

## Joint ownership of property in France

### Introduction

French law applies to the disposal of real estate situated in France upon the death of the property owner. Furthermore, French law does not permit complete freedom of action on the disposal of real estate assets on death. In such situations 'reserved heirship' rules apply whereby the children of a marriage or civil partnership have absolute rights of inheritance over a protected percentage share of the estate of a deceased parent. For example, for an only child, 50% of the estate must be reserved to that child; for two children 1/3 is reserved for each child. In the latter case this leaves 50% of the estate available and freely disposable by the parent and in the former case 1/3 will be freely disposable.

This law applies to all property holders owning real estate in France whatever their nationality. It is important therefore that both foreign residents and non-residents owning real estate in France are aware of this rule of French public policy when deciding on the method of holding real estate in France.

There are three different methods of multiple ownership of property in France:

1. *En indivision*
2. *En Tontin*
3. Purchase of the property by a company *Société Civile Immobilière (SCI)*

### 1. **Ownership en Indivision**

In English law '*en division*' is similar to a 'tenancy in common'. It is the most common method of joint ownership in France. The property is purchased by two or more persons, with each one holding a share (known as a 'part') corresponding to their investment in it. For example, a couple may purchase in equal parts (50/50) while in cases where there are more than two purchasers, it would normally be in proportion to the amount each party has contributed to the financing of the purchase e.g. 60% / 20% / 20%.

If the parties wish to hold the property in equal shares, but with different contributions, it should be made clear in the purchase deed that the larger contribution is not a gift, but a loan in order to avoid potential future complications with the French tax authorities concerning the *droits de donation* (gift tax).

This issue may also become important should a couple later separate or divorce. Unless, at the time of purchase, the differing contributions of each party are reflected in the purchase deed, the property will be considered held in equal shares by the holders and the sale proceeds after divorce or separation will be divided equally between the parties.

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One of the principle features of *indivision* is the decision making process that goes with it so that all holders of the parts are entitled to full participation in any decision making in relation to the property. This may be of little importance for a cohabiting couple, but it may easily present complications where several unrelated parties hold shares in the property or where the property is held by several beneficiaries as a result of a succession. In such circumstances the law stipulates that any decisions affecting the property must be made by at least a two-third majority of the property holders unless one or more of them can demonstrate to the court that it is in the overwhelming interests of the *indivision* that a specific type of action be taken. For this reason it is common for part-holders to agree a *convention d'indivision* (management agreement).

Even where one property holder has a two-thirds or more share in the ownership of the property, this does not grant the majority part-holder the automatic right to do as they wish with it. In all decisions concerning the property a fairly strict and lengthy legal procedure applies, especially regarding its sale. The *notaire* involved in the sale is responsible for ensuring that minority interests are properly heard.

If there is deadlock between joint part-holders, an application to the court will be required for an order for the sale of the property. These proceedings may take several years to be heard and either side will have an automatic right of appeal.

A holder of part of the property may dispose of it by sale or gift. Where disposal is by sale, all the existing part-holders have a right of pre-emption; this rule does not apply to disposal by way of gift.

Property may be held in *indivision* either by married couples or civil partnerships (*Pacte Civile de Solidarité - PACS*), or between separate unrelated part-holders.

### ➤ **Married/Civil partnership couples *en indivision***

With regard to rights of inheritance, *indivision* has historically been problematic for the surviving spouse who was often obliged to sell the matrimonial home at the request of beneficiaries (often the children of the marriage) entitled by law to a share in the estate of the deceased (see above 'reserved heirship rule').

In recent years the situation has improved somewhat and the surviving spouse is now afforded a relatively large degree of protection by the law. However, the children of the marriage as 'protected heirs' are granted by law a reserved part of their parents' estate. There is no derogation from this rule.

However, although the surviving spouse may not inherit the totality of the property upon the death of the other spouse because of the 'reserve' rule, today, the survivor has the right to remain in the property for life as long as it is their principal home. This is the case regardless of the proportion of the property which belongs to the child or children of the deceased spouse due to the reserved heirship rules.

