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The Notion of Tax Domicile and Its Effect on the Taxation of Foreign Investments

The study of taxation on foreign investments gives rise to many questions, as the legislative power finds itself faced with a double problem: on the one hand, such investments must enjoy a certain protection and, on the other hand, a certain supervision must be carried out over such investments. Favorable treatment is necessary as they form an essential element of the vital economy of the country concerned; but supervision is also called for in order that the returns from these investments are profitable to the country of their origin. Such control is doubly ensured in France by the institution known as exchange control and by taxation.

Exchange control exists in practically all European countries. Thus, the foreign investor must not overlook the fact that as from the time he contemplates investment he will have to take a look at the consequences of such action, not only from a taxation point of view, but also from that of exchange control. The rules applicable in exchange control are indeed different from those usual in tax matters. Thus, any study of the regulations concerning foreign investments should bear both on the effect of the functioning of exchange control on such investments and on the taxation which is applicable. It is, of course, obvious that any consultation for the benefit of a foreign investor should be carried out on these lines. To go into these, however, would take us rather far afield. For this reason, I have deliberately limited this study to the second aspect of the problem, that is foreign investment considered from the point of view of taxation. This question is in itself of a complex nature and my comments do not pretend to be exhaustive. At the very most, I hope they will enable a certain number of points to be clarified and that they will prompt some questions from those present here.

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Before entering into how foreign investments in France are taxed, a clear and exact definition of tax domicile would not be out of place.

The idea of tax domicile is, indeed, different from that of nationality. Thus, a foreign investor may be looked upon as being domiciled in the country where his investment is made, but such domicile is only from the point of view of revenue; or the contrary may be the case, that is to say, his domicile from the revenue point of view is not in that country.

Thus, the tax on investments differs, depending whether the investor's tax domicile is in the country where the investment is made, or whether he is domiciled abroad. The importance of tax domicile is confirmed by the fact that it is referred to in the legislation of practically every country and that it has been considerably developed in international agreements.

The French Definition

Article on the French law of December 29, 1976, provides a new definition of tax domicile. Before that date the French Inland Revenue started from the principle of the "centre of vital interests." Since 1976, preference has been given to criteria of a personal, professional or economic order. It is now only necessary for one condition to be fulfilled for taxation to be levied on the grounds of domicile. A person is domiciled in France if his home is there. The aim of the law is to fix the domicile as the place where the taxpayer's family lives, even should the taxpayer himself carry on activity outside France.

In the same way, a person is domiciled in France if he resides there most of the time. Such a person may be liable to tax if he has stayed in France for less than five years. By reason of the rule concerning the annual character of income tax, it is only necessary for a person to have lived in France for more than 183 days in the year to be taxed as if he were domiciled.

Professional Condition

It is clearly laid down that any person carrying on a professional activity in France is domiciled in that country, whether or not such activity be remunerated. However, the law allows the interested party to bring proof that his activity is purely secondary, and in the nature of a sideline.

Economic Condition

This condition recalls the previous condition laid down by the Government and the Council of State, and runs the risk of being very little used, since in general a person carrying on a profession in France lives there most of the time. This third condition may, however, affect persons whose incomes come mainly from the possession in France of capital or rights of variable character: rent from premises situated in France, royalties, dues from patents received in France by the heirs of artists, writers, inventors. . . .

The Definition of the Standard Type of O.E.C.D. Agreement

Article 4, § 2 and 3, of this agreement lays down that, when in accordance with the provisions of § 1, a person is considered to be resident in each of the contracting states, his position is regulated as follows:

a) This person is considered to be resident in the contracting state where he has a permanent home; or when he has a permanent home in each of the contracting states, in which case he is considered to be a resident in the contracting state with which he has the closest personal and economic ties (centre of vital interests).

b) If it is impossible to determine in which of the contracting states such a person has his centre of vital interests, or if he does not possess a permanent dwelling place in any of the contracting states, that person will be deemed to be resident in the contracting state where he generally lives.

c) Should the person in question stay regularly in each of the contracting states or, on the contrary, does not so stay in any of them, he is considered as being resident in the contracting state whose nationality he possesses.

d) Should the person in question possess the nationality of each of the contracting states or, on the contrary, not possess the nationality of any of them, the competent authorities of the contracting states will settle the question by common agreement.

