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# 7 Public Policies and Household Saving in France

Denis Fougère

## 7.1 Introduction

After relative stability at approximately 19 percent during the seventies, the household annual saving rate in France sharply decreased from 1980 to 1987 and then slightly increased over the period 1988–91 (see table 7.1). The evolution of the structure of household current financial assets (see table 7.2) sheds some light on this phenomenon. First of all, we observe a relative decrease of demand deposits, resulting from high real interest rates (which increase the opportunity cost of cash resources) and from the extension of the line of financial products during the eighties. After 1985, the proportion of investments in passbooks not subject to taxation diminishes with the decrease of the nominal rate of return. Moreover, the increase of the tax burden explains the decline of investments in passbooks subject to taxation.

In 1990, investments in securities became the major component of household financial assets. This is essentially due to the relative increase of shares and UCITS investments, which can be partly explained by the introduction of a tax deduction on bond interest and dividends (progressively raised to 8,000 francs for an individual and 16,000 francs for a married couple).<sup>1</sup> Finally,

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1. In France, mutual funds are collected by the so-called *organismes de placement collectif en valeurs mobilières* (OPCVM, or UCITS), which include *sociétés d'investissement à capital variable* (SICAV) and *fonds communs de placement* (FCP). At the end of 1990, UCITS deposits

**Table 7.1 Household Saving Rate in France**

	1981	1985	1987	1988	1989	1990	1991
Gross saving rate	18.0	14.0	10.8	11.0	11.7	12.2	12.6
Nonfinancial saving rate	11.3	9.2	9.2	9.0	9.6	9.3	8.8
Financial saving rate	6.7	4.8	1.6	2.0	2.1	2.9	3.8

Source: *Comptes et indicateurs économiques: Rapport sur les comptes de la Nation* (1988–91).

Note: The gross saving rate is defined as the ratio of gross savings to gross disposable income of households; nonfinancial savings include housing purchase and maintenance paid by households and investments made by sole company holders.

the proportion represented by life insurance has also increased, because of high rates of return and important tax deductions. (See *L'Allocation des flux d'épargne* 1991.)

## 7.2 Overview of the Household Balance Sheet

### 7.2.1 Share of Total Household Gross Worth in Various Assets

According to a recent Centre d'Etudes des Revenus et des Coûts (CERC; Center for the Study of Incomes and Costs) report (see Malpot and Paquel 1992), aggregate household gross worth (before the deduction of debt) in France was approximately 18,000 billion francs in 1988.<sup>2</sup> The mean household gross worth was 840,000 francs. But this mean varies highly across socio-professional groups: the mean gross worth of a professional is 3 million francs, while that of a worker is approximately 350,000 francs.

Different components of household gross wealth can be grouped in three categories: (1) *goods for domestic use* (38 percent)—liquidities (2.3 percent), primary home (31.2 percent), vacation home (4.3 percent); (2) *financial assets and rental goods* (51 percent)—savings-bank passbooks (6.4 percent), building-society passbooks and other bank deposits (5.7 percent), investments, bonds, and insurance policies (7.6 percent), quoted and nonquoted shares (12.5 percent), rental properties (14.9 percent), rented or nonrented lands and forests (4.5 percent); (3) *goods for professional use* (11 percent)—farmed land (1.9 percent), buildings (2 percent), equipment, cattle, and stock (4 percent), incorporeal assets (2.7 percent).<sup>3</sup> These proportions concern household gross wealth

amounted to approximately 2,000 billion francs, while bank deposit accounts amounted to approximately 6,000 billion francs.

2. These estimates do not include domestic durable goods (cars, furniture, consumer durables, gold, jewels, and works of art).

3. Wealth held by self-employed people for professional use does not include rented goods or any estimate of the "goodwill" associated with a professional reputation. It concerns equipment, machinery, buildings, farmed land, cattle, stock, and incorporeal assets (such as rights to a lease). It does not include shares, quoted or not.

**Table 7.2** Structure of Household Current Financial Assets (million francs)

	1979		1985		1989	
	Amount	%	Amount	%	Amount	%
Liquidities:	1,580	62.2	2,697	50.9	3,456	36.0
Cash, demand deposits	468	18.4	764	14.4	1,123	11.7
Passbooks not subject to taxation	436	17.1	967.4	18.2	1,079	11.2
Passbooks subject to taxation	184	7.2	209.7	3.9	217	2.3
Savings plans	122	4.8	228.2	4.3	448	4.7
Others liquidities	370	14.6	527.7	10.0	589	6.1
Securities:	546	21.5	1,812	34.2	4,802	50.0
Shares	294	11.6	1,017	19.2	3,527	36.7
Bonds	204	8.0	380	7.2	283	3.0
UCITS	48	1.3	415	7.8	992	10.3
Insurance	168	6.6	443	8.4	959	10.0
Credits and accounting gaps	245	9.6	348	6.6	386	4.0
<b>Total</b>	<b>2,539</b>		<b>5,300</b>		<b>9,603</b>	<b>100.0</b>

Sources: *Rapport sur les comptes de la Nation* (1991); *Rapport annuel au conseil National du Cr dit* (1992).

because available data do not permit any evaluation of the amount of debt incurred for the acquisition of each type of good.

The composition of household wealth varies across socioprofessional groups, as shown in table 7.3. Wealth of professionals represents more than half of farmers' total wealth, and between 20 and 30 percent of the total wealth of self-employed people (i.e., manufacturers, craftsmen, and merchants). The proportion of total household wealth marked for domestic use decreases with total wealth. The composition of "domestic use" wealth does not significantly vary across socioprofessional groups: the primary home represents its principal component (more than 70 percent). However, the primary home value for professional and senior executives is approximately twice that of workers and farmers.

The mean value of financial assets and rental goods held by households was around 430,000 francs in 1988. But, once again, this mean and the composition of this kind of wealth varies greatly across socioprofessional groups (see table 7.4). Socioprofessional groups whose mean value is high hold rental properties and shares proportionally more than the other groups. These goods represent about two-thirds of their whole wealth in financial assets and rental goods. On the other hand, more traditional liquid assets (savings-bank and building-society passbooks) represent a relatively higher proportion of the wealth of low-mean-value groups.

Moreover, farmers own proportionally less shares but more land and forest. By value, self-employed people (excluding farmers) and senior executives hold 57 percent of all shares, but 26 percent of all passbooks, while they represent

**Table 7.3**                    **Composition of Household Gross Wealth (%)**

Socioprofessional group	Goods for Domestic Use	Financial Assets and Rental Goods	Goods for Professional Use
Farmers	17	29	54
Manufacturers, craftsmen, merchants	24	55	21
Professionals	25	43	32
Senior executives	41	56	3
Intermediate occupations	53	44	3
Employees	58	40	2
Workers	66	32	2
Nonparticipants	35	63	2
Total	38	51	11

*Source:* Malpot and Paquel (1992).

**Table 7.4**                    **Mean Value and Composition (%) of Financial Assets and Rental Goods Held by Households**

Socioprofessional Group	Mean value (thousand francs)	Saving-Banks Passbook	Building-Society Passbooks	Investments, Bonds, and Insurance	Shares	Rental Properties	Lands and Forest
Retired self-employed (nonfarmers)	1,470	8	6	10	23	44	9
Professionals	1,250	6	8	17	25	35	9
Manufacturers, artisans, merchants	1,050	5	6	13	36	34	6
Senior executives	760	9	9	14	40	23	5
Farmers	590	11	13	16	7	19	34
Retired farmers	570	14	13	13	6	27	27
Retired wage earners	530	16	14	13	25	26	6
Intermediate occupations	290	17	15	17	20	26	5
Employees	150	22	14	18	11	27	8
Workers	110	24	18	25	8	20	5
Total	430	12	11	15	24	29	9

*Source:* Malpot and Paquel (1992).

only 17 percent of the whole population. The nonworking population, essentially retired people, holds 46 percent of the total value of financial assets and rental goods, while it represents 36 percent of the whole population.