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If the deceased has children by a previous marriage or relationship, then they too are entitled to a share in the deceased parent's property in the same way as children of the last marriage. Obviously this may be a source of conflict between family members however it will not weaken the legal position of the surviving spouse who will have a life interest in the property.

There is a spouse exemption with regard to *droit de succession* (Inheritance tax - IHT), but this does not apply to the children. However, in France the amount of IHT due by a beneficiary depends on the degree of blood relationship between the deceased and the beneficiary. As children are the closest in blood line to their parents the tax allowances available are the most generous.

The purchase of property *en indivision* is a common method of holding property for married couples. All marriages in France are covered by one of three *régimes* (pre-nuptial agreements). The *régime de communauté universelle* allows the spouses to leave the part of their estate identified in the marriage contract to the surviving spouse by means of a clause *d'attribution intégrale*. If however the spouses have children by previous relationships, such a French marriage *régime* will effectively disinherit children from outside the marriage who are not the children of the last spouse to die. *Notaires* are therefore reluctant to allow couples with children outside the relationship to enter into such a marriage contract. In such circumstances the *notaire* is under a duty to notify such children of their position so that they may contest the marriage regime. The children then have a three month period in which to make their opposition known and challenge the marriage regime in court. The court will have to decide whether the matrimonial regime is in the best interests of the family.

Should the *notaire* fail to notify the children, they may bring an "*action en retranchement*" for the annulment of the matrimonial regime, or, should they only become aware of the regime after the death of their parent, they may seek a proportion of the inheritance through a court action. It is possible for a child of a former marriage or relationship to renounce their right to bring *l'action en retranchement*, on condition that on the death of the surviving spouse they will retain their rights to an inheritance in the same way as the children of the existing marriage. This is done by way of a *pacte successoral*" (family inheritance agreement) collateral to the marriage regime.

A simple alternative to *indivision* is to purchase the property through an *SCI* (see below).

## ➤ **Unrelated Persons *en Indivision***

If the property holders are unmarried or in a civil partnership, then the approach to property held on *indivision* will be different and often more complex.

Upon the death of one of the part-holders with children, the property of the deceased will pass to the children who will share the property *indivision*. They may then force the sale of the property and a surviving part-holder will have limited rights.

There are alternative solutions to this situation depending on the individual circumstances of the parties but they are generally based on granting a 'life interest' in the property to the surviving part-holder.

This may be done through a *testament* (will) or *donation* (gift). In this way the heirs of the deceased part-holder will receive the reversionary freehold interest in the property while the surviving part-holder will have a life interest in the property. The drawback is that while the life interest protects the surviving part-holder there will be a potential inheritance tax liability on the value of the life interest, currently charged at 60% of the value of the life interest after deduction of any personal allowance available.

Of course this tax imposition will not apply if the surviving part holder is married to the deceased or is in a *PACS* and has granted the co-part holder preferential rights to the property; in both these cases the spouse/partner tax exemption will apply, although this will mean that compensation must be paid to the heirs.

It is essential when purchasing property in such conditions that provision be made to take into account events such as separation or death of one of the part-holders by means of a *convention d'indivision* (tenancy in common agreement), drafted by a *notaire*, which will normally be valid for a period of five years unless stipulated to be made for an indefinite period.

A *convention d'indivision* cannot override the entrenched inheritance rights of the children, or avoid inheritance tax, however subject to these two exceptions it will clarify the situation in the event of separation or death. Such agreement should include a clause known as a *faculté d'acquisition ou d'attribution de l'indivisaire survivant*, to protect the survivor so that the part of the property belonging to the deceased will be held on life interest for the survivor, as long as adequate compensation is paid to the heirs.

Such an agreement will also set out the terms of the management arrangements for the property during the lifetime of its part-owners. This will include the appointment of one of them as the property manager.

## ➤ Conclusion

*Indivision* is an appropriate method of holding property for married or *PACS* couples. If however unmarried parties or unrelated part-holders purchase property *en indivision*, it may well lead to future complications on disposal following the death of one of the part-holders especially with regard to the French reserved heirship rules which automatically apply on death.

