

U.S. TAXATION OF FRENCH ENTITIES

PART I – FRENCH ENTITIES AND U.S. ENTITY CLASSIFICATION RULES

FANNY KARAMAN

Admitted to the New York and Paris Bars

FRENCH ENTITIES & U.S. ENTITY CLASSIFICATION RULES

1. **The U.S. Entity Classification Rules**
2. **Regularly Used French Entities: S.A., S.A.S., S.A.R.L. and S.C.I.**
3. **Classification of French Entities for U.S. Tax Purposes**

The U.S. Entity Classification Rules

Four Classifications

- Trust
- Corporation
- Partnership
- Disregarded

Six Questions (U.S. Entities)

- Date of formation?
- Trust or business entity?
- Is it a corporation?
- Does it have at least two members?
- Does it have only one member?
- Was an entity classification made?

Seven Questions (Non-U.S. Entities)

- Date of formation?
- Trust or business entity?
- Is it a “per se” corporation?
- Liability of the member(s)?
- Does it have only one member?
- Does it have two or more members?
- Was an entity classification made?

The U.S. Entity Classification Rules

- Why is it important?
- Examples:
 - Who is the taxpayer? Entity v. owner
 - Controlled Foreign Corporation
 - Passive Foreign Investment Companies

The U.S. Entity Classification Rules

- Domestic and foreign classification rules are found in Regs. §§301.7701-1 to 301.7701-4.
- Generally applicable as of 1997.
- Regulations classify domestic and foreign entities for U.S. tax purposes and allow certain business entities (“Eligible Entities”) to choose their classification for Federal tax purposes under an elective regime.

The U.S. Entity Classification Rules

- For both domestic and foreign entities: is it a Trust?
 - A business entity is generally any entity recognized for federal tax purposes that is not properly classified as a trust or otherwise subject to special treatment.
 - Trust: an arrangement created either by a will or by an *inter vivos* declaration whereby trustees take title to property for the purpose of protecting or conserving it for the beneficiaries under the ordinary rules applied in chancery or probate courts.

The U.S. Entity Classification Rules

- For domestic entities: Is it a corporation for federal tax purposes?
 - Generally, a corporation formed under Federal or State statute (look for the terms “inc.”, “incorporated”, “corporation”, “body corporate”, or “body politic”)
 - A business entity organized under a State statute, if the statute describes or refers to the entity as a joint-stock company or joint-stock association
 - An insurance company.
 - A State-chartered business entity conducting banking activities.
 - Certain State or government owned entities.
 - A business entity that is taxable as a corporation under a provision of the Internal Revenue Code (other than Code §7701)

The U.S. Entity Classification Rules

- A business entity that is not necessarily classified as a corporation under Reg. §301.7701-2(b) is an "eligible entity" and can elect its classification for Federal tax purposes under Reg. §301.7701-3.
- Domestic eligible entities are classified as follows in the absence of an election:
 - An eligible entity with 2+ members is classified as a partnership.
 - A single member entity is classified as a "disregarded entity" that is not separate from its owner.
 - As a result, a U.S. L.L.C. is automatically a pass-thru entity.

The U.S. Entity Classification Rules

Summary – Domestic Entities

Individual



Corporation



(U.S. “inc” → *Always a corporation*)