Considering now total household wealth, self-employed people and wage earners own 27 and 36 percent of its total value, respectively, while they represent 11 and 53 percent of the whole population, respectively.

### 7.2.2 Importance of Debt on the Balance Sheet

Table 7.5 reports the evolution of the net outstanding financial assets and debts of households, at the end of each year, from 1982 to 1991. Because available data give no information on the yearly evolution of household gross (or net) wealth, it is impossible to appreciate precisely how the ratio between net (outstanding) debt and gross wealth has evolved during recent years in France. However, table 7.5 shows that:

- While the amount of household net outstanding debt has strongly increased during the past ten years, the ratio between this amount and the sum of net financial assets and net outstanding debts has remained approximately constant
- The share of medium- and long-term loans (for the most part mortgage loans) in household net outstanding debt has decreased: faced with the slackened growth of their purchasing power, households have increasingly used short-term loans to maintain their consumption levels during recent years.

These observations can be completed with the results of a study by Arrondel and Kessler (1989) using the 1986 Institut National de la Statistique et des Etudes Economiques (INSEE; French National Institute of Statistics and Economic Surveys) Survey on Financial Assets. According to this study, 45.6 percent of French households were indebted in 1986, while an earlier Centre de Recherches Economiques sur l'Epargne, Paris (CREP; Center of Economic Research on Savings) study estimated that this proportion was 39 percent in 1984. In 1986, 25.5 percent of all households were indebted to finance their primary home, 5.1 percent to finance other real estate, 5.2 percent to pay for construction work, and 17 percent to buy consumer durables. Finally, liquidity credits and other credits concerned only 2.6 and 5.6 percent of households, respectively.

Among indebted households, 27.5 percent were indebted for more than one reason: the most frequent combination is a real estate loan (frequently a long-term loan) together with a loan for the acquisition of consumer durables (usually a short-term loan).

The household rate of indebtedness is highest when the head of household is middle-aged at adult ages (73.2 percent for ages between 40 and 44 years old) and increases with household gross wealth and household current income. It is also higher for married couples with two or three children.

**Table 7.5 Household Net Outstanding Financial Assets and Debts (end of year; billion francs)**

	Net Outstanding Financial Assets										Net Outstanding Debts			Ratios (%)
	Liquidities	Investment Securities	Bonds	Shares	Credits	Insurance Reserve	Total (1)	Liquidities	Short-term Loans	Medium- and Long-term Loans (2)	Total (3)	(3)/(1)+(3)	(2)/(3)	
1982	2,212		385	455	338	267	3,656		514	1,022	1,536	29.6	66.5	
1983	2,429		447	721	339	314	4,250	1	534	1,135	1,670	28.2	68.0	
1984	2,579		424	1,006	340	374	4,723		684	1,275	1,959	29.3	65.1	
1985	2,757		380	1,431	349	443	5,360	1	677	1,425	2,104	28.2	67.8	
1986	2,918		491	2,347	412	532	6,701	1	820	1,505	2,236	25.0	67.3	
1987	3,130	7	349	2,232	384	632	6,734	1	940	1,742	2,657	28.3	65.6	
1988	3,365	14	384	3,292	334	771	8,160	2	1,217	1,903	3,122	27.7	60.9	
1989	3,532	4	400	4,293	411	974	9,614	2	1,429	2,026	3,457	26.4	58.6	
1990	3,652	8	382	3,683	504	1,145	9,373	2	1,422	2,166	3,590	27.7	60.3	
1991	3,642	10	412	4,147	478	1,318	10,006	2	1,478	2,223	3,703	27.0	60.0	

Source: Comptes et indicateurs économiques: Rapport sur les comptes de la Nation (1988-91).

Because the 1986 INSEE Survey on Financial Assets does not include any information on household debt incurred for professional reasons, the estimated rate of indebtedness for different socioprofessional groups is necessarily biased. However, Arrondel and Kessler (1989) found that this rate (excluding debt for professional reasons), and the rate for primary-home debt only, were respectively:

- Approximately 60 and 40 percent for those employed in intermediate occupations
- Approximately 55 and 35 percent for executives
- 55 and 28 percent for professionals
- Approximately 53 and 30 percent for the large-business self-employed
- Approximately 50 and 29 percent for qualified workers
- 45.6 and 25.8 percent for the small-business self-employed
- 29.1 and 13.9 percent for nonqualified workers
- 37.2 and 13.3 percent for farmers

### 7.2.3 Mean Net Worth of Households

Malpot and Paquel (1992) have estimated household mean gross wealth and mean debt (not including short-term indebtedness for nonprofessional reasons). On the basis of these two mean estimates, they have deduced an approximate evaluation of the mean net worth of French households in 1988. Their results are reported in table 7.6.

The rankings of socioprofessional groups according to their mean gross and net wealth are approximately the same. The mean net worths of some categories are very close—as for farmers and manufacturers, or for retired farmers and retired wage earners. However, (white-collar) employees and (blue-collar) workers, who hold approximately the same mean gross worth, have more differentiated mean net worths (because of unequal levels of mean indebtedness). Farmers, manufacturers, artisans, and merchants are relatively more indebted for professional reasons. Senior executives, incumbents of intermediate occupations, employees, and workers are relatively more indebted (in the medium and long terms) for nonprofessional reasons.

### 7.2.4 On the Concentration of Wealth

Using data from the 1986 INSEE Survey on Financial Assets, Lollivier and Verger (1990) have shown that, in France, wealth is much more concentrated than income. In fact, the less wealthy half of the population holds only 6 percent of overall gross wealth (including outstanding loans), while the wealthiest 10 percent holds 54 percent of overall gross wealth. However, when households are ranked according to activity income (which includes wages, profits, and pensions, but excludes Social Security benefits and income from personal

**Table 7.6 Mean Net Worth of French Households, 1988 (thousand francs)**

Socioprofessional Group	Mean Gross Worth	Mean Indebtedness			Mean Net Worth
		Professional	Nonprofessional	Total	
Professionals	2,880	191.5	150.3	341.8	2,538.2
Retired selfemployed (nonfarmers)	2,030	7.9	5.4	13.3	2,016.7
Farmers	2,020	315.3	41.4	356.7	1,663.3
Manufacturers, artisans, merchants	1,920	162.8	96.2	259	1661
Senior executives	1,360	6.2	138.5	144.7	1,215.3
Retired farmers	890	18.5	3.5	22	868
Retired wage earners	880	1.5	9.1	10.6	869.4
Intermediate occupations	660	6.1	122.5	128.6	531.4
Employees	370	2.8	61.8	64.6	315.4
Workers	350	2.8	77.4	80.2	269.8
Total	840	27.1	62.0	89.1	750.9

Source: Malpot and Paquel (1992).

assets), the top 10 percent earn only 28 percent of total income. Table 7.7 gives concentration curves for wealth and income in France during 1986.

This survey also shows that the concentration of wealth increases with the population density of the residence area. In rural districts, the wealthiest 10 percent hold 52 percent of the total wealth, while in Paris, they hold 74 percent of the total. Concentration is stronger at both extremes of the income distribution. Among households earning less than 30,000 francs per year, the 10 percent at the upper tail possess 58 percent of the subgroup's total wealth. The percentage held by the top 10 percent is close to 61 percent in the subgroup of households earning more than 300,000 francs per year. It is only equal to 38 percent for households earning between 200,000 and 300,000 francs per year.

