out its failures, by effectively ducking their constitutional responsibilities and pointing the fiscal finger in another direction, the foreigner, and to take the term further "fingering" trustees for penalties.

That said, the instructions commenting on the declarations were published two weeks after the formal due date: on 16th October; 2012.

Congratulations therefore to the French administration and Parliamentary process for the precise legal definitions that determine the right to tax at the tax point; two weeks after the "event".

It is only to be hoped that the idea of inflicting any form or penalty of €10.000 or 5% of the trust assets, not the net trust fund, of any trustee who has not been able to translate or understand the degree of complexity of the declaration required will evaporate on challenge, if nothing else out of pure shame. It is only to be hoped that the information exchange mechanisms that the French administration believe that they can count on will be blocked by the majority of Treaty or administrative assistance partners owing to the arrogant lack of notification and information as to the changes, which form a condition as to the operation of TIEAs.

The Instructions, parsimonious as they are, make specific reference to the source of the tax provision, as being the "definition" of the Trust contained not only in the Hague Convention of 1st July 1985 on the law applicable to trusts and their recognition[1]; which therefore includes the preliminary works contained in the tome published by the Hague Conference. France participated in the preliminary works of the Conference, and signed the Convention, but has yet to ratify it. In effect, the civil servants drafting the law and eth instructions have chosen to subjugate the taxation concept to the Convention and the preliminary works involved, cherry picking in taking certain options which were not taken up in the final definition of what characteristics provided the skeleton for recognition of certain Trusts and requiring theirs recognition. In France the preliminary works are evidence as to the Convention's meaning and interpretation. This in part explains why the French were able to deploy the definition or rather amended definition, as it is not the same as that in the final Hague Convention, as a general concept, not as a specific device aimed only at common law trusts. Hence the comprehension of the Liechtenstein vehicles in the concept, to the extent that these meet the definition. There will be therefore be other civil law vehicles of a similar nature also caught by the definition.

[1] *http://www.hcch.net/index_en.php?act=conventions.text&cid=59*

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The umbrella document may be found at : http://bofip.impots.gouv.fr/bofip/1-PGP.html#.

The outline definition is at : http://bofip.impots.gouv.fr/bofip/7964-PGP?branch=2

It repeats the main definition of a trust, which is stated to be valid for the whole of the Code Général des Impôts, and which is subsequently confirmed in the interpretation Instruction as defining what a trust is:

It is to be stressed that the tax definition does not correspond exactly to article 2 of the Hague Convention of 1985, as it uses several different terms, for example, an "administrateur"[2] rather than a trustee, and includes certain terms which do not figure in it.

The summary confirms that :

1. The article 792-0 bis definition will comfort the solutions from prior jurisprudence, both cases and academic theory, in situations where the presence of a trust will not block the application of prior fiscal rules ; and on the other hand,
2. Creates tax régimes in the area of Wealth Tax, (ISF) and gratuitous transfer duties (DMTG) and the specific declaration of property placed in a trust. It also institutes a sui generis levy applicable where there is no correct declaration for Wealth tax purposes of assets ad rights placed within a trust.

There are three specific Instructions :

The first reiterates the statutory definition, does not condescend to detail and sets out the legal framework of the trust taxation régime. It specifically excludes certain types of trust, settled by corporates, or fund structures from the main declarative obligations, stating however that units or shares in such funds will of course be considered property in their own right.

It is to be stressed that the Hague Convention specifically excludes trusts constituted by court decision from the Treaty Definition, and therefore these may not be covered by the Tax definition. The Hague Convention also excludes trusts arising by operation of law, or which are not reduced to writing.

The Instruction also admits that, if any vehicle or arrangement falls outside the definition, at least according to the Instruction, it cannot be considered a trust and the consequences are that it, the settlors trustees and beneficiaries cannot be taxed as such. Pension funds managing employee rights will also be exempted, although it remains as yet

[2] *This is important, as in reducing a trustee to the position of a mere manager, not owner, the Tax definition is therefore open to challenge.*

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unclear as to whether Private Pension Funds in a trust format can escape the régime, whether for wealth tax or for succession duty.

The Instruction generally takes the position that corporate settlements, including Employee Pension Plans are not within the scope to the instruction. However that generalisation is not to be trusted as an absolute in this context.

However, the Instruction has the temerity if not a bare faced falsehood, to assert that the definition reiterates in substance the definition of a trust contained in article 2 of the Hague Convention of 1st July 1985 concerning the law applicable to trusts and their recognition, but- admits that the Convention has not been ratified by France. Any serious reading of the Conference documentation and preliminary work would reveal that the definition in article 792-0 bis bears some but not real substantive resemblance to the heads of criteria that the Convention lays down for determining whether a foreign arrangement contains the necessary criteria for recognition as to its full effectiveness in the host state. It is interesting that the French tax definition turns the conventional verb "administrer", meaning "manage" into a substantive "administrateur" i.e. "manager". That in essence is where the French definition separates itself from that of the Hague Convention which it is attempting to exploit.