When according to the provisions of paragraph I, a corporative body is looked upon as resident in each of the contracting states, then actual residence is considered to be in the country where the head office is situated.

Similarity of the French Definition and That of the Standard "O.E.C.D." Agreement

These two definitions, indeed, give preference to criteria of a personal order rather than professional or economic. Such proximity of definition is of recent date; former art. 164/I of the General Code of Taxation did not adopt this order of priority. However, it is still too soon (the French law dates from December 29, 1976) to know if such proximity of definition desired by the law will receive total confirmation in case law.

However that may be, it should be remarked that the French definition of domicile is somewhat narrower in scope than that adopted by the O.E.C.D. agreement; indeed, the idea of domicile properly speaking is applicable in France to individual persons only. On the contrary, article 4 of the O.E.C.D. agreement deals in subparagraph 2 with the criteria of domicile for individual persons and subparagraph 3 with legal entities other than individual persons. In the same way, article 3 of the Franco-American Agreement, under the heading "resident tax domicile" lumps together individual persons and corporative bodies. Such assimilation is not to be found in French law, which in

fact makes no mention of corporation domiciled in France, but simply of those "liable to tax" in France. The category covered includes: corporative bodies possessing permanent autonomous establishment in that country (i.e., a center or focal point from which business is run but also subjected to the application of international agreements); those corporations not having a fixed establishment in France, but carrying on commercial activity there through the instrumentality of representatives without any distinct legal personality apart from that of the corporation, and qualified to represent the corporation—or those which, whilst not having fixed establishments or qualified representatives in France, nonetheless carry on commercial activity of a permanent nature, particularly when they carry out a cycle of transactions that may be looked upon as being complete.

By virtue of the same territorial principle, a corporation having its head office in France is not liable to tax on transactions carried out anywhere outside France, either in an autonomous establishment or through agents who have no distinct legal personality, or even in the case where no establishment exists or where there are no representatives, once the transactions carried out abroad form a complete commercial cycle.

The interpretation set forth herein has followed the interpretation given by the General Code of Taxation. However, the definition given by the standard O.E.C.D. Agreement is undeniably more complete and must be taken as the yardstick. Thus, when future mention is made of the idea of domicile considered from the point of view of taxation, within the limits of this study, we mean the tax domicile both of individual persons and corporative bodies, but we should not lose sight of the fact that in France, the expression "tax domicile" is only used for individuals.

Foreign investments are, in general, subject to taxation through income tax; however, the fact of a person investing abroad may also have repercussions in the field of capital transfer tax and tax on fortune. Indeed, the fact of investing money in another country naturally lends an international aspect to the inheritance of the investment, a part of which is often taxed in the country in which these investments were made. On the other hand, in some European countries, such investments sometimes entail a capital tax.

Part I: Taxation of Foreign Investments When the Investor Is Domiciled in France for Purposes of Revenue

As from the moment when the investor is domiciled in France for purposes of revenue there is no longer any question of a foreign investment. Such a manner of looking at things would be clearly erroneous were it not for the fact that it is often the investment itself that brings about the determination of domicile. To understand the problem requires further comment relative to the cases of legal entities and of individual persons.

Section I: The Case of Corporations

1. *The Position in France*

As has already been said, the General Code of Taxation does not apply the idea of tax domicile to corporations. This concept is found, however, in the O.E.C.D. standard agreements. But, in truth, this distinction between the O.E.C.D. agreement and the General Code of Taxation is purely formal; and it is quite possible to talk about "tax domicile" for corporations liable to tax in France. But this idea of "tax domicile" is based solely on the hard facts of economics and not on law.