Wealth concentration is also very strong among farmers and professionals, the opposite of the case for qualified workers and members of intermediate occupations. Wealth concentration is higher at extreme ages, and lowest for those between the ages of 30 and 40. Finally, wealth concentration is stronger among single individuals and among households receiving no gift or bequest after the death of parents.

### 7.3 The Taxation of Capital Income

First, note that any single individual with a yearly capital income of less than 8,000 francs is exempted from tax on this income; for married couples the amount is 16,000 francs or less. The tax revenue loss generated by this provision was equal to approximately 8.2 billion francs in 1991 (see *Project*

**Table 7.7** Concentration (Lorenz) Curves for Wealth and Income in France, 1986

Quantile	Cumulated Wealth (%)	Cumulated Income (%)
0.05	0.03	0.81
0.10	0.12	2.18
0.15	0.25	3.90
0.20	0.44	6.01
0.25	0.75	8.34
0.30	1.21	10.95
0.35	1.87	13.82
0.40	2.77	16.97
0.45	4.11	20.39
0.50	6.04	24.17
0.55	8.74	28.36
0.60	11.94	32.96
0.65	15.71	37.99
0.70	20.15	43.52
0.75	25.25	49.52
0.80	31.13	56.15
0.85	37.98	63.61
0.90	46.21	72.28
0.95	57.28	82.74

Source: Lollivier and Verger (1990).

for the 1992 Finance Act 1992). This section describes tax legislation as of January 1, 1992.

### 7.3.1 Total Tax Burden on Interest Income

Interest income refers to household income received from fixed-yield or variable-yield investments, such as bonds and other marketable loan certificates, claims, deposits, current accounts, treasury bills, and short-term notes. Such income is subject to specific tax treatment, characterized by flat-rate withholding.

In fact, the beneficiary may require the debtor (or the institution or bank representing this debtor) to convert interest into a standard deduction at source. When this deduction is made, the beneficiary is discharged from the requirement to pay progressive income tax on the interest. This deduction involves two base rates: a 35 percent rate and a 15 percent rate (applied in particular to income from marketable bonds), which are increased to 38.1 and 18.1 percent, respectively, with the application of three additional taxes: (1) the social contribution (1 percent), (2) social withholding (1 percent), instituted in 1987, and (3) the generalized social contribution (1.1 percent), instituted in 1990.

The flat-rate withholding option is reserved for natural persons (as opposed to legal entities) and only allowed for claims and interest with no escalator clause; this includes convertible and profit-sharing bonds. Interest income paid

to persons or corporations not residing in France must be subject to flat-rate withholding. In this case, maximum rates are 15 percent for bond income and 35 percent for other interest income.

Income from marketable bonds includes interest, redemption premiums, and lotteries. Interest yielded by marketable bonds issued before January 1, 1987, is subject to a 10 percent deduction at source made by the issuing legal entity. For redemption premiums and lotteries, the rate of the deduction at source is 12 percent (10 percent for redemption premiums on loans issued after January 1, 1986). When bond interest is subject to a deduction at source, the flat-rate withholding must be decreased by this previous deduction. For example, consider a 100 franc gross interest payment, subject to a 10 franc deduction at source; the theoretical amount of the 18.1 percent flat-rate withholding is 18.10 francs, but its effective amount is  $18.10 - 10 = 8.10$  francs.

When the beneficiary does not choose the flat-rate withholding option, the bond interest is included in taxable income. The taxable amount is then the gross interest before deduction at source, but the amount of this deduction constitutes a tax credit which reduces the progressive tax.

The only short-term notes on which flat-rate withholding can be applied are the ones issued by banks. In this case, the rate, usually 38.1 percent (or 48.1 percent for short-term notes issued before January 1, 1990), is raised to 53.1 percent if the beneficiary does not communicate his identity and residence to the payer institution. Short-term notes issued by corporations other than banks are subject to the 10 percent deduction at source and then to the progressive tax.

For income yielded by investment growth bonds, capitalization, and life insurance contracts, the principle is the following:

- The tax takes the form of a 53.1 percent withholding when the beneficiary chooses a tax anonymity scheme.
- If the beneficiary does not choose a tax anonymity scheme, the tax is due only for contracts subscribed after a given date and may, on the beneficiary's request, take the form of a lower-rate withholding. For subscriptions taken before 1990, the tax concerns contracts with a maturity of less than six years: the withholding rate is 48.1 percent for a maturity of less than two years and 28.1 percent for a maturity between four and six years; for subscriptions taken after January 1, 1990, the exemption concerns contracts with a maturity of more than eight years, and there are only two withholding rates: 38.1 percent if the maturity is less than four years and 18.1 percent if it is between four and eight years.

Income from claims which are nonquoted but tradable in a regulated market (such as commercial paper issued by nonbanking corporations and certificates of deposit reserved for banks) may be subject only to 18.1 percent flat-rate withholding.

### 7.3.2 Tax Burden on Equity Income from Corporations

#### *Dividend Income*

It is interesting to recall that, until 1959, dividends distributed by corporations to shareholders were first subject to a proportional tax (deducted at source by the firm) and then the remaining net sum was included in the shareholder's total income for the calculation of the progressive surtax. For example, given that the proportional tax rate was 0.22 in 1959, if a corporation had to distribute a dividend of 100 francs that year, the shareholder received a net dividend of 78 francs. Then, if the shareholder was liable for a 45 percent progressive surtax, dividend income was subject to a withholding equal to  $78 \times 0.45 = 35.10$  francs, so that the effective income was equal to

$$(1 - \tau_{\text{div}})(1 - \tau_{\text{corp}})100 = (1 - 0.45)(1 - 0.22)100 = 42.90 \text{ francs.}$$

The act issued on December 28, 1959, suppressed the proportional tax on dividends and kept up a deduction at source for investment income, which was finally suppressed for any natural or legal resident person by the act issued July 12, 1965. Moreover, this act allowed a 50 percent tax credit to beneficiaries of dividends. The principle of this tax credit is the following: whenever a firm liable for corporate tax distributes a dividend of 100 francs, the shareholder receives a total income of 150 francs, composed of the 100-franc coupon she cashes and the amount of 50 francs that is deducted from the tax on the 150 franc dividend income.

If, for example, the shareholder is subject to a 40 percent income tax rate, then her tax on a dividend income of 150 francs (including the tax credit of 50 francs) is calculated as follows:  $(150 \text{ francs} \times 0.40) - (\text{tax credit of } 50 \text{ francs}) = 10 \text{ francs}$ . So the effective income after tax is 90 francs. This example shows that the after-tax net income of a shareholder receiving a dividend income of 100 francs, accompanied by a tax credit of 50 francs, is exactly the same as the one resulting from a dividend of 150 francs without any tax credit. When the corporate tax rate was 50 percent (from 1958 to 1985), the distribution of a 100 franc dividend by a firm required a 200 franc profit; the distribution of a 150 franc dividend with the same profit could have been possible were the corporate tax rate 25 percent. Consequently, the tax credit for distributed dividends grants shareholders a kind of rebate on the corporate tax.

Reductions of the corporate tax rate to 45 percent in 1986 and 1987, then to 42 percent in 1988, have implied that the corporate tax rate effectively burdening distributed profits has been simultaneously lowered from 25 percent to 17.5 percent, and then to 13 percent. Successive reductions of the corporate tax rate to 39 percent in 1989, 37 percent in 1990, and 34 percent since 1991, have not changed the effective rate of 13 percent on distributed profits, because the distribution of a dividend is now accompanied by an additional tax intended to set the corporate tax rate at 42 percent.

