INTERNATIONAL BONNARD LAWSON LAW FIRM

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Swiss Lump Sum Taxation

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How to pay less taxes in Switzerland…

…Being foreigner and rich

…Being Swiss and poor

by Mix et Remix - in RTS.ch

1. History

- Introduced in **1934**: A specific tax regime was adopted for a certain category of foreigners residing in Switzerland without carrying out a lucrative activity in Switzerland

- In **1940**, the Swiss Government confirmed this specific taxation procedure for foreigners in its "National Defense Tax Decree"

- In **1948**, art. 18bis was introduced – covering the "taxation based on the spending" (*imposition d'après la dépense/forfait – lump sum taxation*)

- **1993-95**: enactment of the Harmonized Federal Direct Tax Act (HDTA) and Federal Direct Tax Act (FDTA), which concretized the "modern" lump sum tax regime

- January 1st, **2001** – Deadline for the cantons to include the Federal provisions on lump sum taxation in their cantonal tax law

- New regime starting from **2016**

2. Current situation in Switzerland

- At the cantonal level:

  - Zurich abolished the lump sum taxation in 2009 – voted by the people (approx. 200 lump sum taxpayers in Zurich at the end of 2008)
  - Followed by Schaffhausen (in 2011), Appenzell-Ausserrhoden (in 2012), Basel-Land (in 2012), Basel-Stadt (in 2012)
  - Other cantons, such as Geneva and Vaud have maintained the lump sum tax regime and have reinforced it

- At the federal level

  - Initiative to abolish the lump sum tax regime in 2012.
  - Vote on November 2014: Swiss voters decided to maintain the lump sum tax regime by 59,2%...
  - At the same time, this vote confirmed the entry into force of the new Swiss federal provisions in 2016.

3. Numbers

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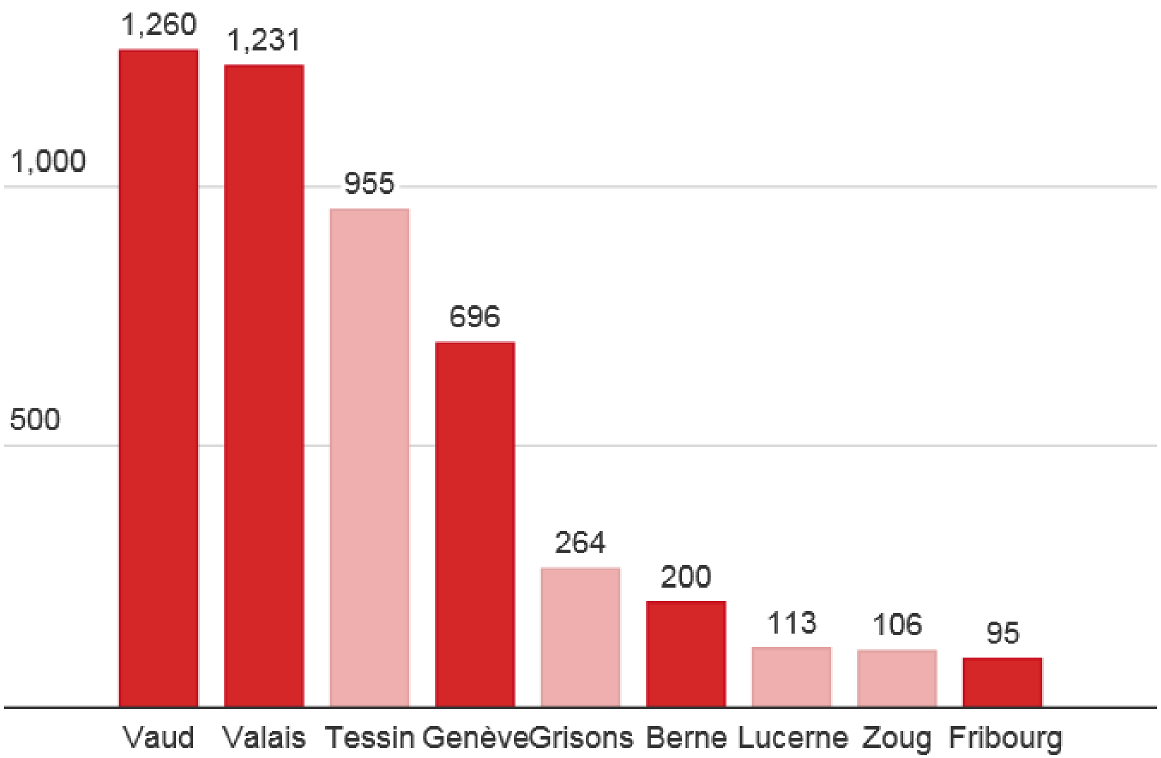
- End of 2014, there were 5’382 lump sum tax payers in Switzerland
- 4,5% less than in 2013
- Notably Zurich, Basel, Schaffousen, and Aarau have abolished the regime at their cantonal levels.