Indeed, once an enterprise is exploited in France it follows as a natural consequence that it is liable to corporation tax. On the other hand, an enterprise which from a juridical point of view may perhaps be considered as French is not liable to corporation tax and cannot be looked upon as being domiciled in France for the purposes of revenue by reason of transactions forming a complete commercial cycle but carried out abroad. This definition of "tax domicile" leads to two consequences as far as foreign investments made in France are concerned.

a) When a foreign person or company acquires, creates or installs in France, a legal entity which carries on activity in France, this company is looked upon as being fiscally domiciled in France.

b) When a foreign person or company installs, acquires or creates in France a corporation which carries out no activity of a commercial nature in French territory, this company is not theoretically looked upon as being domiciled in France for the purposes of revenue.

A. THE CASE OF COMPANY CARRYING ON COMMERCIAL ACTIVITY IN FRANCE

Such a company (legal entity) is totally assimilated to a French corporation and is subject to the same tax liabilities and obligations both with respect to returns and levy. The assimilation holds good whatever may be the juridical nature and nationality of the corporation in question. This is particularly the case of the following persons or companies which are to be looked upon as being officially domiciled in France: foreign persons and companies possessing in that country a permanent establishment (with a centre from which the business is run), and, on the other hand, persons and companies who, whilst not possessing a fixed establishment, nevertheless carry on habitual commercial activity through a representative who has no separate legal personality apart from the company and is qualified to represent such persons or companies, or who, without having either a fixed establishment or representative qualified to represent them, carry out commercial transactions in the country as a normal and usual activity, particularly when such transactions form a complete cycle.

Finally, it goes without saying that when a foreign person or company constitutes a company in France in accordance with French law and carries on business in France, such a person or company is a fortiori liable to tax and looked upon as being domiciled in France for the purposes of revenue.

B. THE CASE OF A BODY CORPORATE NOT CARRYING ON ACTIVITY IN FRANCE

It may be queried whether a body corporate which installs an office in France, but carries on no commercial activity properly speaking is subject to the corporation tax.

A negative answer would seem to be called for since it would mean that it is possible to install administrative offices in France for the purposes of co-ordination, without necessarily assimilating such offices to French corporations for tax purposes. Certain countries and in particular Monaco, admit the existence of such offices in certain cases. In France the practice is recognized by such double taxation agreements as the Franco-Swiss and Franco-American agreements; the latter agreement, in article 4 § 3, lays down that:

> Notwithstanding the provisions of paragraph 1 of the present article it is not thought that a fixed establishment exists when a permanent business installation is utilized only for one or several of the following puposes:
>
> a) the use of the installation for the stocking, display and delivery of goods belonging to the resident for
>
> b) warehousing of goods belonging to the resident for stocking, display or delivery;
>
> c) warehousing of goods belonging to the resident whilst awaiting transformation by another person,
>
> d) the use of the permanent installation for the purchase of goods or while the resident gathers information,
>
> e) the use of the above-mentioned premises for advertising purposes, making known the results of scientific research, or for analogous activities of a preparatory or auxiliary character as far as the resident is concerned.

One might be led to think that France admits the existence of administrative offices and places them under a system of favourable treatment in derogation of corporation tax law. However, although statute law does not forbid such practices, the French tax authorities are remarkably coy about this solution, fearing that investors would bend it to allow for tax avoidance.

2. *The Impact of International Law*

A. THE FRANCO-AMERICAN AGREEMENT

Article 4 subparagraph I of the Franco-American Agreement defines the notion of permanent establishment. Within the meaning of the above mentioned agreement, "permanent establishment" is defined as the setting up of permanent business premises by means of which a resident of one of the contracting states carries on industrial or commercial activity.

Putting it in a different way, when a resident American individual corpora-

tion begins some commercial activity in France, such an individual or corporation is liable to income tax or corporation tax in France. The Franco-American Agreement specifies that the expression "permanent establishment" includes particularly a head office, a branch office, a factory, a workshop, a warehouse, a quarry, etc. or a work site in existence for more than twelve months.