To illustrate this point, let us assume that a firm has realized a 100,000-franc

profit during fiscal year 1992. This profit implies a corporate tax of 34,000 francs and leaves an available profit of 66,000 francs. If the firm decides to distribute this whole amount to shareholders, it is subject to an additional tax of 8,000 francs, corresponding to the difference between the 42 percent tax rate and the 34 percent one. Note that this additional corporate tax represents 8/66ths of the available profit (after the 34 percent tax) and 8/58ths of the distributed dividends (equal to  $66,000 - 8,000 = 58,000$  francs). For this reason the legislation states that the additional corporate tax to be paid in the case of distributed dividends must be equal to “8/58 of the net distributed amount.”

### *Capital Gains*

1. Capital gains resulting from a transfer (for valuable consideration) of a shareholding representing more than 25 percent of the equity of a firm subject to corporate tax are subject to a 18.1 percent tax. Transfers without valuable consideration, via inheritance or donation to the spouse, a descendant, or an ascendant, are exempted from tax. However, this exemption can be annulled if, within five years, the transferee sells at least one of these shares to someone not a member of the transferor's family.

2. When the transfer concerns less than 25 percent of the equity of a firm subject to corporate tax, the tax rate is 18.1 percent if the total transfer during the fiscal year is greater than 316,900 francs (in 1991). This taxation scheme applies to quoted securities (shares, bonds, nonvoting preference shares, equity shares), application rights on such securities, mutual funds, but also to shares of nonquoted firms subject to corporate tax.

3. When a transfer for valuable consideration concerns shares of a nonquoted property development company, capital gains are taxable as ones yielded by the sale of private buildings.

4. When capital gains are made by one of the partners working in a partnership firm that is not subject to corporate tax, they are taxable as professional capital gains. Since September 1990, capital gains made by nonworking partners have also been taxable. The single tax rate is 18.1 percent.

### 7.3.3 Average Marginal Tax Rate on Capital Income

The marginal tax rate (MTR) and average marginal tax rate (AMTR) on capital income (interest income, dividends, capital gains) during 1989 are given in table 7.8. The calculation of MTR and AMTR are based on a 1 percent and a - 100 percent variation of capital income or dividends, respectively. In other words, AMTR is calculated by setting the corresponding income category to zero. The MTR and AMTR on dividends are lower than the corresponding ones on capital income excluding dividends. This is the direct consequence of the tax credit scheme applied to dividends.

### 7.3.4 Wealth Taxes

The 1989 Finance Act instituted a yearly wealth tax, called *Impôt de Solidarité sur la Fortune* (ISF), only slightly different from the previous wealth

**Table 7.8** Marginal and Average Marginal Tax Rates on Capital Income, 1989

	MTR (%)	AMTR (%)
Capital income	16.1	8.8
Dividends	13.4	7.6
Other capital income	17.4	13.6

Source: Réponse au questionnaire O.C.D.E. sur la fiscalité de l'épargne (1992).

tax, called Impôt sur les Grandes Fortunes (IGF), which was applied from 1982 to 1986. The new yearly wealth tax has the following characteristics:

- It is exclusively a personal tax, with an application threshold of 4,390,000 francs since 1992
- It concerns all goods and assets making up the household net wealth, including any held by nonemancipated minor children
- The most important exemption concerns goods for professional use
- Its rate is progressive: the 1992 tax scale consists of five bands with progressive rates of 0.5, 0.7, 0.9, 1.2, and 1.5 percent
- The tax amount may be reduced according to the household income value;
- The ISF must be calculated by taxpayers themselves and paid when the yearly declaration of wealth is made.

Taxable wealth consists of all real estate (land, houses, etc.), business assets and goodwill, securities, claims, movables, and personal estate (cars, gold, cash, foreign currency, etc.). In addition to goods for professional use, exemption is given to works of art, rights of literary and artistic ownership, patent rights whenever these rights are included in the inventor's wealth, and rural goods on long leases. In 1992, the rates of the ISF are the following:

For the fraction of the taxable net wealth

- below 4,390,000 francs: 0 percent
- between 4,390,000 and 7,130,000 francs: 0.5 percent
- between 7,130,000 and 14,150,000 francs: 0.7 percent
- between 14,150,000 and 21,960,000 francs: 0.9 percent
- between 21,960,000 and 42,520,000 francs: 1.2 percent
- above 42,520,000 francs: 1.5 percent

Valuation of wealth subject to the ISF is made according to the following principles:

1. Real estate is appraised at its market value, defined as the price at which it could have been sold at the beginning of the fiscal year. The valuation must take into account real estate characteristics and maintenance, but also legal causes of depreciation, such as renting agreements.

2. Listed bonds and shares are appraised according to closing prices on the last day of the year preceding the tax declaration; their valuation may be alternatively calculated as the mean of the last 30 quotations of the previous year. The market value of unquoted shares is based simultaneously on their yield value, on the value of firm net assets, and on growth prospects of the firm.

3. Claims are valued at their nominal value, increased with accrued interest.

4. Jewels cannot be appraised at a value lower than the one fixed in an insurance contract.

5. Movableables may be valued on an inclusive basis, set to 5 percent of the whole value of other nonexempted wealth components. Tangible property (including cars, boats, race horses, etc.) must be valued at its market value.

Debts to be paid to banks and other credit institutions (including debts contracted for the acquisition of real estate) may be deducted from taxable wealth.

Total wealth and income taxes that must be paid in the same year cannot exceed 85 percent of income and interest (subject to withholding taxes) realized during the previous year. If a surplus is observed, it must be deducted from the ISF. For example, consider a person whose net wealth is evaluated at 40 million francs on January 1, 1992, and so, who owes under the ISF 353,420 francs. If his or her 1991 taxable income and interest consists of an income of 500,000 francs (subject to an income tax of 207,000 francs) and bond yields of 150,000 francs (subject to a withholding tax of 25,500 francs), the total wealth and income taxes amount to  $353,420 + 232,500 = 585,920$  francs. The upper limit under the 85 percent ceiling is  $650,000 \times 0.85 = 552,500$  francs. Consequently, there is an excess of  $585,920 - 552,500 = 33,420$  francs, which must be deducted from the ISF, which finally amounts to  $353,420 - 33,420 = 320,000$  francs.

During 1990, 140,461 tax declarations were subject to the ISF, and the payment of this tax yielded a total of 6,061 million francs: from 1989 to 1990, the number of declarations and the amount of tax paid increased by 11.2 percent and 6.1 percent, respectively. (See Gambier and Mercier 1992.)

### 7.3.5 Inheritance Taxes

When an inheritance passes to a spouse or an individual in the direct lineage, the calculation of inheritance taxes is the following:

- Since January 1, 1992, a personal tax exemption of 330,000 francs applies to the spouse's share; an exemption of 300,000 francs applies to the share of each child or ascendant.
- After application tax exemptions, the share of any heir is subject to progressive rates, between 5 and 40 percent. Initially, the rates increase rapidly: for example, a 20 percent rate applies to any child on the part above 100,000 francs, and to the spouse on the part above 200,000 francs. Then the tax scale increases less progressively: higher rates apply only on the

part above 3,400,000 francs for any heir. More precisely, the rate is 30 percent for the fraction between 3,400,000 and 5,600,000 francs, 35 percent for the fraction between 5,600,000 and 11,200,000 francs, and 40 percent for the fraction above this last amount.

- Any testamentary heir with three or more children is eligible for a reduction of 4,000 francs per child after the third one.

When inheritance concerns collaterals or nonrelatives, exemptions are very low and rates particularly high:

- For bequests between brothers and sisters, the rate is 35 percent and goes up to 45 percent for the fraction above 150,000 francs
- For bequests between uncles (or aunts) and nephews (or nieces), or between first cousins, it is uniformly equal to 55 percent,
- It is uniformly equal to 60 percent for relatives above the fourth degree of kinship (e.g., grandparents' grandparents) or for nonrelatives.

