International Bar Association

Search IBA…

# Tax and immigration planning and compliance for high net worth individuals - Taxes Committee newsletter article, August 2018

**Thursday 30 August 2018**

**Back to Taxes Committee publications**

Ruth Bloch-Riemer

*Bär & Karrer, Zurich*

**ruth.blochriemer@baerkarrer.ch**

*Report on Wealth Management Workshop I at the 18th Annual Tax Planning Strategies – US and Europe Conference in Amsterdam*

**Wednesday 11 April 2018**

**Session Co-Chairs**
Alan W Granwell *Sharp Partners PA, Washington, DC*
Daniel Simon *Collyer Bristow, London*

**Speakers**
Ruth Bloch-Riemer *Bär & Karrer, Zurich*
Bruno Gangemi *Macchi Di Cellere Gangemi Studio Legale, Rome*
Rachel Mainwaring-Taylor *Farrer & Co, London*
Zhanna A Ziering *Caplin & Drysdale, New York*

## Introduction

The session focused on four relevant aspects of high net worth (HNW) individuals and their advisers when reviewing relocation options, particularly to Switzerland, Italy, the United Kingdom and the United States:

1. How do you become a tax resident or tax domiciled in the four jurisdictions and what is the difference between residency and domicile?
2. What are the tax consequences of becoming resident or domiciled in the four jurisdictions?
3. What key pre-immigration steps should an individual take?
4. How and when does an individual lose his/her residency or domicile status and what are the potential tax consequences of doing so?

The panel discussion was based on the assumptions that the relocating HNW individuals and their families derived all of their wealth from legal sources, are fully tax compliant in their home jurisdiction, report all of their offshore structures, do not intend to avoid or evade the Common Reporting Standard (CRS), and will comply with all laws and regulations applicable in their new jurisdiction.

## Relevant practical aspects for relocating HNW individuals and their families

Whereas the panellists recognised important differences with regard to the four core questions of the jurisdictions represented on the panel, the panel discussion also reflected that, with respect to many aspects, the continental European jurisdictions, that is, Switzerland and Italy, and the Anglo-Saxon jurisdictions, that is, the UK and US, each have comparable solution concepts.

The panellists' discussion, furthermore, showed that diligent pre-immigration and pre-emigration planning is recommended to review the key taxation aspects of relocation and identify whether measures have to be implemented with regard to the individuals' wealth and estate planning when relocating to a new jurisdiction. Due to the evolving tax, legal and regulatory framework, and the complex cross-border aspects that need to be considered in each individual's and family's specific case, sufficient time is necessary to assess and implement relocation.

## The four questions

The discussion's principal results can be summarised as follows:

### *Question 1: How do you become a tax resident or tax domiciled in the four jurisdictions and what is the difference between residency and domicile?*

SWITZERLAND

Tax domicile and tax residency have the same meaning and, according to Swiss domestic tax legislation, can be established for income and wealth, as well as inheritance and gift tax purposes by either: (1) a physical presence with the intention to stay permanently; or (2) a generally uninterrupted physical presence of 30 days (in the case of professional activity) or 90 days (without a professional activity) in the country. In some cases, domicile is established by an operation of law (eg, for minors).

In practice, the tie breaker clauses contained in Switzerland's large network of double taxation treaties on income and wealth taxation, and in certain Swiss double taxation treaties on inheritance taxation, provide procedures to allocate the tax domicile of a person with a nexus to more than one country. Tax domicile typically is allocated to the place where a person has his/her centre of vital interests.

It is recommended that written documentation evidences the physical presence or absence, for example, by way of a calendar, and substantiates, by objective standards, the centre of vital interests.

(Swiss) citizenship is not relevant for becoming a Swiss taxpayer.

ITALY

An individual is considered resident in Italy for income tax purposes if, for the greatest part of the year (ie, 183 days), any of the following requirements is met:

- the individual is registered in the register of the Italian resident population;
- the individual has *residency* (ie, place of habitual abode, physical presence and intention to live permanently) in a place in Italy; or
- the individual has his/her *domicile* (ie, centre of vital interests, manifested mainly by interest of economic, professional, social, moral and familiar nature) in Italy.

The registration in the register of Italian resident population constitutes a non-rebuttable presumption of tax residence in Italy.

Citizenship is not relevant.

UK

In the UK, a distinction is drawn between the concept of domicile and the notion of residence:

- Domicile as a typical common law concept that reflects the legal 'home' of a person, and UK legislation differentiates between a person's domicile of origin (usually the place where an individual or his/her father was born), domicile of choice and deemed domicile.
- Residence is perceived as a more technical connector because it is generally based on a statutory 'day count' test; rules are provided for automatic non-residence and residence. Overall, a combination of the number of ties to the UK and the day count are relevant.