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## 2. *Ownership en tontine*

A *tontine* clause is used to avoid the reserved heirship rights of children under French law, so that no part of the property will pass to them during the lifetime of any of the existing part-holders.

Under *tontine* the law does not recognise that each part-holder has a separate share in the property as is the case on *indivision*. So where a property is purchased by a couple *en tontine*, upon the death of the first, the surviving spouse/partner will become the sole owner. This is similar to the rights of survivorship in English law where the parties purchase property as beneficial joint tenants where each party in effect owns the whole of the property. If one of the party's dies the property automatically passes to the surviving joint tenant(s) under the rights of survivorship.

A *tontine* clause is not often used in France because it may have *droits de succession* (IHT) disadvantages, and it also disinherits children not of the blood line. These tax disadvantages however are less important today for married or civil partnership couples.

### ➤ **IHT (*droits de succession*)**

The *tontine* gives security of tenure to the surviving partner in a non-married, non-civil partnership relationship. However, as the parties are considered to be unrelated persons, there will be a liability to IHT at the rate of 60% on 50% of any property held by the couple which is valued over €76,000.

Such parties should, as an alternative, use an *SCI* (see below) to purchase the property directly or purchase it through an *SCI* containing a *tontine* clause in its by-laws. In this way the parties would pay *droit d'enregistrement* (stamp duty) on the transfer of the shares, but would avoid paying IHT.

For married and civil partnership couples, there is a tax exemption. The tax liability arises when the property is inherited by the children or nearest relatives. However there are tax allowances available to children and a 'tapering relief' tax allowance for other relatives depending on the degree of blood relationship to the deceased.

### ➤ **The Rights of inheritance**

Where a couple already have children from previous relationships, the *tontine* clause will disenfranchise one side of the family. Thus, on the death of the surviving partner, only the progeny of the deceased will have an automatic right to inheritance. For example, Fred has two children by a previous relationship. He and his new partner Maggie buy their French home *en tontine*. They later have a child, Susan. If Fred is the first to die, his partner Maggie will inherit the property. When Maggie dies, the property will pass to Susan as there is no blood relationship between Fred's children

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and Maggie. If Maggie dies first, and Fred inherits the property, the children by the previous relationship as well as Susan will inherit the property.

In such cases it will be necessary to make separate provision for children from previous relationships by gifts during lifetime or other means.

## ➤ **Further considerations**

There are also other practical disadvantages of the *en tontine* clause:

- It cannot be waived without the agreement of both parties;
- In the event of divorce the property will remain in the joint names of the parties unless they can reach agreement on its disposal;
- In the absence of such agreement, the property will remain *en tontine* until the first to die, at which time it will transfer to the survivor;
- Using such a clause may also make it difficult to obtain a mortgage or loan on a property, although this may be circumvented by arranging separate loans under the names of each of the part-holders.

Because of the nature of ownership *en tontine*, it will serve to protect the property from other creditors who will have no recourse against it apart from a bank with a mortgage on the property.

## ➤ **Conclusion**

Purchase of property *en tontine* is viable only if the intention of the parties is that the survivor inherits the totality of the property. In French law today, the surviving spouse already has a high level of legal protection and a French marriage regime can work just as well as a *tontine clause*, giving rights over the whole of the estate and not just the property.

For unmarried couples, purchasing a French property *en tontine* is a useful way of protecting the surviving partner, especially if accompanied by a civil partnership so as to avoid any liability to IHT. However, in either situation the impact of the *tontine* clause will disenfranchise children born outside the relationship.

In these circumstances, for non-resident unmarried and non-civil partnership couples who have children from previous relationships, it would be more appropriate to purchase property through an *SCI*.

### **3. Purchase of the property by a company: Société Civile Immobilière (SCI)**

An alternative to the purchase by individuals is to use a corporate vehicle to carry out the acquisition. In France an *SCI* is a corporate structure which is designed to facilitate the easy acquisition and management of property.

