

## TAX INFO: Proposed Modifications to the Expatriate Ordinance

The tax allowances for special professional expenses shall in principle be maintained, but will be more restrictive and the ordinance's scope of application shall be limited.

Whether, resp. to which extent, and when the proposed modifications will enter into force, lies within the competence of the Swiss Federal Department of Finance.

Our tax specialists are available to answer any questions you may have or to advise you with regard to your specific needs.

### Introduction

Under the current state of law, so-called expatriates, i.e. key employees and specialists with special professional qualifications, are entitled to claim additional tax deductions (special professional costs). The legal basis for this is the Expatriate Ordinance (Ordinance governing the deduction of specific professional costs [for federal direct tax purposes] of key employees and specialists temporarily working in Switzerland, hereinafter "ExpaV", SR 642.118.3).

Two parliamentary motions submitted in 2009 and 2012 (no 12.3510; no 12.3560) called for an abolition of such tax allowances as they would privilege expatriates over other taxpayers to an unjustified extent. The Swiss Federal Council, although rejecting the cited motions, set up a working group to review the current deductions. The working group concluded that although the deductions provided for in the ExpaV represent professional costs and do have a sufficient legal basis in art. 26 Federal Direct Tax Act ("FDTA", SR 642.11), the ExpaV has some weaknesses.

Based on the results of the working group, the Swiss Federal Department of Finance (FDF) proposes the following modifications to the ExpaV:

- Limitation of ExpaV's scope of application;
- Clarification of the deductions for housing costs, schooling fees and lump-sum deduction;
- Changes in the salary certificate with regard to employer benefits;
- Repeal of FTA Circular of April 7, 1988, on (schooling) contributions from international companies for the children of foreign workers.

On April 10, 2014, FDF launched a three-months hearing on the planned changes. The Federal Tax Administration (FTA) is currently evaluating the results from the hearing and will thereafter prepare a proposal to the FDF based on the results. According to the FTA, the probability that the ExpaV will be revised is high. Whether, resp. to which extent, the proposed modifications will enter into force, lies however within the competence of the FDF. According to the FTA, the format decision will be expected in autumn 2014. In case the FDF will

decide to revise the Expav, the revised ordinance will enter into force either already on 1 January 2015 or on 1 January 2016.

## Comparison: Current Tax Allowances versus Proposed Modifications

| Art. of Expav   | Current law<br>(wording of legal act in italics)  | Proposed modifications<br>(wording of legal act in italics)   |
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| Art. 1:<br>Scope of application                           | <p><i>a. key employees temporarily posted by their foreign employer to Switzerland; b. specialists of any kind performing a timely limited task in Switzerland [...]</i></p> <ul style="list-style-type: none"> <li>- The term "specialist" not only includes IT specialist, but also professional athletes, doctors and healthcare professionals. Only the employment in Switzerland with a fixed-term contract is required.</li> </ul>  | <p><i>a. key employees and specialists with special professional qualifications temporarily posted by their foreign employer to Switzerland (Expatriate) [...]</i></p> <ul style="list-style-type: none"> <li>- The posting element shall be required also for specialists;</li> <li>- Posting means that the employee intends to return to prior place of residence in the foreseeable future.</li> </ul>                          |
| Art. 2 Abs. 1 lit. a:<br>Deduction for travel expenses    | <i>a. the usual travel expenses between the foreign place of residence and Switzerland</i>  | <i>a. the necessary travel expenses between the foreign place of residence and Switzerland</i>  |
| Art. 2 Abs. 1 lit. b, (c):<br>Deduction for housing costs | <p><i>b. necessary housing costs in Switzerland;</i></p> <p><i>c. reasonable living costs in Switzerland under the condition that a permanent residence is maintained in the home country.</i></p> <ul style="list-style-type: none"> <li>- Deduction for reasonable housing costs in Switzerland is possible also in case the property abroad is rented out;</li> <li>- In certain cantons deduction of housing costs will not be granted in case the property is rented out;</li> <li>- Other cantons only grant the difference between the housing costs in Switzerland and the foreign income from real property to be tax deductible.</li> </ul> | <p><i>b. reasonable housing costs in Switzerland in case a permanent residence abroad for exclusive personal use is maintained.</i></p> <ul style="list-style-type: none"> <li>- Deduction for reasonable housing cost in Switzerland will be granted under the condition that the permanent residence abroad is for exclusive personal use only;</li> <li>- No deduction will be granted if the property is rented out.</li> </ul> |