US

US legislation provides for three options on how to become a US taxpayer:

- US citizenship subjects an individual to worldwide income and transfer taxation, irrespective of where he/she resides or whether he/she has other passports.
- Domicile (established for aliens by living in the US with no present intention of leaving the US, ie, individual's intent to make the locality a fixed and permanent home) determines whether a non-citizen is subject to worldwide estate, gift or generation-skipping taxation. While a person may have more than one residence, he/she can have only one domicile.
- Residence determines whether a non-citizen is subject to worldwide income taxation. Individuals who are 'green card' holders, satisfy the substantial presence test or elect residence are considered US income tax residents.

### *Question 2: What are the tax consequences of becoming resident or domiciled in the four jurisdictions?*

ITALY

Tax residence in Italy leads to the following consequences:

- Individual income tax: taxation of worldwide income (43 per cent maximum rate; 26 per cent tax on passive income; new special tax regime for new residents), including filing obligations. Typically, the valuation of assets is a relevant planning element: if the origin jurisdiction imposes an exit tax, taxation in Italy will be based on market values; otherwise, acquisition costs are decisive.
- Wealth tax is not imposed on moveable assets (other than foreign financial instruments: 0.2 per cent); Italy, however, levies a real estate property tax on Italian real estate (0.76 per cent) and on foreign real estate (0.76 per cent).
- Inheritance and gift tax is levied at comparably moderate rates, ranging from four per cent to eight per cent, with a credit imputed for foreign taxes.

US

A US taxpayer (including an individual holding a green card at any time during the tax year) is subject to worldwide taxation as follows:

- Income taxation: Double taxation is generally avoided through foreign tax credits. Under the US controlled foreign corporation (CFC) and global intangible low-taxed income and passive foreign investment company rules, income of non-US corporations may be taxed if certain requirements are met. In addition, there are special rules for non-US trusts that need to be considered in relocation planning.
- The US does not impose a general wealth tax. State and local governments, however, may impose a property tax.
- Transfer taxation generally applies to US citizens, irrespective of where domiciled, and non-citizen individuals domiciled in the US with respect to lifetime gratuitous transfers and testamentary gifts at a maximum rate of up to 40 per cent. As of 2018, an exemption amount of $11.18m will apply for individuals and $22.36 for married couples; these exemption amounts are scheduled to increase with inflation for each year until 2025, at which time, the exemption amounts are scheduled to revert to the 2017 levels adjusted for inflation.

Important planning tools are the treaty tie-breaker rules applicable where an alien (including a green card holder) is classified as a US tax resident but, at the same time, classified as a tax resident under the domestic law of a country that has entered into a bilateral income tax, or estate or gift tax treaty with the US.

Furthermore, specific attention must be paid to the complex US tax reporting and international compliance form filing requirements.

SWITZERLAND

Tax residents are subject to unlimited tax liability as follows:

- reporting and taxation of worldwide income, with relevant exemptions based on domestic law (eg, private capital gains, foreign real estate or business income) or double taxation treaties; Switzerland, and the Swiss cantons and municipalities apply progressive tax rates, with significant differences between cantons and municipalities;
- reporting and taxation of worldwide wealth (including, *inter alia*, non-Swiss bank accounts and art) on a cantonal and municipal level, with relevant exemptions based on domestic law (real estate and business abroad) or certain double taxation treaties, at a progressive tax rate, with moderate differences between Swiss locations; and
- inheritance and gift tax is levied on cantonal/communal level only, with tax rates, exemptions and details of legislation varying considerably among the cantons. Inheritance and gift taxation is triggered for gifts and successions of Swiss residents and/or transfer of Swiss situs real estate; the recipient in Switzerland or abroad is liable for tax in the relevant canton, and typically has filing obligations. Note, the lump-sum (forfait) taxation

regime does not cover inheritance and gift tax but may have detrimental effects on these taxes.

UK

UK legislation provides for the following tax consequences, depending on the connecting factors:

- UK resident and domiciled individuals are subject to income tax and capital gains tax on worldwide income and gains are subject to inheritance tax on a worldwide estate.
- UK resident (but not domiciled) individuals may claim taxation on the remittance basis: The UK does not levy tax on foreign income/gains unless this income or these gains are remitted to the UK. A remittance basis charge is levied after seven years of residence in the UK. Inheritance tax is levied on UK situs assets only. If an individual was a UK resident but not domiciled for 15 out of 20 years, he/she would be deemed domiciled for inheritance tax purposes.

### *Question 3: What key pre-immigration steps should an individual take?*

UK

The following should be considered for the UK:

- timing of arrival in the UK (taking into account that the UK tax year runs from 6 April to 5 April of the following calendar year);
- segregation of clean capital with a view to taxation as a resident but not domiciled individual: clean capital is not taxed on remittance and includes pre-remittance income, gains, gifts and inheritance; and
- eliminate pre-arrival gains typically by way of disposals to avoid exposure on accrued gains as there is no automatic rebasing of assets.

