

New Circular Letter on Lump-Sum Taxation in Switzerland

September 4, 2018

Key points

- The Swiss Federal Tax Administration published a new circular letter on lump-sum taxation.
- The circular sets out a minimum taxable income of CHF 400,000 even if the living expenses are lower.
- The stricter rules will be applied to everyone from 1 January 2021.

Lump-Sum Taxation

In Switzerland, foreign wealthy families often benefit from special tax deals: lump-sum taxation or *forfait fiscal* in French. Instead of paying tax on the worldwide income and assets, the tax is calculated based on the living expenses.

The Swiss Federal Tax Administration Published a New Circular on 24 July 2018

The Swiss Federal Tax Administration (the “Administration”) published on 24 July 2018 a circular letter summarizing the legal framework and the practice of the Administration and of the cantonal tax authorities (the “Circular”).

The Circular:

- confirms the transitional period of five years for taxpayers who applied for the lump-sum taxation after 1 January 2016;
- confirms that the new rules adopted in September 2012 will apply to all deals from 1 January 2021;
- sets out a minimum taxable income of CHF 400,000.

General Conditions

The Swiss lump-sum tax regime can only be applied to individuals who:

- do not have Swiss citizenship;

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- take up residency in Switzerland for the first time (or after an absence of 10 years); and
- do not perform any commercial activity (employed or self-employed) in Switzerland. According to the Circular, performing a commercial activity in Switzerland means carrying out any type of employment (main or auxiliary, employed or self-employed) in the Swiss territory generating income in Switzerland or abroad; it is unclear at this stage how the cantonal tax authorities will interpret the Circular in this respect, in particular regarding foreign athletes.

In the case of married couples, both partners must fulfill the requirements to benefit from the lump-sum taxation.

Living Expenses

The relevant living expenses include:

- cost of food and clothing;
- housing costs;
- expenses for education;
- travel expenses;
- maintenance costs for vehicles

The total living expenses have to:

- reach a multiple of the annual rental value of the taxpayer's home (if owned) or of the annual rent paid; and
- be at least equivalent to the taxes on the income from Swiss sources at the ordinary tax rate.

In practice, the total living expenses are frequently agreed with the cantonal tax authorities in order to represent a multiple of the annual rental value of the taxpayer's home or of the annual rent paid. Under the new legislation (since 1 January 2016), the annual living expenses must correspond to at least seven times the annual rental value of the taxpayer's home or the annual rent paid.

The Circular explicitly provides that, if the taxpayer has more than one real estate property in Switzerland, the highest annual rental value or rent paid has to be taken into consideration.

Lump-sum taxation is not available in all of the cantons. For example, the canton of Zurich decided to abolish it. At the federal level, lump-sum taxation is possible only if it is also granted at the cantonal level. The cantonal tax authorities of the cantons of Geneva, Vaud and Valais are very attractive to tax wealthy families on a lump-sum basis.

Control Calculation

Swiss law provides that every taxpayer that is subject to the lump-sum tax regime has to establish a "control calculation" on an annual basis (with the annual tax return). The amount of tax payable under the lump sum taxation has to exceed the income tax which would be due under the ordinary system on the gross income from Swiss sources, including financial assets (e.g., shares and bonds). The Circular specifies that

Swiss-sourced financial assets mean that the issuer of the security must be a Swiss resident; the physical location of the security is not relevant. The control calculation also comprises foreign-sourced income (e.g., dividends, interests and royalties) for which the taxpayer wants to claim for partial or total exemption of foreign withholding taxes under a double tax treaty.

Specific regulations are applicable with respect to the double tax treaties with Austria, Belgium, Canada, France, Germany, Italy, Norway and the United States.