Goods to which inheritance taxes apply must be estimated at the date of death. This estimation concerns business and real estate, quoted and nonquoted shares, and movables. Among exclusions, the most notable are: (1) life insurance policies taken out by the decedent (however, the fraction above 200,000 francs of premiums paid after the age of 70 is subject to inheritance taxes), (2) woods and forests (up to three-quarters of their value), (3) rural goods long leases (up to half or three-quarters of their value, and when they are transferred free of charge for the first time), and (4) works of art donated to the state with its approval.

Inheritance taxes can be avoided to a certain extent through donations. Generally, donations are subject to the same tax rates as inheritances, but with the following particularities: (a) debts entailing donated goods cannot be deducted, and (b) the donor may pay taxes usually incumbent on the donee: thus, for the same total disbursement, the donor may increase the donee's wealth in this way.

In the case of a donation partition, taxes are reduced by 25 percent if donors are under age 65, and by 15 percent if they are between 65 and 75 years old. Donations of equity shares to the benefit of a firm's employees may give rise to a tax reduction of 100,000 francs for each beneficiary, if the Finance Ministry consents.

When a firm is transferred through inheritance or donation, tax payment may be deferred for five years from the date payable and then split into twenty-one installments over ten years (the interval between two successive installments being six months). This measure applies to individual industrial, commercial, craft, agricultural, or professional firms, but also to nonquoted shares of such firms, provided that the beneficiary receives at least 5 percent of the capital. Taking advantage of this deferral requires the payment of interest, whose basic rate is reduced proportionally as the heir's or donee's share increases. The rate

of interest is reduced still more when beneficiaries are collaterals or nonrelatives. (See Gambier and Mercier 1992.)

### 7.3.6 Tax Treatment of Consumer Debt

Interest on consumer debt is generally not deductible from income tax, except for interest on debt contracted for the acquisition, building, repair, or amelioration of property.

## 7.4 Employment-linked Retirement Saving

### 7.4.1 Tax Treatment of Employer-provided Pensions

According to French social legislation, any wage earner must be affiliated with a basic pension (Social Security) plan and then to a complementary pension plan. Wage earners may be also obligated to support another complementary (called “overcomplementary”) pension scheme, either within their firm or within their line of work.

Contributions to obligatory plans are deductible. However, deduction is allowed only below some fixed amount, which depends on the total yearly amount of employee’s and employer’s contributions to basic and complementary pension schemes and to complementary provident funds. The upper limit was 209,395 francs in 1991. Contributions to optimal or voluntary plans, however, are nondeductible.

Private or public retirement pensions are included in the calculation of the taxable income. They are subject, first, to a 10 percent tax reduction with a lower limit of 1,800 francs for each pensioner, and an upper limit of 29,300 francs for the total amount of retirement pensions received by household members; then, to a 20 percent tax reduction, with an upper limit of 125,200 francs for each pensioner. The net amount of public and private retirement pensions (calculated after the two successive tax reliefs) is added to the whole taxable income of the household.

The payment of capital within the framework of a private pension plan is not taxable. Tax legislation does not stipulate any penalty in the case of withdrawal from a private pension plan.

Life annuities in return for payment are subject to taxation only on a given proportion of their amount. This proportion is a function of the annuitants’ age when they take possession of the annuities. It is fixed at: 70 percent under age 50, 50 percent between ages 50 and 59, 40 percent between ages 60 and 69, and 30 percent over age 69.

### 7.4.2 Private Pensions in Saving and Retirement Income

To complete individual retirement income resulting from obligatory pension plans (i.e., Social Security and complementary pension plans), insurance companies and banks offer “capitalization contracts” to firms and households,

among which we can distinguish: (1) individual contracts, collective contracts, or collective contracts with individual adhesion; (2) contracts in which the contribution is payable by the employer, by the employee, or by both; (3) contracts with predefined contributions or with predefined benefits, and (4) contracts involving (obligatory or optional) life annuities.

Individual contracts include individual savings plans (called “PEPs”) and life-insurance contracts, which will be presented in sections 7.5 and 7.6, respectively.

Among capitalization contracts signed inside the firm, two kinds of contracts may be distinguished. They are identified by the number of the corresponding article of the Internal Revenue Code (IRC). The first kind consists of contracts specified by article 83 of the IRC which may be signed in the framework of either a collective agreement or a firm agreement; they concern either the whole personnel of the firm or a homogeneous category only, such as executives; the retirement funds are supported by employer contributions, and eventually by employees’ contributions. The second consists of contracts specified by article 82 of the IRC which are subscribed to and financed by the employer to the benefit of appointed employees.

These “article 82”-type contracts may involve either predefined contributions or predefined benefits. The predefined contributions comprise a given percentage of the employee’s wage, the employee keeping the benefit of the accumulated capital if he or she leaves the firm. In the case of predefined benefits, the firm offers to all or part of its personnel an additional retirement pension whose level is equal to some percentage of the employee’s last wage before retirement. The firm may also complement the amount of individual retirement income with “hat” insurance (*retraite “chapeau”*), such that the total amount equals some given percentage of the employee’s last wage for each year of service in the firm (such contracts are sometimes called “article 39”-type contracts).

In this case, contributions are exclusively chargeable to the employer: the aim is to develop personnel loyalty, because eventual extra pensions are paid only to employees still occupied in the firm at the date of their retirement. The firm may also transfer its commitments to an insurance company; however, the insurance company may change substantially the level of contributions paid by the firm. In fact, the insurance company must achieve actuarial balance between contributions and returns on their investments on the receipt side, and pensions to be paid and charges on the expense side.

Funded pension plans are offered by life insurance companies but also by other bodies, such as institutions coming under the French Mutual Insurance Company (Mutualité Française) and distributing the “Mutex” contract to firms or to their members.

A firm savings plan (*plan d’épargne d’entreprise* [PEE]) may be set up inside a firm agreement; it is funded by the employee’s contributions (eventually chosen to benefits from profit sharing) and by a lump sum paid by the firm.

This lump sum may be restricted to plan management charges, its ceiling value is 10,000 francs per year (15,000 francs in the event that the employee purchases the firm's shares), and it must be lower than three times the employee's contribution. The employee's contribution as set out in the agreement may reach 25 percent of wages. Devoted to the purchase of securities, stocks, and bonds, PEEs benefit from tax incentives: given that invested sums are held for at least five years, returns and capital gains from the plan are tax-exempt. The PEE may be converted into a life insurance contract allowing the payment of a taxable life annuity from the date of retirement (see section 7.4.1 for tax rates applied to life annuities).

Unfortunately, available statistics do not permit us to identify precisely (1) the amount of contributions paid by firms preparing complementary retirement pension plans for (some of) their employees and (2) banking investments corresponding to individual long-term savings, which will be withdrawn essentially during the retirement period.

#### 7.4.3 Severance Bonuses for Retirement and Early Retirement

Several measures have been taken to ensure replacement income for wage earners who come to the end of their working lives or who resign, agree to cut back their working hours, or get laid off. These measures include:

- The special allowance of the French National Employment Fund (Fonds National pour l'Emploi [FNE]), which is provided to older workers when they are subject to economic redundancies or when they agree to change from full-time to part-time employment
- The Solidarity Contracts for progressive early retirement
- The progressive retirement system, which permits to workers over age 60 who have made 150 quarterly payments to the Social Security System, to receive part of their retirement pension while continuing to work part-time.