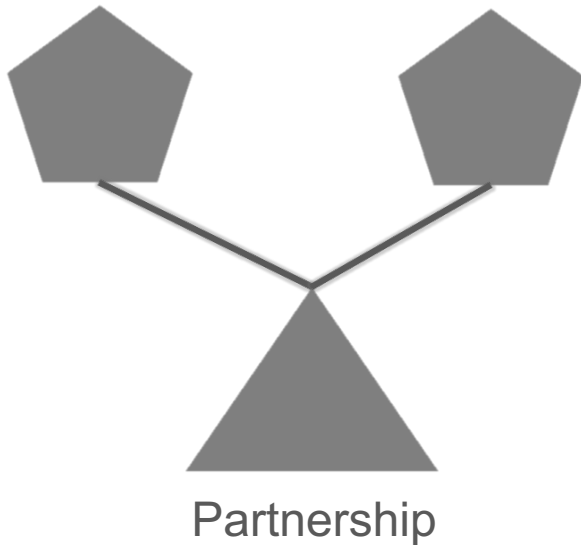
Partnership or
Disregarded



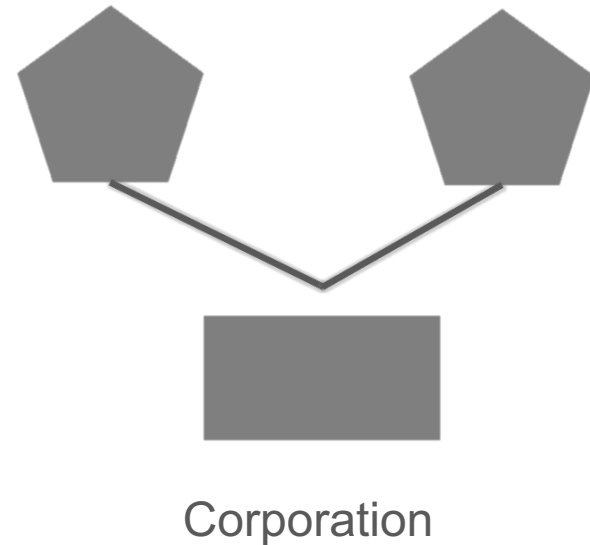
Unknown

The U.S. Entity Classification Rules: Summary (Domestic Entities)

Default Rules

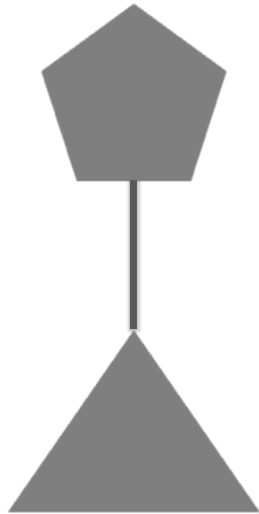


Possible Check-the-Box



The U.S. Entity Classification Rules: Summary (Domestic Entities)

Default Rules



L.L.C./Disregarded

Possible Check-the-Box



Corporation

The U.S. Entity Classification Rules

- For foreign entities: is it a corporation for federal tax purposes?
- Foreign business entities are categorized as either eligible entities or per se corporations.
- *Per Se* corporations:
 - Foreign entities that are specifically listed in Reg. §301.7701-2(b)(8)
 - These entities must be treated as corporations and cannot make a classification election.

The U.S. Entity Classification Rules

- Examples are:
 - S.A. formed under Argentine, Brazilian, Chilean, Columbian, French, Luxembourg, Mexican, Panamanian, Polish, Portuguese, Spanish, Swiss, Uruguayan, Venezuelan law, etc.
 - A.G. formed under German, Liechtenstein, Swiss law
 - P.L.C. formed under Australian, Cypriot, Maltese, Singapore, South African, U.K. law, etc.
 - An O.A.O. formed under Russian law, and N.V. formed under Dutch law, and a G.Y.G. formed in under Chinese law.

The U.S. Entity Classification Rules

- Eligible Entities:
 - All members have limited liability → default corporation - can elect partnership treatment
 - 2 members or more and at least one has unlimited liability → default partnership –can elect corporate treatment
 - 1 member with unlimited liability → default disregarded - can elect corporate treatment
 - A foreign eligible entity may elect a different treatment on a timely filed Form 8832 (Entity Classification Election)

The U.S. Entity Classification Rules

Summary – Foreign Entities

Individual –
Unlimited Liability



Individual –
Limited Liability



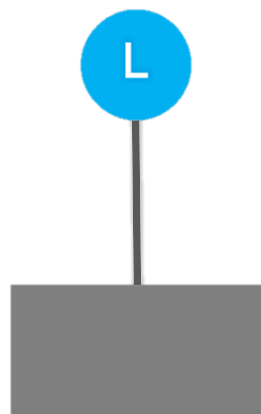
Partnership or
Disregarded



Corporation

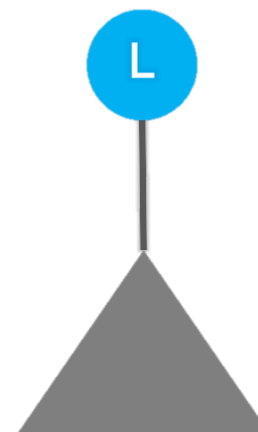
The U.S. Entity Classification Rules: Summary (Foreign Entities)