« Cette reprise ne conduit pas pour autant à introduire le trust en droit français mais permet seulement la qualification de structures étrangères de trust au regard du droit fiscal. » in other words, if the foreign arrangement or set of relationships does not fall within the deviant definition, it cannot be a trust. The fact that the French definition has gone further than article 2 in inserting "l'ensemble", ie "the set" of legal relationships, rather than the conventional phrase which refers to "the legal relationships", is a further cause for concern. This use of the term "ensemble" or "set" was a draft proposal from the Foreign and Commonwealth Secretariat that the Hague Conference, including France, considered and rejected early in the work as an inadequate definition. It is a brazen attempt to have the trust treated as a set of agency agreements, which also was rejected by the Hague Conference as it was accepted that a trust was neither contract nor mandate.

There is no indication of whether the term "bénéficiaire" is limited to its French sense, or incorporates the term as deployed in the foreign legal context. Whilst the reference to the Hague Convention will inevitable be used to apprehend unvested members of a discretionary class, it will doubtless also be used by the administration to attempt to apprehend discretionary and therefore Accumulation and Maintenance trusts by reference to the Conventional phrase "dans un but determiné" "for a specified purpose". It will become apparent that the Hague classification definition is an inadequate hook upon which to hang a fiscal definition with sufficient certainty, particularly given the linguistic compromises in the two official languages, which in effect to not hold the same meanings in some important areas..

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It is therefore still possible that the members of a non-specific discretionary class may fall outside the definition. However, as the definition of "trust" includes those trusts set up for a specified purpose, that may not be conclusive as to whether the trust is a "trust" or not. If the French administration are to attach the term bénéficiaire to its Hague equivalent, "beneficiary", then discretionary beneficiaries might be caught, and certainly will be once gratified.

The Instruction has the merit of admitting that if a vehicle falls outside the definition of a trust, it is not to be treated as such. Quite whether English trusts of land are therefore caught or not will be determined in practice, as there is no real administration involved in these, in the French sense of the term.

What is equally interesting is that the instruction is at pains to point out that a dismemberment –usufruit or droit d'occupation and nue-propriété - is not a "trust".

The First Instruction may be found at :

BOI-DJC-TRUST : Dispositions juridiques communes - Définition du Trust

The second addresses specifically droits d'enregistrement, being DMTG and the consequences of assets being placed in trust.

BOI-ENR-DMTG -30 : Enregistrement - Droits de mutation à titre gratuit - Biens mis en Trust. It does not specifically address the declarative issues related to these taxes, the declarations of "existence modification and extinction", which are addressed in the third instruction at § 270 et seq.

The third addresses Wealth tax and the levy declarations, and includes the current declaration requirements for both the DMTG (§310) now baptised as the "declaration événementielle", and the Levy (§350). It also confirms the penalties and that both the Constituant, and the bénéficiaires deemed as such, after the settlor's decease are jointly liable with the trustees for any declaratory default : the higher of €10.000 or 5% of the value of the trust assets :

BOI-PAT-ISF-30-20-30

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The administration were content simply to leave the drafting ambiguity (perhaps "gaffe" would be more appropriate) in the decree, a sad reflection on the education of the French civil servants drafting it, until they confirmed that trustees of trusts existing on 31st July, as opposed to those existing but modified or extinguished between 31st July 2011 and 15th September, 2012 also benefitted from the extended declaration period for the "déclaration événementielle" to 31st December, 2012.

However, those trusts settled modified or extinguished after 15th September, 2012, only have one month from the date of the event in which to file that declaration.

A further point, the First Instruction admits that the prior rules and caselaw applicable to trusts in existence prior to 31st July, 2011 remain applicable to those trusts for situations prior to that date. It is also unlikely that the administration will be able to entirely rewrite history from this new perspective for those trusts, although for the purposes of deceases after 31st July, 2011 the new rules will be applicable.

The only manner in which this new methodology can be addressed is with a cool head, seasoned with a sense of pragmatism and timely reference to both the Hague Convention and its timeline of preparatory work. It is only in that manner that the French administration can be brought to the realisation in each case that they are dealing with a form of property management institution which is not in itself a mechanism for fraud and evasion.

Further commentaries on these will be published on this site. Any trustee needing information or advice more rapidly is invited to contact Peter Harris at Chambers on oc@overseaschambers.com or on + 44 1534 6258779.

Overseas Chambers