An *SCI* is a French 'company' (*société*), constituted for the ownership and management of 'real estate' (*immobilière*). '*Civile*' means that it is a 'non-trading' company, thereby distinguishing it from a company set up to pursue commercial objectives.

The *SCI* will have a distinct legal identity from that of its shareholders. However, normally it has no separate tax identity and is fiscally transparent.

Where an *SCI* is used for the purchase of real estate, the owners effectively become occupants of the property owned by the company.

The *SCI* may hold more than one property, including principal and secondary homes, as well as letting properties.

Many French and international purchasers choose to buy property through an *SCI* because of the advantages it offers over the other two forms of ownership:

- purchasing property by multiple persons
- providing stability and continuity in the ownership and management of property
- facilitating the transfer and ownership of property
- avoiding the constraints of French IHT
- some tax advantages
- protecting the property from business creditors

One of the main reasons why an *SCI* is used is because it is probably the most suitable form of ownership for an extended family, or a group of co-owners.

For a couple who are neither married nor in a civil partnership, it also offers advantages in relation to French inheritance laws and reserved heirship (see above).

The *SCI* offers a simple method for two or more persons pooling funds to buy property in such a way that ownership is clearly defined in accordance with the contribution of each owner.

With regard to decision making, the *SCI* provides greater flexibility than other ownership structures. For example where several people are buying a property, an *SCI* can provide for a decision-making procedure less strict than the two-third majority required for *indivision*. Furthermore it can also provide a method of selling the property, which would not be available *en tontine*.

If for example a decision has to be made concerning major repairs to the property, or about letting the property, then the *statutes* (by-laws) of the *SCI* could provide that a

simple majority decision is required, or that decisions could be delegated to the *gérant* (manager) or of the company.

The by-laws of the *SCI* will also regulate the cost sharing by the owners for repairs to the property and any other management costs.

It will also fix the sharing of any rental income, should the property be let.

It may also organize the periods of occupation of the property by the different owners in a similar way to a timeshare.

The *SCI* presents such advantages during the lifetime of the ownership, but there are also great advantages to the *SCI* following the death of one of the shareholders because of the French inheritance laws (see below).

Therefore the *SCI* clearly offers greater flexibility in the management arrangements of the property.

The downside is that any majority decision making structure such as an *SCI* will inevitably mean that the views of the minority are less well protected.

If there are two shareholders in the *SCI* each holding 50% of the capital of the company then there is always the possibility of deadlock in decision making.

Furthermore, if the shareholders decide that some or all decisions must be made unanimously, then this will inevitably lead to complications. For couples, this may not be a real problem but for unconnected parties such as investors, they may find themselves locked in.

Therefore it is most important to consider what would happen in the event that there was disagreement between the shareholders of the *SCI* and careful drafting of the by-laws of the *SCI* needs to be undertaken to anticipate such possibilities as a fall-out between shareholders.

## ➤ French succession laws

One of the principle advantages of buying French real estate through an *SCI* is to avoid French inheritance rules on reserved heirship (see above). If an *SCI* is set up to hold a property in France then the owners will hold shares in the *SCI* and the *SCI* itself will own the property. Therefore upon death only the shares will change ownership and the property will remain in the *SCI*. French law considers shares to be personal property and they will pass in accordance with the succession laws of the country of domicile or permanent residence of the deceased. If the deceased was ordinarily resident in the UK this will mean that English law applies so that the shares

can be bequeathed to whomever the deceased wishes thus avoiding the onerous French succession rules. There will of course be French CGT and IHT liability.

## ➤ Formation & Management of an *SCI*

An *SCI* is quick and easy to set-up, only two shareholders are required and their nationality is irrelevant. The *SCI* can be managed by one *gérant* (manager) who does not necessarily have to be a shareholder.

There is no fixed minimum value of shares and no minimum amount of capital is required for an *SCI*; the amount of capital usually reflects the value of the property being acquired, but there is no requirement to pay up in full upon incorporation.