The FNE agreements are concluded between firms and the state. Older workers who are laid off by a firm that has concluded a FNE agreement are eligible for a special allowance equal to 65 percent of the reference daily wage, if this wage is lower than 390.25 francs (the threshold wage on January 1, 1992), and equal to 50 percent of the reference daily wage, if it is higher than 390.25 francs. The reference daily wage is calculated from wages earned during the past twelve months. The FNE special allowance is paid until the beneficiary is 65 years old, or until the beneficiary (if more than 60 years old) has made 150 quarterly payments to the Social Security system. To be eligible for the FNE special allowance, a laid-off worker must be more than 55 years old and must have been employed in the firm for at least twelve months prior to dismissal.

A firm that has reached an FNE agreement contributes to the special allow-

ance according to a rate depending on its size: on average, 6 percent for firms with fewer than 500 employees, and 8 percent for firms with more than 500 employees or belonging to a trust.

A firm laying off a worker over age 50 must pay a contribution to the Association for Industrial and Commercial Employment (ASSEDIC) when an FNE agreement has not been previously reached.<sup>4</sup> The amount of this contribution varies from one to six months' gross wages, according to the age of the laid-off worker at the time of dismissal.<sup>5</sup> The rate of this contribution is reduced by half for firms that normally have fewer than twenty employees. For the firm, this contribution is deductible from its corporate tax.

Under an act issued July 30, 1987, any retirement is accompanied by the payment of compensation defined as follows. In the case of voluntary retirement of an employee over age 60, the employee receives either the indemnity fixed by the law or the indemnity fixed by the collective agreement or by the labor contract (if this amount is greater). The indemnity fixed by the law is equal to: half the monthly wage when the employee's seniority is greater than ten years; one month's wages when it is greater than 15 years; one-and-a-half month's wages when it is greater than 20 years; or two months' wages when it is greater than 30 years. In these cases, the monthly wage is calculated as the mean wage over the past twelve months, or as the mean wage over the past three months if this is greater.

In the case of retirement initiated by the employer, the law distinguishes between two situations:

- If conditions for compulsory retirement are fulfilled (i.e., if the employee is eligible for the full-rate pension and is older than the compulsory retirement age fixed by the collective agreement or the labor contract), then the employee is entitled either to the official redundancy payment or to the contractual redundancy payment, which may be higher. The official redundancy payment is equal to one-tenth for each year of seniority in the firm (if seniority is between two and ten years), or one-tenth per year plus one-fifth per year above the tenth year of seniority (this gives, e.g., 7.9 months for a seniority of 33 years).
- If the above conditions are not fulfilled, compulsory retirement is considered a redundancy. The employer then must respect the stipulated procedure, and the redundancy must be justified by a cause such as the reduction of professional abilities due to age. Otherwise, the employer may be ordered to pay damages to the employee.

4. The age limit at which such contributions are required was previously 55 years old: it was lowered to 50 years old on August 1, 1992.

The ASSEDIC is the institution that manages the payment of unemployment insurance.

5. The number of paid months increases with the age of a dismissed worker.

Beneficiaries of severance pay for (early) retirement may divide the taxable amount of this pay in four equal parts over the four successive years following the year of payment. In general, this option is attractive because taxable income during the years immediately after retirement is usually lower than in the last working year. The tax-exempted portion of severance pay is 20,000 francs. But in the case of retirement or early retirement initiated by the employer, the exemption may reach the level of the severance pay defined by collective, professional, or interprofessional agreements.

#### 7.4.4 The Social Security Replacement Rate

The general Social Security pension scheme involves any wage earner in the trade, industrial, craft, or service sectors.<sup>6</sup> In return for contributions withdrawn from monthly wages at the rate of 15.80 percent, any wage earner receives a full-rate retirement income when he reaches age 65, or age 60 if he or she has made 150 quarterly payments to the Social Security System. The full rate is 50 percent of the mean yearly wage, which is calculated over the ten “best” years (after 1948). Deductions are applied to wage earners who are less than 65 years old and have contributed fewer than 150 quarterly payments. For example, the rate is 37.5 percent at ages 60, 61, or 62, when 140 quarterly (35 years) payments have been made. In fact, the amount of the basic Social Security pension ( $P$ ) is calculated as:

$$P = \bar{W} \times T \times \frac{N}{150},$$

where  $\bar{W}$  is the mean yearly wage calculated over the ten “best” years for the fraction below the stipulated upper limit,<sup>7</sup>  $T$  is the pension rate, and  $N$  is the number of quarterly payments made to the Social Security plan. In the previous example,  $T = 0.375$  and  $N = 140$ . In the normal case,  $T = 0.50$  and  $N = 150$ .

Generally, given the adjustment rates and the upper limits used for the calculation of  $\bar{W}$ , the Social Security retirement income is frequently lower than half of the effective mean wage resulting from the ten “best” years. It is particularly true for people who earned more than the Social Security ceiling wage: the replacement rate of their Social Security retirement pension can be much lower than 50 percent of the last wage they earned.

Such replacement rates have been recently calculated for a sample of individuals born in October 1922 and surveyed in 1988 (see Lacroix 1991; and table 7.9 below). Estimates show, for example, that women whose last monthly

6. Administration officials and salaried farm employees are insured by special pension plans. However, the Social Security regime is extended to nonsalaried categories, such as students, artists, and actors.

7. Wages of the ten “best” years and their corresponding upper limit are adjusted according to yearly varying rates. On July 1, 1991, e.g., these rates were 1.721, 5.843, and 15.942 for the years 1980, 1970, and 1960, respectively. The corresponding upper limits of  $\bar{W}$  are 103, 466, 105, 174, and 109,043 francs, respectively (the Social Security monthly wage ceiling was 11,620 francs).

**Table 7.9** Mean Replacement Rates of Retirement Pensions for Individuals Born in 1922 and Surveyed in 1988

Last Monthly Wage (francs)	Men			Women		
	Global	Social Security Pension	Complementary Pension	Global	Social Security Pension	Complementary Pension
<5,000	1.13	0.86	0.27	0.95	0.72	0.23
5,000–6,000	1.02	0.75	0.27	0.79	0.60	0.19
6,000–8,000	0.93	0.63	0.30	0.79	0.57	0.22
8,000–10,000	0.84	0.52	0.32	0.75	0.49	0.26
10,000–12,000	0.83	0.43	0.40	0.74	0.41	0.33
12,000–16,000	0.77	0.34	0.43	0.69	0.34	0.35
>16,000	0.66	0.20	0.46	—	—	—

Source: Lacroix (1991).

Note: The last monthly wage and the retirement income are net of social contributions.

wage was less than 5,000 francs have a global replacement rate equal to 95 percent and a Social Security replacement rate equal to 72 percent; for men whose last monthly wage was greater than 16,000 francs, these two replacement rates are equal to 66 and 20 percent, respectively.

#### 7.4.5 Health Expenses<sup>8</sup>

The French health-care system of social insurance (the so-called *Sécurité Sociale*) was set up in 1945 with the objective of guaranteeing health care for all, especially children, mothers, and retired workers. The legislators' concern was clearly equality of access. Thus the 1958 hospital reform defines the notion of public duty (*mission de service public*) which mandates access to hospital care for all. The system is based on both the notions of insurance and of solidarity. Risk sharing applies, as in insurance, but contributions are compulsory, are related to income rather than risk, and entitle the insured and family to open-ended benefits. The system is based on a three-tier solidarity principle: between the sick and the healthy, the young and the elderly, and the poor and the wealthy. It is divided into three main branches: Assurance Maladie (health insurance), Assurance Vieillesse (pension fund), and the Branche Famille (family benefits).

In 1990, the total share of GDP allocated to health-care spending rose to 8.9 percent, or 538 billion francs. Its rather rapid growth over the past decade has been of growing concern to policymakers.

Today, more than 98 percent of the population is covered under three main national health insurance funds: salaried workers (75 percent) under the

8. This subsection is largely based on a paper written by Lise Rochaix (1992). I wish to thank her for giving me permission to use some parts of her text.