Source: Group of Cantonal Finance Directors – press release dated May 26, 2015 – le Temps dated May 26, 2015

3. Numbers (2)

- The total tax revenue increased to 740 million between 2012 and 2014
- The lowest taxation amounted to CHF 10’000
- The highest taxation amounted to CHF 7’753’188
- The average taxable amount also increased to CHF 137’495

Schweiz	**2006**	**2008**	**2010**	**2012**	**2014**
Recettes de l'impôt fédéral (en mio. de CHF)	105	154	204	192	202
Recettes des impôts cantonaux (en mio. de CHF)	176	271	300	325	344
Recettes des impôts communaux (en mio. de CHF)	111	152	165	178	194
Recettes totales (en mio. de CHF)	**392**	**578**	**668**	**695**	**740**
Quel est le montant forfaitaire encaissé le plus bas (en CHF) ?	2'000	10'046	10'000	10'000	10'000
Quel est le montant forfaitaire encaissé le plus élevé (en CHF) ?	2'713'400	23'210'876	11'969'000	8'230'326	7'753'188

Source: Group of Cantonal Finance Directors – press release dated May 26, 2015

4. How does it work?

- **Subjective conditions**:

An individual may benefit from the Swiss lump sum tax regime if:

1. DOMICILE OR STAY IN SWITZERLAND

- Fully liable to tax in Switzerland for the first time or after an absence of ten years;
- Taking domicile or spending at least 90 days per year in Switzerland;
- Fictive domicile does not give right to lump sum taxation.

2. NO LUCRATIVE ACTIVITY

- Not carrying out a lucrative activity in Switzerland;
- Activity abroad is compliant with the lump sum taxation as long as the taxpayer keeps his/her domicile in Switzerland.
- Specific cases: artists and sportsmen

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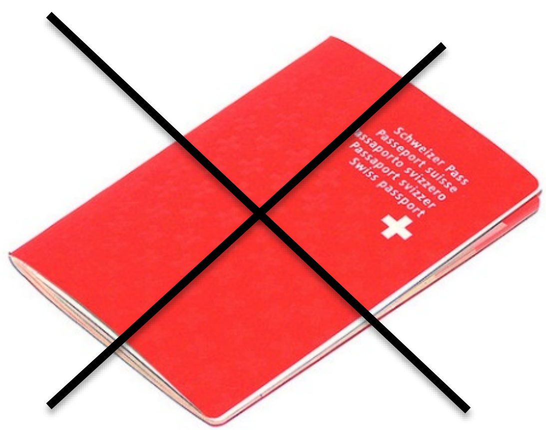
4. How does it work? (2)

- **<u>Subjective conditions</u>**:

3. NATIONALITY

- Not having the Swiss nationality.
- Spouses leaving in the same household shall fulfill all the conditions



4. How does it work? (3)

- **<u>Objective conditions</u>**:

1. LIVING EXPENSES

- ➢ The taxable basis is determined based on the Swiss and foreign living expenses of the taxpayer including any dependent persons living in Switzerland.
- ➢ Basis: - food and clothing;
  - housing, including charges, cleaning, maintenance of the garden, etc.;
  - personnel charges;
  - education, travels, holidays;
  - maintenance of expensive domestic animals (horses, etc);
  - maintenance and using of cars, yachts and aircraft, etc.;
  - other living costs.
- ➢ Minimum at the federal level, alternatively, the highest of the below:
  - CHF 400’000
  - <u>seven times</u> the rental value of the home owned by the taxpayer;
  - <u>seven times</u> the rent he pays for the living place;
  - <u>three times</u> the pension for the living place and food.
- ➢ The taxable basis is negotiated with the cantonal tax authorities

4. How does it work? (4)

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- **Objective conditions**:

2. CONTROL CALCULATION

- The taxable basis determined based on the living expenses may not be lower than the control calculation.
- Control calculation provides that the taxable basis should not be lower in any case than the Swiss source income and any foreign source income for which the taxpayer requires the application of a DTT.
- Are taken into account:
  - Swiss based real estate income;
  - Swiss source income derived from movable capital;
  - Swiss source income from movables (rather rare);
  - Income from copyrights, patents and other IP exploited in Switzerland;
  - Swiss source pensions;
  - Foreign source income for which the taxpayer claims treaty benefits.
- Deductible costs: maintenance and management costs of real estate in Switzerland and usual costs of management of movable capital.

5. Example

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- Mr. & Mrs Gibbs, both UK national, 70 and respectively 67 y.o. are moving to Switzerland, in the canton of Geneva, to enjoy their retirement.

- They are looking to buy a property of approximately CHF 8 millions - annual rental value: CHF 80’000.

