SIMONARD & SOREL
A V O C A T S

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Tax Talk 2012 ©

US Tax Law Developments

In 2011 the US tax law news was that there were very few new tax laws passed. Many fiscal questions were left unanswered, the only thing we do know is what is on the books now, and that change will be coming soon. The US is also looking for revenues wherever they might be found, and it's possible that some decision makers stateside see citizens and Greencard-holders residing abroad as a base without a solid voting or protesting block. Do not hesitate to write to your representatives to let them know you are still their constituent.

FATCA and other Foreign Taxpayer Profanities

The Foreign Account Tax Compliance Act (FATCA) enacted in 2010 is going into effect for tax year ending 12/31/2011. This act requires all US RESIDENT taxpayers with more than $50,000 at the end of the year or more than $75,000 at any time during the year in « aggregate specified foreign financial assets » to report them on form 8938. If you are a FOREIGN RESIDENT the thresholds for filing the form are $200,000 for the last day of the year and $300,000 at any point in the year. These thresholds are for unmarried or married-filing-separately taxpayers, if you are married filing jointly, these thresholds are doubled.

If you are not required to file a tax return, you are not required to file form 8938. FATCA and form 8938 do not replace form TDF 90-22.1, Report of Foreign Bank and Financial Accounts whose filing threshold remains $10,000 at any time in the year in total in foreign bank and financial accounts.

The details of what exactly is a « specified foreign financial asset » are quite technical, but in general, if it's not something the US already knows about, then it's probably included. Examples include Assurance Vies, French Trusts, shares in French SCIs, foreign pension and deferred compensation plans, bank accounts, and shares in foreign partnerships and corporations. Assets already included on the forms 3520 (trusts), 3520-A (trusts), 5471 (corporations), 8621 (PFICs), 8865 (partnerships), and 8891 (Canadian retirement plans), do not need to be included in the total value for the form 8938, but do need to be specified.

CSG/CRDS and the IRS

From tax year 2008 and forward, CSG and CRDS taxes have been treated by the IRS as non-creditable and non-deductible social contributions. The IRS made this decision somewhat on its own, as there were differentiating court cases, however no decisive case has passed in the taxpayer's favor. Since mid-2010 the Paris tax community has seen a significant increase in IRS examinations concerning foreign tax credits, form 2555 (§911 exclusion), and compensation. Please be advised that CSG and CRDS taxes are not foreign tax credits for US tax purposes. Additionally, all salaries should be declared at their gross or « brut » values translated into dollars on US tax returns. If our firm prepared your returns for these years, these calculations were made in accordance with the IRS's rules with the information you supplied to us.

The average IRS auditor is often overburdened and not a specialist in foreign tax laws, which can result in errors. If you receive an examination notice or an assessment you do not understand or believe is incorrect, please let us know as soon as possible. Many of these examinations have resulted in no change from what was previously reported, but if a response to the examination notice is not submitted timely, the IRS can proceed to collections very rapidly.

Estate and Gift Taxes, same as prior year

In last year's tax talk, the big question on the US side was the Estate and Gift Tax regime. As explained in that issue, the extension of the Bush-era rates and exemptions were effective for both tax years 2011 and 2012. So just to repeat and give any inflation adjustments, for estates of those dying in and gifts made in 2011 and 2012, there is an exemption from the Estate and Gift Tax of $5 million and $5.12 million, respectively. Above those amounts, the estate and gift tax is a flat 35% rate. The annual gift tax exclusion (per giver per receiver) is $13,000 for both years and please be reminded that the exclusion for gift and estate taxes is reduced by prior years' gifts.

For tax year 2013, the rates and exclusions revert back to the statutory amounts of a maximum 55% tax rate and maximum exclusion of $1 million. There is considerable doubt that the statutory rates will not be repealed, changed, or some other patch applied, but this is the situation at present. Therefore, if you have considerable assets in the United States that you would like to transfer to your heirs and have not already planned how to do so, 2011 and 2012 are tax favorable years. Keep in mind that French Estate and Gift Taxes could be payable instead of or in addition to US taxes, so please consult with us before making any significant transfers.

Foreign Earned Income Exclusion

The Foreign Earned Income Exclusion has been inflation adjusted for the 2011 and 2012 income tax years to allow maximum exclusions of $92,900 and $95,100, respectively, of Earned Income for those who are considered tax residents of a foreign country under either the Bona Fide Residence Test or the Physical Presence Test.

Other General US Tax Information

The legislative changes made in 2010 continue to be effective for 2011, these include:

- No increase in rates at all income levels, with the maximum income tax rate remaining at 35% and maximum qualified dividends and capital gains rates of 15%.
- The itemized deduction and personal exemption phase-outs are repealed for 2011 and 2012.

French Tax News

Income Tax rate

There will be no changes in the tax bands used for the calculation of the 2011 income tax for French tax residents (same flat rate of 20% applying to non French residents):

- Up to €5,963 : 0%
- €5,964 to €11,896 : 5.5%
- €11,897 to €26,420 : 14%
- €26,421 to €70,830 : 30%
- Over €70,830 : 41%

Social Charges rate

From Oct. 1st 2011, French social charges have increased from 12.3% to **13.5%**.
Please note that non residents are not subject to social charges.

New assessment of the Capital Gains Tax from Feb. 1st 2012

Under the current law, the sale of French secondary residences as real estate is totally exempt from Capital Gains Tax after 15 years of ownership. Under the new law the gain will be totally exempt from tax after 30 years of ownership. The new Capital Gains Tax will be applied to sales completed as of 1st February 2012.