The Franco-American Agreement causes corporations to be liable to French tax in accordance with criteria very close to those used by French internal legislation. In fact, the activity carried on in France by an American corporation and corresponding to a complete commercial cycle is taxable in France. On the other hand, as from the moment when it is clear that there is no exploitation of an enterprise in France, the French installation no longer comes within the category of a stable establishment. But in any case, the right of deciding whether or not an enterprise is exploited in France belongs to the administrative authorities.

B. THE "O.E.C.D." AGREEMENT

This agreement, like French legislation and the Franco-American Agreement, lays stress on the effective means of determining the country in which a corporation should be taxed. The wording of article 46/III is indeed quite shrewd for it states "a legal entity other than a person...is considered as resident" in the contracting state in which is to be found the actual office from which affairs are administered.

The accent is thus placed, not so much on the effective reality of the transaction carried out in a given country, but on the effective reality of the administration and management. The article looks unfavourably on administrative offices concerned only with coordination and which are not subject to tax, or at least subject to a small amount of tax only, by reason of the fact that they do not constitute stable establishments. Thus it avoids ambiguous situations such as that of the French administration faced with the problems of administrative offices.

To conclude the subject of corporation tax, it may be said in adopting as a criterion of taxation the notion of activity, France levies a substantial sum of taxes on these foreign corporations.

In practice, indeed, such corporations are domiciled in France within the meaning of the "O.E.C.D." agreement by the very fact of carrying on activity in that country. The most notable example that can be given to illustrate this statement is, of course, article 13 of the new law of December 29, 1976.

In accordance with the terms of this article, the mere fact that a foreign body corporate possesses or has at its disposal immovable property (real estate) in France is sufficient to assimilate such possession to an "activity," thus enabling the French Inland Revenue to levy corporation tax on the body

corporate, such tax being assessed on the basis of three times the rental value of the premises.

Thus the attitude of the French Inland Revenue towards foreign companies is seen to be somewhat harsh.

Is the same policy adopted with respect to persons?

Section II: The Case of Persons Having Their Tax Domicile in France

1. *French Legislation*

As already noted, the criteria for determining domicile are, in France, different for corporations and for persons.

As far as persons are concerned, indeed, considerations of a personal order take precedence over those of a professional or economic kind. However, it may be the underlying principle of taxation is the same; thus, as in the case of corporations—where French taxpayers and foreign taxpayers domiciled in France are in exactly the same position—individual persons are subject to the same rules. Traditional French legislation was completely disrupted by the law of December 29, 1976, which modifies to a considerable degree the system applying to the state in which tax should be levied. Under the new system, importance will be attached to tax domicile rather than to habitual residence, as in the past. It is of course obvious that this reform entails consequences for foreigners who are domiciled in France for the purpose of revenue.

Article 164 of the former law laid down that persons of foreign nationality domiciled in France were, as a general rule, taxed in France on the whole of their income. An important exception was, however, provided for: taxation did not affect income of foreign origin which had already been subject to tax on total income in the country of origin of the taxpayer in question.

The new law will rescind this exception as from the moment of the 1979 tax levy, which means that from 1979 foreigners having their tax domicile in France will be taxed in France on the whole of their income and in particular, on income from investments, even should such income be of foreign source. Thus, a foreigner domiciled in France for the purpose of revenue and having investments outside that country will pay income tax in France on the income from such investments.

This will be true even where a double taxation agreement has been entered into by France and the country in which the above-mentioned investments are made. The reform will in fact lead to a change in the manner of assessing tax to be paid by a foreigner domiciled in France. The exoneration provided for in article 164/I has the effect of reducing the progressive character of the income tax, as the income exempted from tax is not taken into consideration for the assessment of the tax tranche. The new law fully restores this progressive character since in the case where a part of the income may be taxed abroad and

not in France by reason of double taxation agreements, the amount of such income is not taken into consideration to enable the assessment of the tax tranche to be made.

