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# Estate planning in France for US citizens : EU regulation and its tax consequences

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# THE NEW EU REGULATION SINCE AUGUST 2015

## Reminder : the former rule

Prior to August 2015, the former rule was to apply the French inheritance law for real estate property located in France regardless of the citizenship of the decedent and of his place of residence. The rest of the assets, movable property such as bank accounts, stocks, furniture, etc, were devolved according to the law of the country of residence of the decedent.
As a consequence, the French forced heirship system (*réserve héréditaire*) that creates an enforceable right for the children to inherit, was always applicable over the transmission of a French property.

## The new rule

In application to the new EU law, there is no distinction anymore between movable and immovable property. The decedent's estate will be governed according to only one law : the law of the country of residence.

## Choosing the law applicable to the estate

The revolutionary aspect of this regulation is the new possibility to choose the law applicable to the estate. By drafting a will, one may designate his law of citizenship to apply, instead of the law of the country of residence.

## EU regulation for US citizens

Even though this might seem counter-intuitive, this EU regulation must be used, in France, whatever the citizenship of the decedent is. Therefore, US citizens are authorized to designate, by will, their own law.

## French forced heirship system

In application to the French inheritance law, the children are entitled to receive a share of the estate of the decedent, in application to the *réserve héréditaire* (forced heirship system). Thanks to the choice of law that the new EU regulation allows, it will now be possible to avoid the application of the *réserve héréditaire* by choosing a law that doesn't create such claim for the children.

For instance, a US citizen living in France and owning a piece of property in PARIS will now have the choice to select by will the law of his US state and to bequeath all his property in full ownership to his spouse.

However, it is not possible to predict yet if a French Court would one day decide that the French forced heirship system is a matter of public order, in order to try and reinstall it over the French based property. A prediction seems quite obvious though : the more French the situation will be (citizenship of the decedent, of his heirs, assets located only in France, etc), the higher the risk.

# ESTATE AND GIFT TAX

## International taxation

The EU regulation is of no effect from a tax law standpoint. The decedent can't elect the tax law applicable to the estate.The former system is still in effect and the French-US estate and gift tax treaty will be used.

## Tax basis

According to this tax treaty, the French estate tax will be schematically payable over the entire worldwide estate, if the decedent was a French tax resident. (The tax paid in the US over US based property will be allowed in deduction to the French tax).

## Inheritance tax

The French estate tax system actually works like an inheritance tax : depending on whom inherits, the taxation will differ. The closer a relative the heir is, the lower the tax will be.

## Tax credit and tax exemption

The estate tax is not payable on the first Euro of the estate.

-> The children start paying the tax after deducting a 100.000 EUR tax credit on their share.

-> The spouse is fully exempted of paying any estate tax, with no limitation.

-> Charitable organizations, if recognized as such by the French tax administration, do not pay any estate tax.

## Tax rate

The tax rate is a progressive one and varies depending on how big the estate is.

If the share received by each child, after deducting the tax credit, is less than 550.000 €, the rate is 20%.

If the inherited share exceeds this limit, the tax rate will be 30% on the excessive amount up until 900.000 €.

Over this limit, the rate will rise to 40% and even 45% after 1.8 M € per taxable share.

## Examples

**1°** Robert SMITH is a French tax resident and dies leaving his spouse and three children. Under his will, the law applicable is the US law of his home state of California and the spouse is to be his sole heir. His estate is worth 500.000 €.

The spouse will receive the entire estate and **no estate tax** will be due in France, thanks to the tax exemption.

**2°** Robert SMITH dies in the same conditions but under his will his spouse is to inherit only for the usufruct (life interest). She is 70 at the time of death.

The spouse's usufruct is worth 40% of 500.000 = 200.000 EUR for taxation purposes. **No tax will be due** on this amount, thanks to the spousal exemption.

Each child will receive 1/3 of the rest = 100.000 EUR. Thanks to the tax credit, no tax will be due on the children' share. Therefore, **no estate tax** at all will be perceived.

**3°** Robert SMITH dies in the same conditions, but leaves an estate of 1 M €. His spouse is 92 yo at the time of death and inherits for the usufruct only.

The spouse's usufruct is worth 10% of 1 M = 100.000 EUR for taxation purposes.
No tax will be due on this amount, thanks to the spousal exemption.
Each child will receive 1/3 of the rest = 300.000 EUR. After deduction of the tax credit, the tax rate if 20%.
The tax liability by child will be 40.000 EUR. **The global tax liability will be 120.000 EUR**.

## Reducing the tax liability

The key to improving the tax efficiency of a transmission is to anticipate through gifts.

Hence, you may take advantage of :

- The reconstitution of the tax credit that reappears every 15 years,
- The paiement of the tax on the value of the property at the time of the gift, which is likely lower than the value at the time of death,
- The deduction from the tax basis of the value of the usufruct (life interest) that is retained by the donors.

Example: Mr and Mrs ROBINSON own a property that is worth 1M €. They are 68 and 70 yo and have three children. In order to reduce their tax lability, they give the *nue-propriété* (remainder interest) to the children and keep the life interest (*usufruit*) for themselves. After deduction of the value of the usufruct (400.000 €) and of the tax credit (100.000 x 2 x 3 = 600.000 €), **no gift tax will be due**. At death, the property will be automatically owned by the children, without paying any fees or estate tax.