CNAMTS (Caisse Nationale d'Assurance Maladie des Travailleurs Salariés) also called the Régime Général, agricultural workers (8 percent) under the MSA (Mutualité Sociale Agricole), and the self-employed (7 percent) and the remaining 10 percent of the population under about fifteen different special funds.

Contributions to the Régime Général are compulsory and paid by the employees and employers: their shares are, respectively, 30 percent and 70 percent, although these rates may vary across occupational regimes. In 1990, up to 73.6 percent of health-care expenditures were financed by Sécurité Sociale. The state and local authorities contributed 1.1 percent through earmarked taxes on households and 19.2 percent through earmarked taxes on private insurance. The remaining 6.1 percent was paid by the "*mutuelles*" (a kind of nonprofit insurance society). Originally, the *mutuelles* offered insurance to those not covered by Sécurité Sociale. With the extension of Social Security to the vast majority of the population, they now tend to restrict themselves to refunding the cost-sharing element.

For ambulatory care and drugs, the insured generally pays the service charge in full and receives a refund at a fixed rate, depending on the occupational regime. It is usually 75 percent for medical services and 70 percent for pharmaceuticals. The remaining copayment, the so-called *ticket modérateur*, can be partly or totally refunded by private complementary insurance schemes (including *mutuelles*). However, at least 10 percent of the insured suffering from long-term serious illness (such as cancer) are totally or partially exempted from copayment. But the *ticket modérateur* can rise to 40 percent for some pharmaceuticals that are considered nonessential. A small but increasing proportion of pharmaceuticals are actually nonrefundable.

For hospital expenditure, Sécurité Sociale acts as a third-party payer, and patients make only the copayment, which cannot exceed 20 percent of the total bill, exclusive of expensive services. The same principle applies to diagnostic hospital services provided on an outpatient basis and to costly drugs and laboratory tests. In fact, only 4 percent of hospital resources are actually directly financed by households, and only 10 percent of hospital days bear a copayment.

A survey (Bocognano et al. 1992) conducted in 1991 by the Centre de Recherche, d'Etude et de Documentation en Economie de la Santé (CREDES; Center of Research Studies and Documentation on Health Economics) on a sample of households including at least one person covered by Sécurité Sociale shows that:

- 7.8 percent of surveyed individuals are partly or totally exempted from copayment (*Ticket modérateur*); this percentage increases with age (see table 7.10)
- 84 percent are covered by complementary health insurance; as shown in table 7.10, this share decreases with age; among these individuals, 61 per-

**Table 7.10** Individuals Exempted from Copayment and Covered by Complementary Health Insurance, 1991 (% of age group)

Age	Exempted from Copayment (%)	Covered by Complementary Health Insurance (%)
<16	1	84
16-39	4	82
40-64	11	87
65-79	26	85
≥80	41	67

Source: Bocognano et al. (1992).

cent are complementarily covered by *mutuelles*, 24 percent by insurance companies, and 15 percent by *caisses de prévoyance* (provident societies)<sup>9</sup>

- The mean monthly expenses paid by an individual for ambulatory care and drugs are strictly increasing with age (see table 7.11)
- 3.2 percent of the sample has been hospitalized at least once in the three months before the survey; this rate increases with age (2.4 percent for people less than 16 years old, 3.3 percent for those between 16 and 39 years old, 3.1 percent for those between 40 and 64 years old, and 4.7 percent for those more than 65 years old)

## 7.5 Targeted Saving Incentives

During the past ten years, several measures have been taken to stimulate household saving. New products have been successively offered, such as the individual savings passbook (*livret d'épargne populaire*), the industrial development savings account (*compte pour le développement industriel* [CODEVI]), long-term savings commitments (*engagements d'épargne à long terme*) up to 1982, the savings plan provided within the framework of the law promulgated by then Finance Minister Monory (in effect up to 1982), the stock market investment savings account (*compte d'épargne en actions* [CEA]) from 1983 to 1988, the individual retirement plan (*plan d'épargne retraite* [PER]) in 1988 and 1989, the individual savings plan (*plan d'épargne populaire* [PEP]) since January 1, 1990, and finally the stock market investment savings plan (*plan d'épargne en actions* [PEA]) since September 1992.

Common characteristics of these products are the nontaxation of their interest payments below some ceiling value and a deduction of the invested amount from taxable income or a limited tax cut.

9. The percentages covered by *mutuelles*, insurance companies, and *caisses de prévoyance* are respectively 59, 26, and 15 percent for people less than 65 years old and 72, 10, and 18 percent for people more than 65 years old.

**Table 7.11 Mean Monthly Expense (in francs) Paid by an Individual for Ambulatory Care and Drugs, 1991**

Age	Mean Monthly Expenses for:	
	Ambulatory Care	Drugs
<16	80	21
16-39	87	31
40-64	136	47
>65	210	97

Source: Bocognano et al. (1992).

Interest yielded by deposits in savings passbooks, CODEVIs, and building society savings accounts and plans are exempted from income tax.

The two main saving incentive schemes, which are associated with a premium assigned by the state, are (1) the building society savings account (*compte d'épargne logement* [CEL]) and the building society savings plan (*plan d'épargne logement* [PEL]) and (2) the individual savings plan (PEP). We will discuss these in detail.

### 7.5.1 Building Society Savings Accounts and Plans

The main characteristic of these plans and accounts is that they can be borrowed against (usually for home acquisition).

#### *Building Society Savings Account (CEL)*

The rate of return on deposits is 2.75 percent. The premium rate is 1.25 percent in the case of mobilization of loan rights: the upper limit of the premium is 7,500 francs. The ceilings for deposits and loans are 100,000 and 150,000 francs, respectively. The lending rate is 4.25 percent, and the minimum duration of deposits required for the granting of a loan is eighteen months. At the end of December 1991, the number of accounts opened was 8,550,000, and total deposits and loans were 123 and 63 billion francs, respectively.

#### *Building Society Savings Plan (PEL)*

The rate of return on deposits is 6 percent, including the premium rate of 1.5 percent, the upper limit of the premium being fixed at 10,000 francs. The ceilings for deposits and loans are 400,000 and 600,000 francs, respectively. The lending rate is 6.32 percent. The minimum and maximum lengths of this plan are four and ten years, respectively. At the end of December 1991, 10,550,000 PELs were currently subscribed, and total deposits in and loans on these plans were 471 and 170 billion francs, respectively.

Table 7.12 gives the evolution of total deposits and distributed premiums (i.e., the income paid) on such accounts and plans from 1989 to 1991. In this

**Table 7.12 Evolution of CEL and PEL Deposits and Premiums (billion francs)**

	1989		1990		1991	
	CEL	PEL	CEL	PEL	CEL	PEL
Total deposits at the end of December	120	448	119	459	123	471
Distributed premiums	0.90	7.6	0.96	9.2	0.91	7.9

Source: *Rapport annuel au Conseil National du Cr dit* (1992).

table, distributed premiums concern rights relative to accounts or plans that come to maturity and are closed within a given year, and from which deposits have been withdrawn.

In fact, after steps taken in 1982 and 1983 to raise ceiling values and rates of return, the growth of deposits in CELs and PELs was particularly strong up to 1989 and then slackened. This slackening may be explained by the low return rates of CELs and PELs relative to those of more recent products (such as short-term UCITSs and PEPs), but also by the extension of the tax-exemption scheme to such alternative products. However, 33 percent of households participated in a CEL or a PEL in 1992 (see Arrondel et al. 1992).

### 7.5.2 Individual Savings Plan (PEP)

Individual savings plans (PEPs), offered since 1990 by banks and insurance companies, have replaced individual retirement plans (PERs). The number of PEPs opened in 1990 (nearly 7 million) and the total deposits during the same year (112 billion francs on December 31, 1990) testify to the success of this new product.