2. *The Effect of International Law*

The new French law promises to multiply the number of cases of double taxation, since where there is no double taxation agreement in existence or where such an agreement, if it exists, does not cover every possibility, taxation in France will follow automatically as from 1979. Because this question is a particular source of anxiety for the American authorities, representatives of the French and American governments have met in order to examine some of the acute difficulties. For, according to American tax legislation, American citizens remain taxable in the United States, for the sum total of their incomes, whether or not they be resident in their own country.

Let us imagine the case of an American resident in France for the purposes of revenue; until 1976 his situation was fully regulated by the Franco-American Agreement, specifically, the income having its source in another state, one-third was taxed in the United States by virtue, on the one hand, of the exoneration provided for in article 164/I of the General Code of Taxation, and, on the other hand, of the exemption under American tax legislation. As from 1979, this will no longer apply, since the law of December 29, 1976, has abolished the exoneration under article 164/I; i.e., both the French and American authorities will have the right to claim income tax from an American citizen resident in France for the purposes of revenue, on income the source of which was in a state other than in the United States or France (in particular on income from investments).

Part II: Tax on Foreign Investment When the Investor Is Domiciled Outside France for the Purposes of Revenue

It has been shown in the first part of this paper that the simple fact of making an investment in France causes the investor to be looked upon as being a French taxpayer domiciled in France for the purposes of revenue. This statement is strikingly confirmed when a corporate body begins activity in France, or when an individual person makes an investment through the intermediary of a corporate body.

In such a case, the fact that French domicile for the purposes of revenue has been adopted is sufficient to assimilate the investor, should he be of foreign nationality, to a French taxpayer. *Au contraire* might it be said that as from the moment when there is *no* domicile in France for the purposes of revenue, foreign investments escape taxation in France? Unfortunately, such a statement fails to correspond to the reality.

Section I: Determination of the Basis of Assessment

1. *The Idea of Income of French Origin*

Apart from the gift and inheritance taxation of property, which does not fall within the range of our study, foreign investments are liable to French taxation by reason of the income the investor receives from them. The basis of taxation is made up of the amount of income of French origin, which is determined by the provisions of article 4 of the law of 1976, in accordance with the principles applicable to persons domiciled in France. Thus the rule is that calculation of income is made by categories, unless the law lays down that the lump sum system must be used.

We cannot, of course, examine here all the categories of income taxable in France. Not all such income is derived from investments; income arising from activity carried on in France, whether such activity be paid or not, will not be touched upon.

In practice, investments are taxed in France under the headings of income from personal and real property and of capital gains.

In terms of present day legal doctrine, income stemming from French stocks and shares is in all cases of French origin, whether such stocks and shares are lodged in France or in another country. On the other hand, income stemming from foreign stocks and shares is not considered to be of French origin, even should such stocks and shares be lodged in France.

The income from personal property situated in France is also looked upon as being income of a French source taxable in France—income from real property situated in France and from rights appertaining to such real property is also taxable in France, whether or not the investor is domiciled in France for the purposes of revenue. Income from real property is defined by the law as being the rent of premises situated in France and also income derived from share holdings in building societies.

The new legal provisions (art. 4 subpara. 1) do not allow expenses to be deducted from the total income. Such deduction is, however, authorised for interest on loans, stonework refacing and heating insulation concerning the dwelling premises. To take advantage of this deduction, the interested persons must bind themselves to make it their principal place of residence before January 1 of the third year after the signing of the loan contract or the payment of the work carried out.

Capital gains arising from the sale of real property situated in France are taxable in France. In the same way, increment values arising from the sale of precious metals and objects are looked upon as being income of French origin if the sale takes place in France.

2. *Individual Persons Domiciled Outside France and Having a Dwelling Place at Their Disposal in France*

Article 7 of the law of December, 1976, lays down that taxpayers who are domiciled outside France but who have one or more dwelling places at their disposal in that country are liable to income tax according to the scale provided for in article 197-1, on a minimum basis of three times the actual rental value.

This lump sum taxation is not applicable on the one hand, if the income of French origin, including that subjected to preliminary levy, goes beyond the threshold of this valuation, or if, on the other hand, the taxpayer can show that he is quite heavily taxed abroad. The taxpayer who is domiciled in a country which has entered into a double taxation agreement with France escapes this lump sum taxation.