→ Annual income tax subject to ordinary rate:

Income tax:	CHF 7 x 80’000 = CHF 560’000
Taxable wealth:	increase of the lump sum tax base by 10%
TOTAL TAXABLE INCOME:	CHF 560’000 + (10% of 560’000) = CHF **616’000**
ANNUAL TAX LIABILITY:	CHF **224’000**, i.e. around **36%**

5. Example

- If Mr & Mrs Gibbs move to the canton of Schwyz:

Income tax:	CHF 7 x 80’000 =	CHF	560’000
Taxable wealth:	CHF 20 x 560’000 =	CHF	11’200’000

TAX LIABILITY:

Income tax CHF 120’000
Wealth tax CHF 17’700

TOTAL TAX LIABILITY **CHF 137’700**, i.e. around **24,6%**

6. Taxation procedure

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1. **TAX RETURN AND CHOICE**
   - Taxpayer has to file each year the “simplified” tax return providing information regarding the taxable basis and the control calculation.
   - For each tax period, the beneficiary of the lump sum tax regime can opt between the lump sum tax system or the ordinary taxation.

2. FINAL TAX LIABILITY
   - Income tax: The highest amount of tax between the tax amount computed on the living expenses and the one determined based on the control calculation is due.
   - Wealth tax: no harmonized system between cantons. Geneva and Vaud do not levy wealth tax.
   - Ordinary tax rates are applicable on the taxable basis and on the control calculation.

3. CONTRAVENTION AND OFFENCE
   - Lump sum tax payer is subject to tax provisions on contravention and offence.
   - Not disclosing all his income in the control calculation which would be higher than the lump sum taxation may constitute a tax avoidance.

7. Tax at source and DTTs

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1. REFUND OF SWISS WHT

- Lump sum tax payer may get the refund of the Swiss WHT even though the income subject to Swiss WHT did not influence the final tax liability

2. REFUND OF FOREIGN TAX AT SOURCE

- Lump sum taxpayers may in principle benefit from the advantages of DTTs
- Foreign source income benefiting from a DTT has to be added to the income in the control calculation
- Lump sum tax payer may obtain the refund of the foreign tax at source levied according to the foreign domestic law which exceeds the reduce treaty rate.
- Only a part of the foreign tax at source, levied in line with the DTT, can be credited against the taxes paid in Switzerland *(imputation forfaitaire*) by the lump sum tax payer.

7. Tax at source and DTTs (2)

3. PARTICULARITIES

- DTTs with Germany, Italy, Austria, Belgium, USA, Canada; Denmark and Norway:
  - DDTs concluded with these countries do not provide for treaty relief to lump sum tax resident
  - Lump sum taxpayers are not qualified as resident in Switzerland as long as all income attributed to Switzerland under the DTT is not subject to tax.
  - The foreign tax at source would not be reduced and the Swiss domestic credit system is not available.

- In order to benefit from the relief at source provided in the above DTTs, the lump sum taxpayer has to include in the control calculation all income derived from those States (*modified lump sum taxation*).
- Such income is also taken into account for the progression of the tax rate.
- DTT with France…another story…

8. Alternatives

1. Tax shield (*Bouclier fiscal*)

- For some specific cases, tax shield is more favorable than lump sum taxation
- Available notably in the cantons of Geneva, Vaud, Valais, Berne, Luzern
- In the canton of Vaud: cantonal and municipal income and wealth tax cannot exceed 60% of the net income
- For the application of the tax shield, tax authorities takes into account a minimum income of 1% of the net wealth

2. Ordinary taxation…?

- Lump sum taxpayers are subject to inheritance tax even in direct line
- Up to 6% in direct line if the deceased person benefited from a lump sum tax regime once in the three years preceding his death (art. 6A, Geneva cantonal inheritance tax law - D 3 25)

9. Other important considerations

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- **Gift and inheritance taxes**
  - Lump sum tax payers are subject to normal Swiss gift and inheritance tax (Schwyz and Obwald have abolished these cantonal taxes)
  - Not due in direct line in most of the cantons
  - In Geneva, lump sum taxpayers are subject to a fix rate of 7% even in direct line or for the surviving spouse.
  - **Advice on estate planning prior to immigration to Switzerland is essential**

- **Immigration aspects**
  - EU citizens:
    - Free movement of persons
    - Anti-immigration vote of February 9, 2014 to be implemented soon

  - Non-EU citizens:
    - May obtain a residence permit based on the fact that they will provide substantial tax revenues to
    - Increase of the lump sum tax basis
    - Minimum taxable basis range from CHF 750’000 to CHF 1’500’000.

9. Other important considerations

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- **Swiss social security contributions**
  - Residents of Switzerland, older than 25, without gainful activity have to contribute to the Swiss social security until the age of 65 for men and until the age of 64 for women

- **International private law**
  - Highly recommended to review certain civil law aspects before immigrating to Switzerland
  - Matrimonial regime, possible changes to be made to pre-nuptial agreements or testaments, adding provisions on the choice of applicable law, etc.

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