Default Rules



Corporation

Possible Check-the-Box

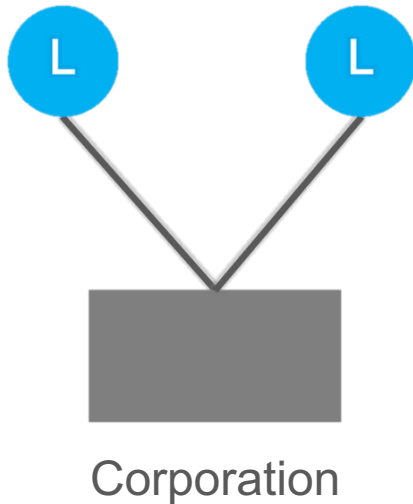


Disregarded

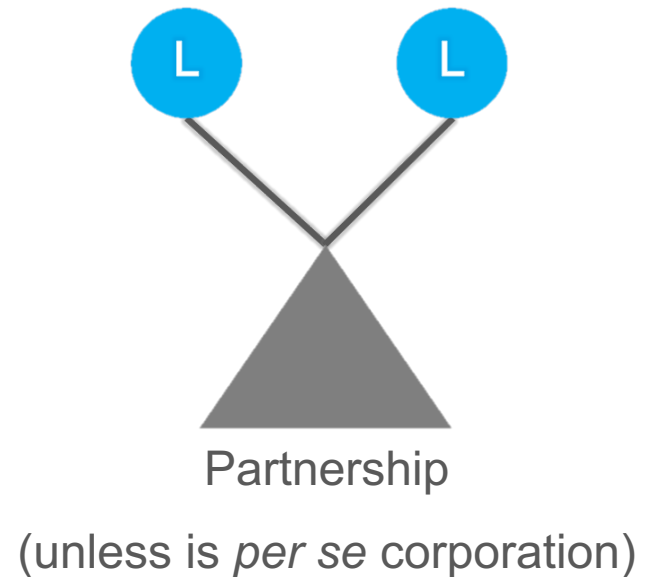
(unless is *per se* corporation)

The U.S. Entity Classification Rules: Summary (Foreign Entities)

Default Rules

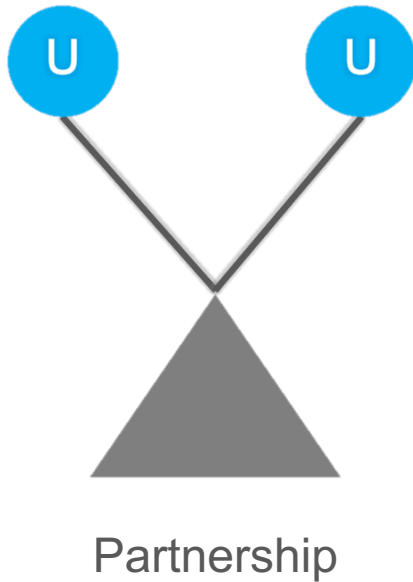


Possible Check-the-Box

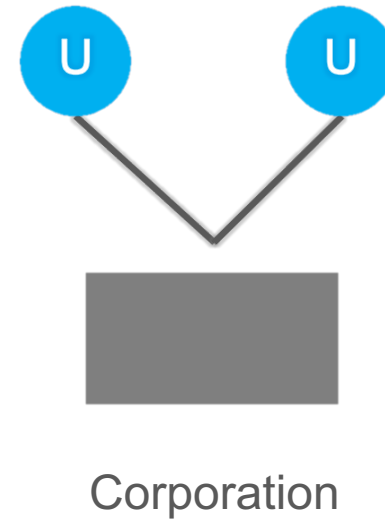


The U.S. Entity Classification Rules: Summary (Foreign Entities)