If successors inherit property, particularly within families, they may sell their shares in an *SCI* without forcing the other shareholders to sell the property as would be the case for the other forms of real estate ownership (see above).

In France, it is not unusual to find an *SCI* used to hold property, and a French commercial company (*SARL*) operating a business from that property. Any rents collected by the *SCI* from the business exploiting its property are shared between the shareholders after deducting costs. This will provide a supplementary source of revenue, which will be taxed as part of the *SCI* shareholders' personal income.

Furthermore an *SCI* can offer protection during insolvency proceedings. If the business occupying the *SCI* premises goes into liquidation, none of the business' creditors will be able to seize the property for repayment of their debts as the business and the *SCI* are two separate entities.

## ➤ Taxation

Under Article 8 (1) of the French General Tax Code, an *SCI* whose sole purpose is to purchase, manage and subdivide a property between its members, is transparent for tax purposes and will therefore not usually be liable to French Corporation Tax (unless the property is a furnished letting). Instead, the shareholders of the *SCI* are treated as individual taxpayers owning a share of the underlying property personally. On disposal shareholders will be assessed individually to Capital Gains Tax (CGT) at 16% or the non-resident 33.1/3%. Share transfers *inter vivos* will be liable to CGT, calculated on the basis of the increase in value of the underlying property, in proportion to the size of the shareholding plus stamp duty at 5%.

Although transparent for tax purposes, an *SCI* is still considered by the French tax authorities as a legal entity, with *parts* (shares), and *statuts* (by-laws) setting out the company's objects and management structure. The by-laws may be drafted to allow for qualified majorities for control, restriction on rights on disposing of shares etc. An *SCI* has no board of directors and is managed by a *gérant* (manager), who may be, but need not be, a shareholder in the *SCI*. The manager will have capital accounts

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prepared and various other returns which need to be filed annually. *SCI*'s require a certain amount of administration and compliance procedures.

## ➤ **Considering the *SCI* and *indivision***

In recent years the law relating to *indivision* has become more flexible so that where originally unanimity was required for decisions on the property, now a two-thirds majority will suffice. The original rule on unanimity was a key factor in the introduction of the *SCI* ownership structure as an alternative to *indivision*.

Furthermore, owners who hold a property on *indivision* may now also enter into a *convention d'indivision* (tenancy in common agreement) concerning the management of the property similar to that available through an *SCI*.

However the drawback to such an agreement is that it has to be renewed every five years, and any single '*indivisaire*' is entitled to go to court to terminate the *indivision* and for the property to be sold "*nul n'est tenu de rester dans l'indivision*". If however, the property is held through an *SCI* an enforced sale would be unnecessary.

In addition, on the death of one of the *indivisaires*, the property will be split again between the new successors in title, making decisions concerning the property even more difficult to obtain.

If one or more of the remaining part-holders uses the right of pre-emption to buy out any other *indivisaires* then it will be necessary to go through a property transfer procedure through a *notaire*, which is unnecessary in an *SCI*, where such a transaction can be accomplished by the transfer or transmission of the shares in the *SCI*.

## ➤ **Conclusion**

In summary, in France the *SCI* is tax neutral and puts its shareholders in the same position as they would be if they owned the property in their own names. However, legally, they own shares rather than land. These shares pass in accordance with the domicile of a deceased and not the *lex situs* so that the French reserved heirship law is avoided and the probate laws of the country of residence of the deceased apply.

Non-resident shareholders in an *SCI* are not taxed in France as the shares are considered personal assets and are therefore taxed in the country of the shareholder's residence.

Setting up an *SCI* does not trigger any taxation but filing requirements such as an annual report must be followed. Only if the *SCI* is rented out will it show any profits. An *SCI* is liable for Capital Gains tax, however, as it is considered a transparent company, taxes will only be declared if the property held by the *SCI* is let for profit.

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For further information: [www.notaires.fr](http://www.notaires.fr)  
[www.impots.gouv.fr](http://www.impots.gouv.fr)