



Article 123 bis is given a new set of teeth to bite into offshore trusts' profits

The recently added Article 34 quater of the 2022 French Budget extends the scope of anti-tax avoidance rules to trust situations.

1. Article 123 bis contains measures to bring income and gains arising within certain entities within the scope of French taxation where these "belong" to French tax residents. These rules apply where, all conditions below are met:

i) An entity is established in a low tax area or jurisdiction, or in a blacklisted non-cooperative territory. As at 4 March 2021, the territories stated on France's blacklist were as follows: Anguilla, British Virgin Islands, Dominica, Fiji, Guam, Palau, Panama, Samoa, Seychelles, Trinidad & Tobago, US Virgin Islands, and Vanuatu.

A "low tax regime" is defined as one resulting in a tax liability which, on average, is half or less compared to the average French corporate tax liability. The current French general corporation tax rate is 26.5%, reducing to 25% in 2022.

ii) Over 50% of its assets consist of financial assets.

iii) The French resident taxpayer, directly or indirectly, holds at least a 10% of the entity's financial and/or voting rights. The 10% holding threshold is automatically deemed to be attained where an individual has transferred assets or rights to an entity in a blacklisted jurisdiction. **Article 34 quater of the 2022 French Budget extends this presumption, to settlors or "deemed settlors" of trusts. Adding that, a trust's irrevocable and discretionary nature cannot be solely relied upon as evidence to the contrary. (N.B. - The term "deemed settlor" refers to the beneficiaries where the settlor is deceased.)**

2. No doubt this addition aims at counteracting the rulings which so far, have precluded several attempts by the French tax administration from applying the look-through taxation to irrevocable and discretionary settlements. The burden of proof has also clearly shifted to the taxpayer. Nevertheless, in our view, the look-through taxation risk was always greater in cases where the original settlor is also a beneficiary.

3. It is not yet clear whether the French tax administration will apply a minimum deemed 10% share or different apportionments. We know that when it comes to wealth tax, trust assets are equally split between the relevant parties.

4. These anti-avoidance rules do not apply to EU entities as long as the structuring cannot be treated as an artificial arrangement aimed at eluding French tax legislation. In the case of non-EU entities, Article 123 bis provisions may be avoided on the same basis, provided the entity is not in a blacklisted territory and is registered in a territory which has signed the following agreements with France:

- i) An agreement to fight against tax fraud and evasion ("*Convention d'Assistance Administrative en vue de Lutter contre la Fraude et l'Evasion Fiscales*"); and
- ii) An agreement for the recovery of taxes which meets similar conditions as set out in EU Directive 2010/24/EU of 16.03.2010 ("*Convention d'Assistance Mutuelle en Matière de Recouvrement des Créances Relatives aux Taxes, Impôts, Droits et Autres Mesures*").

Where the legal entity is established in a State or territory which does not meet the above conditions, taxation on a look-through basis shall not apply if the person domiciled in France demonstrates that the principal objective and effect of exploiting the entity, or of holding shares, rights, financial rights or voting rights therein, is not to cause the location of its profits or income to be treated as arising in a State or territory where it is subject to a preferential tax regime.

5. Where FTC Article 123 bis applies, the entity's profits increased by 25%, are taxed on a look-through basis. If the entity is situated in a backlisted territory or a jurisdiction which does not have the treaty mentioned in (i) above, the taxable profit cannot be below a set minimum return (1.18% for 2020).

6. The new measure applies from 1 January 2022. Nevertheless, depending on the case's circumstances, it may still be possible for the administration to apply Article 123 bis taxation up to the ten-year statutory limit, as well as penalties of

10%, 40% or 80%.

7. Each case needs to be considered on its own merit to fully appreciate the risks and consequences of this change. We expect that, in a number of cases, this will lead to relocations outside France.

Contacts

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