Default Rules

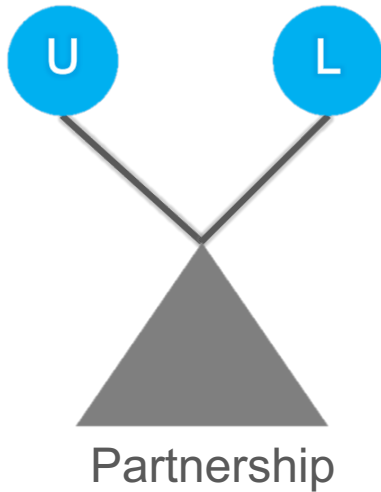


Possible Check-the-Box

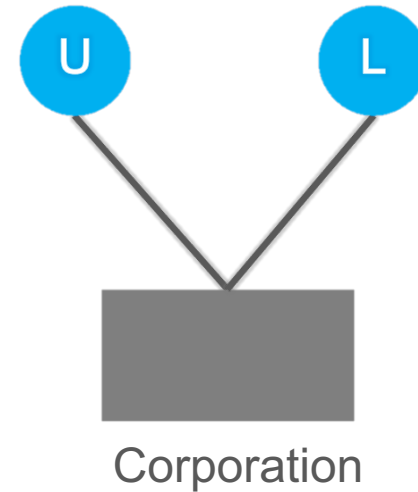


The U.S. Entity Classification Rules: Summary (Foreign Entities)

Default Rules

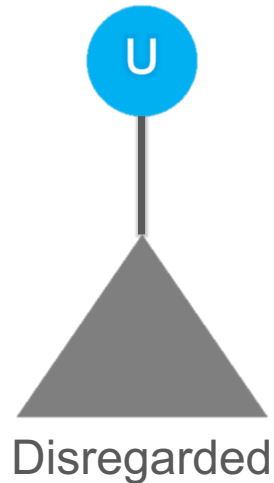


Possible Check-the-Box

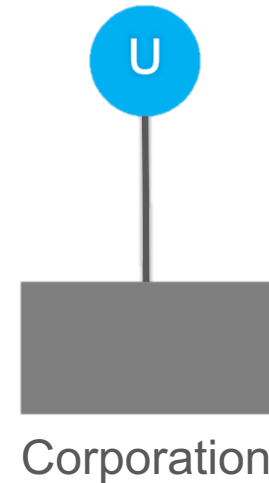


The U.S. Entity Classification Rules: Summary (Foreign Entities)

Default Rules



Possible Check-the-Box



The U.S. Entity Classification Rules

- Miscellaneous Considerations:
 - In general, the election of status is first effective not more than 75 days prior to filing and not more than 12 months after filing
 - Relief for late entity classification election may be available.
 - Caution when making a non-retroactive entity classification election after the entity's formation.

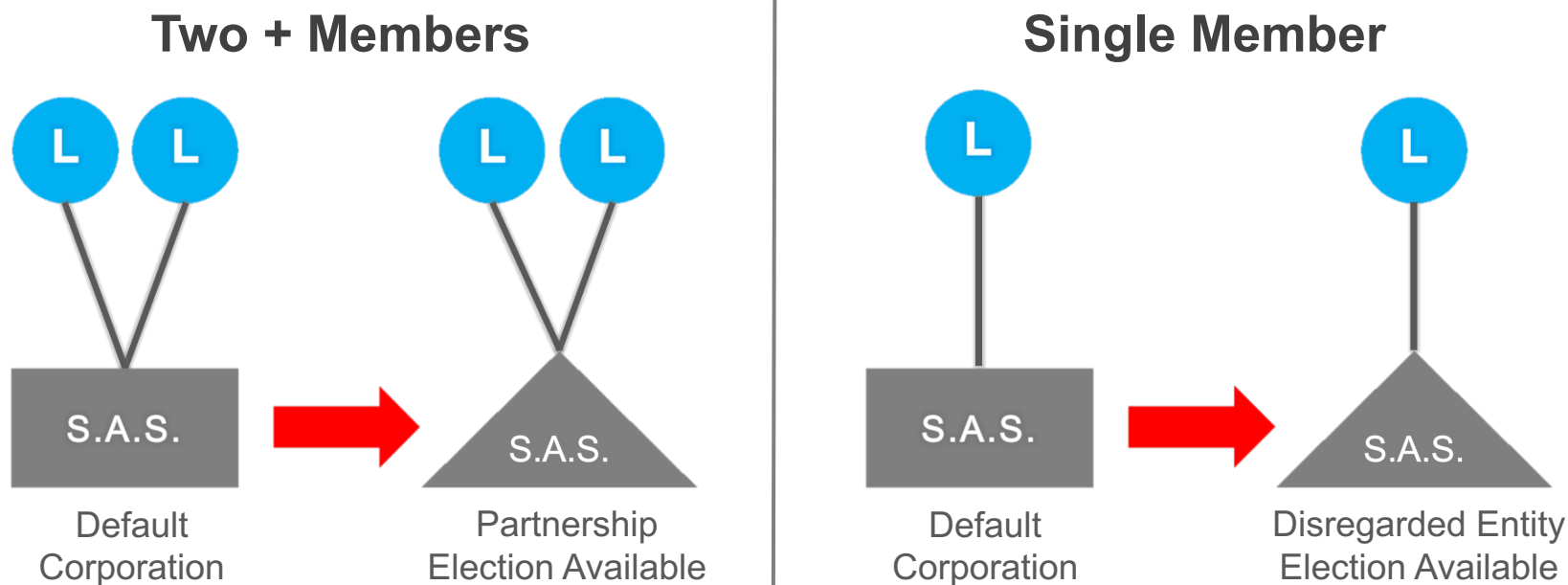
Regularly used French entities: S.A., S.A.S., S.A.R.L. and S.C.I.

