From: Jean-Marc Tirard
To: Mr Bill Lexmond
UBS AG
Chairman STEP Singapore

Dear Mr Lexmond,

As you may be aware, after many years of prevarication and three previous failed attempts, France has now adopted a fiducie. As you can see from the attached article, my opinion is that this new instrument is not particularly interesting, except in as far as it will hopefully increase interest from French quarters regarding the trust. With this in mind the French branch of Step is holding an international conference on 13th and 14th June during which the various different fiducies from around the World will be compared with the trust.

You will find herewith the preliminary programme for this conference. Would it be possible, in advance of the publication of the final programme, to circulate this to members of your branch so that anybody who is interested can mark the dates in their diary? When the final programme is published, if you do not mind, I would also like to send you some copies of that so that you can distribute it. If you agree, please let me know how many copies you would like to receive.

If you have any questions regarding the content or organisation of this event please do not hesitate to contact me.

Yours sincerely,

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The French law on "*fiducie*"– A critical view

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Unfortunately, but not unsurprisingly, the new law on the *fiducie* which was adopted by the French National Assembly on 7th February 2007 is to say the least very disappointing. The *fiducie* which has as a result been introduced into the French Civil Code is a very different institution from the trust both in substance and in form (1). From the tax point of view the so-called tax neutral regime to which it will be subject is a logical consequence of the fact that the French *fiducie* is not a trust but more a contractual relationship between the "*fiduciant"* and the "*fiduciaire"* (2). It will in fact only be a substitute for the trust in a small number of very specific transactions (3). Talk, therefore, of "French trust law" arises either from a flawed understanding of what a trust is, or from a deliberate intention to deceive.

1. The French *fiducie* is very different from the trust in spite of superficial similarities

According to one of the new articles of the Civil Code, the *fiducie* is defined as an operation by which one or more "*constituants*" transfer(s) property or property rights to one or more "*fiduciaires*" [(1)] who must hold them separately from their personal estate and manage them as defined by certain specific goals for the benefit of one or more beneficiaries. Unlike the trustee, the "*fiduciaire*" does not become the legal owner of the property rights transferred to him. These rights make up a fund of allocated assets for which the *fiduciaire* is obliged to maintain separate accounts.

The *fiducie* is set up by means of a contract which must be registered at the *fiduciaire's* local tax office within a month of its signature. The law also provides that a national register of *fiducies* will be kept. Unlike the trust, therefore, *fiducie* contracts will be public in the same way as companies.

Another essential contrast with the trust is that the "*constituant*" of a "*fiducie*" can only be a corporate entity which is subject to corporation tax. In other words neither an individual, nor a partnership, nor any legal fiscally transparent entity can set up a *fiducie*.

[1] In order to avoid confusion with the trust we have deliberately retained the French terms. Thus the rights and obligations of the *fiduciaire* are very different from those of a trustee.

The consequence of this rather strange measure is that it will not be possible to use the *fiducie* for estate planning purposes. This precaution, which did not appear in the first draft of the law, has no doubt been added at the request of the finance minister who is evidently very hostile to this kind of application. The measure is even more surprising given that one particular article of the law already expressly forbids the creation of a *fiducie* for the purpose of making a gift to the beneficiary. The creation of a *fiducie* by a *constituant* who intends to make a gift to the beneficiary would be void. Furthermore, because one can never be too careful, the tax authorities have included a measure which provides that, should anyone (notwithstanding the risk of invalidity) be foolhardy enough to constitute a *fiducie* with the intention of making a gift anyway, the tax consequences of such an act would be extremely severe (see below).

Other measures which set the *fiducie* apart from its supposed model include the following. The length of time over which property rights can be transferred into a *fiducie* is limited to 33 years. Furthermore, the *fiducie* contract can be revoked by the *constituant* subject to the agreement of the beneficiary (where he has accepted the contract). Only banks and insurance companies may hold the office of *fiduciaire*. Finally, both the *constituant* and the *fiduciaire* must be resident in the European Community or in a State which has signed a tax treaty with France containing an administrative assistance clause.

2. Under the pretext of tax neutrality the tax treatment of the *fiducie* leaves no place for tax planning

The assets and rights transferred into the *fiducie* are considered for tax purposes to remain the property of the *constituant*. Consequently, income generated by the assets and rights transferred into a *fiducie* will be subject to corporation tax in the hands of the *constituant*. For the duration of the *fiducie*, the *constituant* will be considered to have an outstanding debt redeemable from the *fiduciaire* with regard to the assets and rights transferred into the *fiducie*. The logical counterpart of this is that it has been provided that capital gains made at the time of transfer of the assets and rights into the *fiducie* are not immediately taxable. The taxation of these gains is deferred until the assets and rights concerned are sold by the *fiduciaire*. The capital gain is calculated at that time by reference to the value of the assets when they were held by the *constituant*. This deferral of capital gains tax is, however, subject to a number of conditions, including a requirement that the *fiduciaire* should be one of the beneficiaries.

Since a *fiducie* contract cannot be made by individuals the law contains no measures regarding wealth tax.

Since by definition the *fiducie* contract cannot have the intention of making a gift as its function, gift and inheritance taxes cannot in principle be due at any point, whether at its creation or at the time of transfer of the property held by the *fiduciaire* to the beneficiaries. However, in order to discourage the temptation to avoid this prohibition, it is specified that the tax authorities will have the right to impose these taxes if they can prove that the *fiducie's raison d'être* was to make a gift to the beneficiary. In this event the transfer of assets in the *fiducie* will be subject to gift tax at the higher rate of 60% and will give rise to an additional penalty of 80%. The law presumes an intention to make a gift if there is no genuine consideration for the transfer or when a benefit in kind or reduction in sale price is accorded to a third party by the *fiduciaire*.

As an exception to the above rule, VAT, professional tax and *"taxe foncière"* will have to be paid by the *fiduciaire*.

3. It will only be possible to use the *fiducie* for very limited transactions

The prohibition on using the *fiducie* for personal estate and tax planning and also for charitable purposes means that it can only be used as a mechanism for managing assets or as a security device. It is clear, therefore, that it cannot in any way aspire to compete with the trust which has an unlimited number of possible uses. In practice, if it is adopted, the *fiducie* could principally be used to replace the trust in certain financial transactions (e.g. for securitisation or defeasance) or as an independent security device (e.g. for structured financing or syndicated loans), provided of course that the economic players have as much confidence in this new concept as in the trust, which cannot be taken for granted.

4. Conclusion

The acknowledged reason for attempting to introduce the *fiducie* into French law is to compete with the Anglo-Saxon trust. However, the numerous constraints contained within the law, the fact that it is not possible to use the *fiducie* for any of the principal functions fulfilled by the trust, combined with a completely transparent tax treatment casts serious doubt on whether this objective will be achieved. It is difficult to see under what circumstances the French *fiducie* could provide an effective replacement for the trust, particularly given that the trust is extremely favourably received by the French courts[(2)]. The French legislator would probably have been more inspired in ratifying the Hague Convention on the recognition of trusts.

[2] See - in French –"Les Trusts Anglo-Saxons et les Pays de Droit Civil" Jean-Paul Béraudo et Jean-Marc Tirard (Academy & Finance)
- in English – "The International Guide to the Taxation of Trusts" (French Chapter written by Jean-Marc Tirard) (International Bureau of Fiscal Documentation)