Section II: Methods of Levying Income Tax on Income from Investments Received by Taxpayers Who Are Not Domiciled in France

1. *The Application of a Minimum Rate of Levy*

Article 4 of the law of December, 1976, provides for a minimum rate of 25 percent in order to avoid giving an unfair advantage to taxpayers domiciled outside France and levied only on their income of French origin, over taxpayers domiciled in France. The rule of the progressive character of the tax is indeed unfavourable for the latter.

The minimum rate is applicable as a general rule every time the average rate of levy tax due (taxable income) is less than 25 percent. However, in accordance with article 4 last subparagraph, if the taxpayer who is domiciled outside France can show that, whilst observing the financial provisions laid down, the taxation of the sum total of his income (both of French and other sources) is less than this minimum of 25 percent, he will then be able to escape this taxation.

2. *The Taxation of Income Coming from Sundry Kinds of Foreign Investments*

A. TAXATION OF STOCKS AND SHARES

(1) THE TAXATION OF INCOME FROM SHARES, AND ASSIMILATED INCOME

The Withholding Tax of 25 Percent

When the recipient of income from personal property has his actual

domicile or office outside France, the income is subject to a withholding tax of 25 percent in case such income has been paid out by companies whose head offices are situated in France. This withholding tax of 25 percent is applicable to income arising from shares and to assimilated income (directors' fees, etc.). Note should be taken of the fact, however, that income from shares and the like paid out by French companies to international organizations, sovereign states or the central banks of these states is exempt from the withholding tax of 25 percent.

The establishments paying out such income must transmit this withholding tax to the Tax Office. For this reason the head office of establishments which pay out as described above must request the recipients of income so received to give proof of the fact that their domiciles or head offices are situated in France. The sums thus retained as withholding tax by the establishment in the course of each quarter must be paid to the appropriate Tax Office and as a general rule in the month following the end of the quarter. The withholding tax of 25 percent is final and of a legally exempting character, which means that the income from which the withholding tax was deducted is not included in the income liable to progressive income tax; *per contra*, the amount of the withholding tax is not chargeable on the tax itself.

The Effect of Double Taxation Agreements

As far as income from personal property is concerned, taxpayers domiciled in France for the purposes of revenue enjoy an advantage to which the term tax credit has been given; this tax credit, which is 50 percent of the sum paid out, was set up to encourage saving. It only applies to persons domiciled in France, but, nonetheless, certain countries have signed an agreement extending the scope of the tax credit. This is especially the case of the United States; the fact of agreeing to the application of the tax asset technique to taxpayers who are not domiciled in France naturally brings in its wake certain consequences with respect to the calculation of the withholding tax of 25 percent. In practice, even if the taxpayer is resident in the state which has signed an extension agreement for the tax asset, the withholding tax of 25 percent is paid by the paying enterprise. This withholding tax is compensated as from January 15 following the year in which payment of the dividend was made, and at the time of the transfer of the tax asset, which transfer is carried out by the paying establishment.

(2) TAXATION OF FIXED INTEREST INVESTMENTS

Lump Sum Pre-Levy of 25 Percent or 33.33 Percent

When the dividend from a fixed income investment is paid in a foreign country, it is subject to a lump sum pre-levy of 25 percent or 33.33 percent. This

obligation is general and in principle affects all dividends from fixed income investments even if they do not fulfil the conditions to which the option open to taxpayers domiciled in France is subject. This pre-levy is final, the income from which the pre-levy was deducted being automatically excluded from the total income subject to the application of the progressive scale; and, consequently, the amount of the pre-levy is not chargeable to the amount of income tax, whether such income tax be assessed on the basis of income of French origin or of the rental value of the residence.