- S.A.: *Société Anonyme*
 - Subject to French corporate income tax (“impôt sur les sociétés”)
 - Entity separate from its shareholders
 - Shareholders have limited liability
- S.A.S.: *Société par Actions Simplifiée*
 - Subject to French corporate income tax (“impôt sur les sociétés”)
 - Entity separate from its shareholders
 - Shareholders have limited liability

Regularly used French entities: S.A., S.A.S., S.A.R.L. and S.C.I.

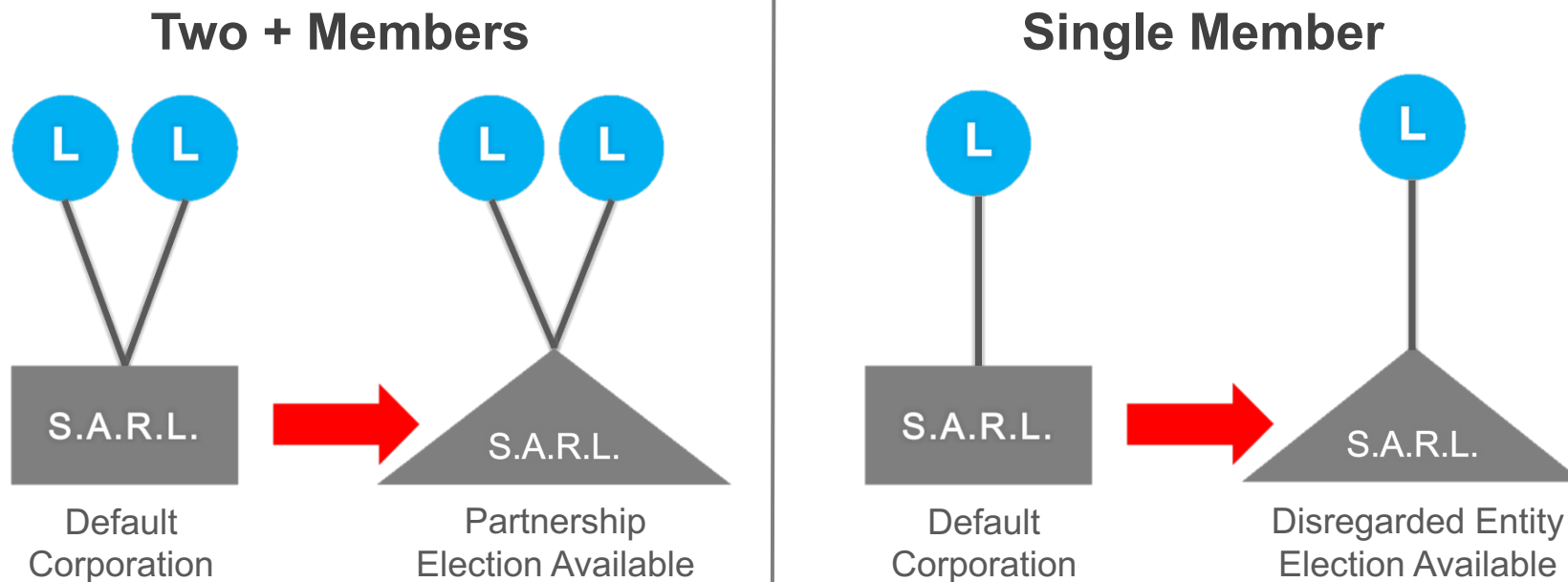
- S.A.R.L.: *Société à Responsabilité Limitée*
 - Subject to French corporate income tax (“*impôt sur les sociétés*”) - can elect otherwise
 - Entity separate from its shareholders
 - Shareholders have limited liability
- S.C.: *Société Civile*
 - Entity not subject to tax (can elect otherwise) – treated as transparent
 - Shareholders are subject to income tax on their share of the S.C.’s profits
 - Shareholders have unlimited liability