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| Art. 4:<br>Lump-sum deduction for relocation, travel and housing costs   | <ul style="list-style-type: none"> <li>- Based on the wording it is not clear whether the lump-sum deduction shall be granted also in case deduction for housing costs is rejected because no permanent residence abroad is maintained; cantonal practices vary.</li> </ul>       | <ul style="list-style-type: none"> <li>- Lump-sum deduction shall only be granted in case permanent residence abroad for exclusive personal use can be evidenced.</li> </ul>  |
| Art. 2 Abs. 2 lit. c:<br>Deduction for private school fees   | <p><i>c. Ordinary expenses for attendance of a foreign-language private school by the minor children, if the public schools do not offer adequate teaching</i></p> <ul style="list-style-type: none"> <li>- Unclear what kind of costs are part of schooling expenses.</li> </ul> | <p><i>c. Expenses for minor foreign-language speaking children for tuition at foreign-language private schools, if the public schools do not offer classes in the respective language.</i></p> <ul style="list-style-type: none"> <li>- The expression "costs of tuition" implies a restrictive application;</li> <li>- Expenses for food or transportation, costs of care before and after classes are not deductible;</li> <li>- In case the child speaks the language in which the public tuition is held, teaching costs are no longer tax deductible.</li> </ul> |
| Art. 2 Abs. 2 lit. c:<br>Declaration in the salary certificate (no amendment of the ordinance, but amendment of para. 60 "Guideline on the salary certificate" ) | <p><i>Such lump-sum expenses include in particular lump-sum allowances for expatriates according to the Federal Ordinance. In this case it is required to indicate the wording "Expatriate Lump-sum expenses" in the appropriate box.</i></p>                                     | <p><i>Professional expenses remunerated in the form of a lump-sum allowance shall not be declared under para. 13.2.3, but have to be added to the salary under para. 2.3 with the remark "lump-sum Expatriate".</i></p> <ul style="list-style-type: none"> <li>- New is that employer with approved expense regulations are required to indicate the amount of professional expenses on the salary certificate para. 13.1.2;</li> <li>- Increased transparency; administrative overhead for employers with expense regulation.</li> </ul>                             |

## Impact on Companies and their Payroll

Under the current law, the amount of special professional costs borne by the employer must be specified in para. 13.1.2 of the salary certificate, if the employer has no approved expense regulation. Employers with approved expense regulation are currently not required to indicate such amount in the salary certificate, the indication of the wording "effective expatriate expenses" in para. 13.1.2 is sufficient. According to the FDF it is not appropriate that the amount of special professional cost borne by the employer does not have to be specified in para. 13.1.2. FDF therefore suggests to delete the last sentence of para. 57 of the guideline on the salary certificate so that also employers with approved expense regulation would be required to indicate the amount of special professional costs in para. 13.1.2.

In addition, para. 60 shall be modified so that lump-sum expenses shall not be declared under para. 13.2.3, but have to be added to the salary under para. 2.3 with the remark "lump-sum expatriate". Amongst other things, this would have the consequence that special professional costs paid to the expatriate in the form of a lump-sum payment would increase gross wage and thus be subject to 1st and 2nd pillar social security contribution.

## International Comparison: Tax Treatment of Expatriates in Belgium, the Netherlands and the United Kingdom

|                       | Belgium   | Netherlands   | United Kingdom  |
|-----------------------|---|---|---|
| <b>Pre-requisites</b> | <ul style="list-style-type: none"> <li>- Executives, directors, researcher or specialists;</li> <li>- Non-resident in the sense of the Belgium income tax law;</li> <li>- Temporary employment in an international group in Belgium.</li> </ul> | <ul style="list-style-type: none"> <li>- Workers must have specific skills that are not adequately available on the Dutch labor market;</li> <li>- Recruitment from abroad;</li> <li>- Employer must be subject to tax in the Netherlands.</li> </ul> | <ul style="list-style-type: none"> <li>- No special expatriate status.</li> </ul> |

| <b>Deductions for Expatriates</b> | <ul style="list-style-type: none"> <li>- Expatriate remuneration such as tax equalizations, cost of living, rental costs, etc. are reimbursed by the employer and not taxable for the employee;</li> <li>- Relocation, settlement costs and tuition costs are tax deductible without limitation.</li> </ul> | <ul style="list-style-type: none"> <li>- "30% ruling" as tax regime for expatriates: tax free reimbursement of the employer which shall not be higher than 30% of total remuneration;</li> <li>- Teaching costs that were paid by the employer are not taxable for the employee.</li> </ul> | <ul style="list-style-type: none"> <li>- No special tax allowances for expatriates;</li> <li>- In case conditions of the tax status "resident but not domiciled" (remittance basis) are fulfilled, expatriates may claim to be taxed accordingly;</li> <li>- Attractive regime for exemption of days physically performed outside of UK.</li> </ul> |
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## Conclusion

In view of an increase of legal certainty, the confirmation of the currently applicable deductions for expatriates is to be welcomed. However, the FDF has missed the opportunity to create with the ExpaV an internationally competitive instrument for the relocation of highly qualified employees and their families.

The tax allowances for special professional expenses shall in principle be maintained, but will be more restrictive and the ordinance's scope of application shall be limited. The proposed regulation would lead to a unification of currently applicable cantonal practices. Therefore, the transparency will be increased and the no longer existing judicial enforceability rebuilt.

The proposed amendments to ExpaV will have an impact not only on the expatriate's tax burden, but also on the companies' payroll. Companies employing expatriates should analyze the modification's impact on tax and social security before the revised ordinance will take effect.

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