The authorized upper limit on saved capital is 600,000 francs for a single taxpayer or 1,200,000 francs for a household, which may open two plans. Interest is tax-free capitalized inside the PEP, if there is no withdrawal during the first eight years. At the end of a PEP, the subscriber can choose either the use of the tax-free saved capital or the payment of an annuity exempted from any income tax. If the plan takes the form of a life insurance contract, the subscriber benefits from the corresponding tax exemption.

The duration of a PEP is at least eight years but usually ten; the plan is contractually renewable up to ten years. After the tenth year, the plan is no longer provisioned but still runs tax-free: partial withdrawals are possible and do not induce the closure of the plan.

In fact, withdrawals are possible at any date, but returns from the plan are taxed if the withdrawal takes place during the first eight years. In this case, returns may eventually be subject to flat-rate withholding of 38.1 percent if the duration of the plan is less than four years and 18 percent if the duration is between four and eight years. Any withdrawal before the tenth year implies the closure of the plan.

However, a tax-exempt withdrawal is possible at any time in the following

cases: death, disability, end of eligibility for the unemployment insurance system, liquidation subject to court supervision (the event may concern either the plan holder or his spouse if either subject to common taxation). Except in the case of death, which implies immediate plan closure, the tax-free withdrawal may occur during the two years following the event.

Deposits made during the first ten years by persons domiciled in France who are not subject to income tax are entitled to a state premium equal to 25 percent of the annual payment; the upper limit of the yearly premium is 1,500 francs per year. The premium is capitalized with the official rate of interest. The sum of yearly premiums and of their capitalized interests is paid by the state either ten years after the opening of the plan or at the date of closure (if this closure happens between the eighth and tenth years of the plan). The premium is not paid when a withdrawal is made before the eighth year (except in the cases listed above).

At the end of December 1990, total current deposits in PEPs and corresponding yearly premium entitlements were, respectively, 112 and 2.3 billion francs. One year later, they were, respectively, 199 and 2.5 billion francs. The rates of return announced for 1990 and 1991 were between 8 and 9 percent.

Characteristics of PEPs vary among the institutions that offer them to the public. The structure of investments, eventual penalties for withdrawal or transformation before the deadline, terms of payments or withdrawal, management charges, and performances (which may be guaranteed or not, indexed or not) make the PEP a differentiated product.

Contractual savings (mainly PELs and CELs) and PEPs opened in banks amounted to 649.3 billion francs in 1992. Their share of household financial assets (excluding UCITS investments and insurance reserve) was 12.6 percent in 1988, 13.5 percent in 1989, 16.3 percent in 1990, and 19.1 percent in 1991.

### 7.5.3 Stock Market Investment Savings Plan (PEA)

Since September 1992, a new product has been offered to the public by banking institutions: the stock market investment savings plan (PEA). This type of savings plan, oriented toward stock market investments, benefits from tax exemptions after the sixth year.

More precisely, returns of savings invested in a PEA are capitalized totally tax-free (exempted from taxation on income and capital gains) and the tax credit (see section 7.3.2) is refunded in the plan after the sixth year. The minimum length of the plan is eight years. Complete or partial withdrawal before this deadline implies plan closure. Any withdrawal made before the sixth year results in taxation at a flat 18.1 percent on returns and capital gains (including the tax credit) above the yearly threshold of 316,900 francs. Before the sixth year, returns are exempted. There is no ceiling for yearly deposits, but there is a global upper limit of 600,000 francs for a single holder, or 1,200,000 francs for a married couple.

A PEA consists of essentially two kinds of products: shares of French com-

panies listed on the Paris Bourse and mutual funds (*Sociétés d'investissement à capital variable* [SICAV] and *fonds communs de placement* [FCP]) invested primarily in French shares. Holders can modify the structure of their PEAs: they may transfer some shares to buy others or prefer one SICAV to another.

Many PEA plans offered by banking institutions make a capital guarantee. The holder is then assured of keeping the invested amount. Moreover, some plans allow an investor to benefit from the upward movement of stock prices without being affected by downward movement. It is still too early to evaluate the success of this new product.

## 7.6 Insurance as a Saving Vehicle

### 7.6.1 Life Insurance and Capitalization Contracts

In addition to life insurance contracts, capitalization contracts are the main saving vehicle offered to households by insurance companies. Life insurance contracts for natural persons may be subdivided into two types of agreements. The first is insurance coverage “in case of decease,” which implies the payment of capital to assignees when the insured person dies before contract termination. The second is insurance coverage “in case of life,” which involves the payment of accumulated savings to the insured person if he or she is still alive at contract termination; the payment may be realized either as the payment of capital or as the payment of a life annuity that complements, for example, individual retirement pensions.

Capitalization contracts are similar to this second type of life insurance contract. The subscriber pays a premium capitalized by the insurance company with a guaranteed minimum rate. At contract termination, the company pays the capital back to subscribers, or eventually to their assignees. Today, capitalization contracts are often used as complements to retirement pension plans (see section 7.4.2).

Although the growth rate of life insurance turnover slackened slightly in 1990,<sup>10</sup> this turnover reached a particularly high level at the end of the eighties (167.5 billion francs in 1990). The mean contribution per resident was 3,100 francs in 1990.<sup>11</sup> Total contributions to life insurance contracts “in case of life” amounted to 124.5 billion francs in 1990 (up 19.0 percent over the previous year): because of the continuous growth of their contributions, such contracts represented 74 percent of total life insurance turnover in 1990 (they represented 26 percent of this turnover in 1980). Among all contributions paid for such contracts, the amounts corresponding to individual, “open group,” and

10. The growth rate of life insurance turnover was + 20 percent (approximately) in 1988 and 1989, and + 15.4 percent in 1990 (see *L'assurance française en 1990 1991*).

11. The same year, it was equal to 7,000 francs in Switzerland, 4,700 francs in Finland, and 4,400 francs in Great Britain.

collective contracts were equal to 41.4, 67.2, and 15.9 billion francs, respectively, in 1990.<sup>12</sup> In the same year, contributions to life insurance contracts “in case of decease” amounted to 37.2 billion francs. They can be divided into parts of 6.8, 9.0, 1.9, and 19.5 billion francs, corresponding to complementary guarantee, individual, “open group,” and collective contracts, respectively.

After a sharp increase from 1984 to 1989, capitalization contract turnover fell drastically in 1990: it was then equal to only 39.0 billion francs (down 29.6 percent from the previous year). This decrease may be explained primarily by the reassignment of savings to individual savings plans (PEPs).

Table 7.5 (section 7.2) gave the evolution of insurance reserves in household net current financial assets: over the past decade, their share of these assets grew from 7.3 percent in 1982 to 13.2 percent in 1991.

### 7.6.2 Tax Treatment of Accumulations through Insurance Policies

Premiums provided by life insurance contracts with a maturity greater than six years are eligible for a 25 percent tax reduction before their incorporation into taxable income. However, this reduction can be applied only on the fraction of the premium under 4,000 francs (plus 1,000 francs for each dependent child).

Life annuities in return for payment are taxable only on a given proportion of their amount (see section 7.4.1).

Returns provided by capitalization contracts are subject to income tax at contract termination. Taxable returns are equal to the difference between the amount refunded and the premiums paid. The beneficiary may choose the flat-rate withholding scheme: for contracts subscribed after January 1, 1990, the rate is 35 percent when the contract maturity is strictly less than four years, and 15 percent when the contract maturity is greater than four years. These rates are raised by 3.1 percent for persons domiciled in France. Returns are tax-exempt when contract maturity is greater than eight years.

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12. Collective contracts include the ones subscribed by firms to provide their employees with complementary retirement pension plans.

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