B. THE TAXATION OF INCOME FROM REALTY

By income from realty is meant the income from the leasing of premises by foreigners in France. The system described here does not apply to foreign corporative bodies. Indeed, a corporative body which possessed premises in France for the purposes of letting would be considered by the French Inland Revenue as being in the nature of a permanent establishment for tax purposes, and on that account liable to corporation tax. On this subject, the law of December 29, 1976, lays down in article 13 that "if a corporative body the head office of which is situated outside France has at its disposal one or more buildings situated in France and agrees to the free use of such on payment of a rent that is below the rental value, such a corporative body is liable to corporation tax on a basis that is in no case less than three times the actual rental value of such building or buildings."

Article 13 is of extreme importance. It is this article that permits the French administrative authorities to tax a foreign corporative body even if, properly speaking, it receives no income from premises. To be liable to taxation, it is sufficient for the corporative body to have real estate property at its disposal in France and to have let such property.

As far as individuals are concerned, the mere fact of possessing real property in France does not cause them to be regarded as being domiciled in France for the purposes of revenue. However, the fact of having real estate property in France may bring in its wake two consequences of a fiscal nature for an individual. Let us consider the case of a person having real property (a building) at his disposal, and so liable to tax on three times the rental value of the building, as has already been explained. Let us further imagine that the same person is in receipt of income arising from leasing the premises, and that his income is treated by the French Inland Revenue in exactly the same way as if such income were received by a French taxpayer. The amount of this tax cannot, however, be less than 25 percent of the income received by the foreign taxpayer.

The French point of view as far as realty income is concerned is perfectly compatible with international agreements and especially the Franco-American convention, which in fact draws a distinction as to whether or not the recipient

of realty income has a permanent establishment in France. Should he possess a permanent establishment, realty income is assimilated to industrial and commercial profits and is subject to corporation tax at the rate of 50 percent. Should the recipient of realty income have no permanent establishment, which means in practice if the recipient is not a corporative body, the income is taxable, in accordance with the terms of article 5 of the agreement, in the contracting state where the real property is situated.

C. TAXATION OF CAPITAL GAINS

Most capital gains realised by individual persons in France have been taxable since the passing of the law of July 19, 1976. This law, of course, brings consequences in its wake not only with respect to capital gains realised by taxpayers not domiciled in France on personal property but also with capital gains realised by the said taxpayers on realty.

(1) CAPITAL GAINS ON REALTY

In the past, articles 150 quarter, 244 bis of the General Code of Taxation subjected respectively the capital gain resulting from the sale of building land and other realty gains to a pre-levy of 50 percent, when realised by non-residents. These two articles have been abrogated by article 12/III of the law of July 19, 1976. Article 8/III of the new law has provided for a pre-levy of one-third for capital gains realized since January 1, 1977. This pre-levy of one-third applies to individual persons and companies not having their domicile or head offices in France, and who do not carry on any industrial or commercial activity in a permanent establishment in France.

(2) CAPITAL GAINS FROM PERSONAL PROPERTY

Taxpayers resident outside France are subject to a pre-levy when they transfer stocks and shares falling within the category set out in article 160 of the General Code of Taxation, i.e., when the rights held in the profits of the company by themselves, their spouses, father or mother or descendant are together greater than 25 percent of these company profits at any time in the course of the five years preceding the year in which the transfer took place.

In such a case, a pre-levy of 15 percent is provided for.

(3) THE EFFECTS OF INTERNATIONAL LAW

These different provisions concerning capital gains from realty and personal property are applicable, of course, only in the absence of a double taxation agreement. Should the contrary be the case, the double taxation agreement takes precedence over national law. Basing our argument on the Franco-American Agreement, we may say that an American resident realizing capital gains in France, as understood by French law, will only be taxed on realty in-

crement values. (Article 12 - para. 1 of the Franco-American Agreement). Capital gains realized on personal property in France by a resident American will not be taxable in France in spite of the French principle of the general nature of tax on capital gains. It is different in the case of realty gain when the recipient who resides in a contracting state has, in the other contracting state, a fixed establishment in which the source of gain is to be actually found; or if the recipient of the gain has a fixed base in France where the source of the gain is so to speak lodged, or if he stays in France for a period or periods of more than 183 days in the course of the fiscal year.