Classification of French Entities for U.S. Tax Purposes



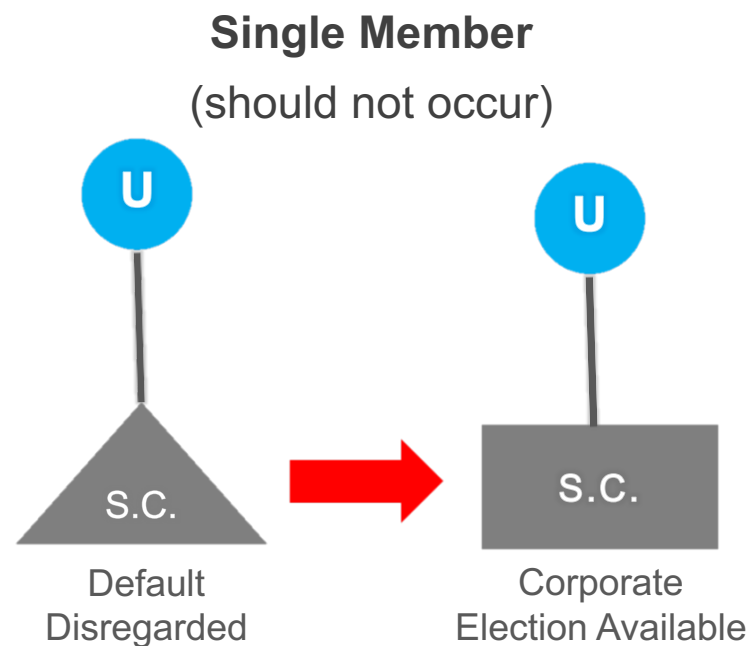
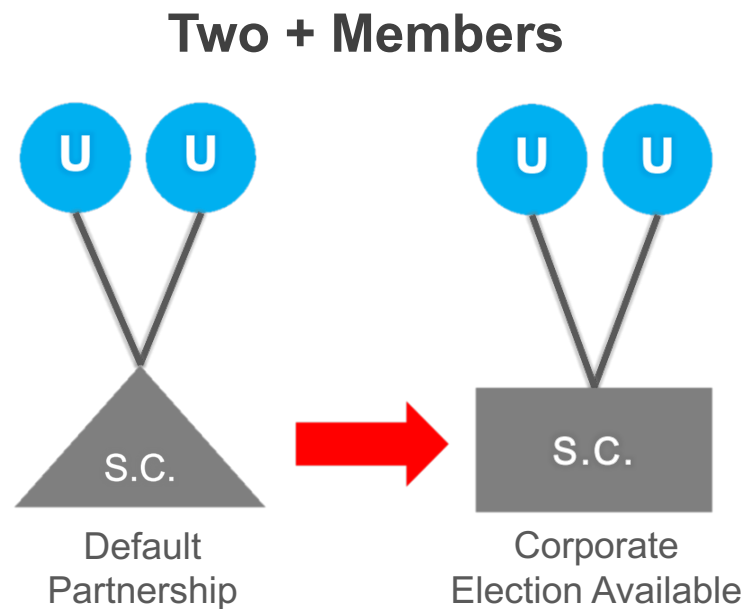
- S.A.: *Per se* corporation → no election possible
- S.A.S.: Default Classification: limited liability → corporation
 - Election possible:
 - One member: L.L.C.
 - Two or more members: partnership

Classification of French Entities for U.S. Tax Purposes



- S.A.R.L.: Default classification: limited liability → corporation
 - Election possible for partnership status if at least two members and disregarded if one member

Classification of French Entities for U.S. Tax Purposes



- S.C.: Default classification: unlimited liability → partnership if 2, disregarded if one
 - Election possible for corporate status

Important Notice

This presentation is not intended to be legal advice. Reading these materials does not create an attorney-client relationship. The outcome of each case stands on its own merits.