Allowances

A summary of the new allowances is as follows:

- The fixed allowance of €1,000 disappeared on Sept. 19th 2011.
- No allowance for the first 5 years of ownership.
- Between 6 and 17 years of ownership: 2% allowance per year.
- Between 18 and 24 years of ownership: 4% allowance per year.
- Between 25 and 30 years of ownership: 8% allowance per year.

Until 1st January 2011, the rate of Capital Gains Tax has been fixed at 19 % + social charges at 13.5%, for a French tax resident.

Non French tax residents are not subject to the social charges, but they are subject to French Capital Gains Tax at different rates depending on where they are resident:

- 19 % if they are resident in an EU Country or Iceland, Norway and Liechtenstein.
- 33.33 % if they are resident in a country other than those above mentioned.
- 50% if they are resident in a country considered by France as an “uncooperative State”

New calculation of the Wealth Tax for 2012

Only people with a net taxable asset superior to **1.3 million euro** will have the obligation to submit a 2012 wealth tax declaration and pay the 2012 wealth tax.

Only 2 tax bands will be used to assess the wealth tax:

- A net taxable asset on Jan. 1st 2012 estimated between 1.3 and 3 million euro will be taxed at a fixed rate of 0.25% on its whole (no allowance)
- A net taxable asset on Jan. 1st 2012 estimated to more than 3 million euro will be taxed at a fixed rate of 0.50% on its whole.

In both cases, tax will be payable from the first euro.

For wealth between EUR 1.3 million and EUR 3 million, taxpayers will no longer file a separate return but will use their income tax returns.

Shareholders' loans held by non French Tax resident in French foreign companies

The Finance Bill also threatens higher taxes for non French tax resident owners of properties in France who have previously avoided paying wealth tax by buying the property through French or foreign companies (such as an SCI) – a company structure to which the shareholders' advanced loans, in order to reduce its taxable value.

As from 1st January 2012, shareholders' loans held by non French tax resident shareholders in French or foreign companies owning French real estate will no longer be taken into account to reduce the value when assessing the value of the shares in the company for Wealth Tax ("ISF") purposes.

Shareholders' loans held by non French-Tax residents will no longer be considered qualifying debts of the Company for Wealth Tax purposes. Currently, shareholder's loans held by a non French-tax resident are deductible when calculating the value of the company's shares for French Inheritance Tax purposes.

Registration of the sale of shares of real estate companies abroad

As of 1st November 2011 the sale of shares of companies holding real estate in France must be formally notarized in France, even if the sale takes place abroad. This notarization will trigger a 5 % real estate transfer tax ("droit d'enregistrement").

New tax treatment of Trusts in France

The 2011 French Amended Finance Bill has set out new rules for the taxation of trusts. To summarize the main changes, income retained within a trust is not taxed until distributed to a beneficiary, a new disclosure regime is introduced for trustees who hold French assets or if the settlor or any beneficiary is a French resident, and wealth tax is extended to trusts if the settlor or beneficiaries do not declare the same.

As from January 1st, 2012 and to the extent that:

- The settlor is a French tax resident,
- One of the beneficiaries is a French tax resident, or
- The trust fund includes French taxable assets,

the trustee will have to disclose to the French tax authorities information regarding the Trust, such as:

- The creation, modification, revocation and terms of the trust.
- The net asset value of the trust as of January 1st of each year.

If the required information is not disclosed to French tax authorities, a penalty of 5% (or EUR 10,000) will be charged. The trustee will be jointly liable with the settlor and beneficiaries for the payments of the said penalty.

Trust and estates will be seriously affected by the new regime with regard to gift and inheritance tax depending on the type of transfer and whether it can be classified as a gift or a succession or some other transfer as well as the relationship between the settlor and the beneficiaries.

Economic Forecast

Our economic forecast for 2011 proved remarkably prescient. Slightly better than expected employment figures didn't lead to explicit tax increases, but continued austerity measures saw unprecedented intensification of tax collection by government authorities.

The root cause of the Great Recession cannot be pinned on any individual nation. America took the first bullet in the 2007/2008 financial crisis, which it ducked by socializing private bank losses. The resulting increase in capital costs hurt weaker debtors in Europe's periphery forcing their governments to follow Washington's lead in using public money to bail out bad bank loans. A few countries suffered an outright credit downgrade fuelling a vicious cycle of rising interest rates for increasingly indebted borrowers.

Emerging markets have largely avoided the crisis lime light, but 2012 might see this changed. China's exports are driven by Western consumers whose discretionary spending is in freefall. The resulting demand contraction can devastate China's externally dependent growth model.

For the forseeable future European leaders will continue to slash government spending on the hopes that moderate GDP growth will cut deficits, shrink debt, and improve competitiveness. Even if mildly successful, such a policy would saddle China with the costs of any subsequent adjustment for the global economy.

Volatility for 2012 might be so high, that forecasts become clairvoyance. Scenarios can span the gamut of global collapse, to a Japanese style stagflation (two decades long). The 2008 financial crisis gave us FATCA. Further economic deterioration could give us Senator Levin's "Stop Tax Haven Abuse Act, 1346."

Although unlikely to make it into law, this bill is a stark reminder what turbulent markets augur. More notices from the IRS, FISC, and other national and state tax authorities questioning the extent of holdings, positions taken, and credits applied, on taxpayers' declarations.

Muscular tax collection is part and parcel of the West's approach to economic growth. Extravagant tax hikes are unlikely, but everything that an average tax officer cannot immediately grasp on a return -- such as international tax credits -- will attract closer scrutiny.