Individuals should review the possibility of creating excluded property trusts.

SWITZERLAND

- Lump-sum taxation regime for income and wealth taxation: Non-Swiss citizens who newly relocate to Switzerland without a professional activity may, in most cantons, without a time-limitation, claim taxation on a lump-sum amount instead of worldwide income and wealth taxation. The lump-sum amount is negotiated with the tax authorities (advance tax ruling) and determined based on the highest of the relocator's worldwide living expenses, sevenfold Swiss housing costs, and a control calculation reflecting Swiss income and wealth, as well as treaty-protected income streams, and cantonal and Federal minimum amounts.
- Individuals should review and, if necessary, obtain a tax ruling on pre-existing or newly established wealth/estate planning structures (trusts, foundations, etc). Note if the lump-sum taxation regime is applied (the lump-sum regime does not cover inheritance/gift tax aspects). Individuals should also review matrimonial property status and estate planning (Swiss forced heirship rules).
- Individuals should obtain a residence permit (more complex and usually tied to a lump-sum arrangement for non-European Union/European Free Trade Association (EFTA) citizens), organise housing and provide for sufficient health insurance coverage.

ITALY

- Italy has recently introduced a special tax regime for new residents who may elect the regime for a maximum duration of 15 years.
- Individuals transferring their tax residence to Italy and who have not been a resident of Italy for at least nine years in the preceding ten years are eligible for the special tax regime.

- The application of the special tax regime leads to the payment of an annual fixed substitutive tax of €100,000 and provides for an exemption of foreign source income from Italian income taxation, with the exception of capital gains from the sale of 'qualified' participations (more than 20 per cent) within the first five years of the regime. Furthermore, it provides for an exemption of foreign assets from Italian inheritance and donation tax, an exemption of foreign assets from real estate property tax (*imposta sul valore immobili esteri* (IVIE)) and tax on foreign financial assets (*imposta sul valore delle attività finanziarie detenute all'estero* (IVAFE)). Finally, assets held abroad do not fall within the scope of Italian reporting obligations under the special tax regime.
- Taxpayers may apply for a ruling to obtain an advance clearance on the applicability of the regime. It is generally possible to extend the regime to other family members (annual fixed substitutive tax of €25,000 per person).
- Electing taxpayers are considered Italian residents for tax treaty purposes. It is possible to exclude from the special tax regime's exemption income from specific countries.
- New relocators who are non-EU nationals require a visa permit, for example, a visa by investment, to be allowed to relocate to Italy.
- Inheritance and gift tax planning is recommended to be performed before relocating to Italy.
- It is further recommended that individuals review foreign structures and consider their reorganisation, as the Italian Revenue Agency may challenge a fictitious interposition of trusts. In addition, other structuring options, such as foreign holding companies, should be reviewed carefully in view of a relocation to Italy, *inter alia*, in light of the current developments in the determination of companies' place of effective management. Finally, Italian legislation and practice with regard to CFC rules, as well as relating to participations in companies resident in blacklisted jurisdictions, should be considered.

US

From a US perspective, it is recommended that individuals review the following aspects before becoming a US taxpayer:

- whether the HNW is the appropriate family member to become a resident;
- for couples, an adequate marital property regime (separate or community property) and existence of a pre-nuptial or post-nuptial agreement;
- identification of all assets, including a review of offshore holdings for interests in non-US corporations, non-US partnerships and non-US trusts, in order to analyse the necessity for restructuring such interests to comply with US tax law; passive foreign investment companies (PFICs) typically are not considered as advantageous when becoming a US taxpayer and further, the application of the new 'downward attribution' rules should be carefully reviewed within the context of US CFC legislation; and
- step-up basis in assets prior to becoming a US resident.
- Consider wealth planning strategies such as, gifts, 'grantor' trusts, irrevocable trusts, wills and private placement insurance.

### *Question 4: How and when does an individual lose his/her residency or domicile status and what are the potential tax consequences of doing so?*

US

US legislation and practice provide the following rules on losing residence or domicile status:

- Income tax: Green card residency status continues unless it is rescinded, or administratively or judicially determined to have been abandoned. Green card holders can terminate their status by filing certain US forms.

Green card holders who take up residence abroad also risk revocation for abandonment if they are absent from the US continuously for over one year or absent extensively (more than 50 per cent), with short visits to US.

- Tax residency generally ends on the last date of a calendar year. Special rules provide that an individual may become a non-resident on the first day during a calendar year in which an individual no longer has a green card, maintains a tax home in the US, has a closer connection to a foreign country following the last day of US presence, and has not been a US resident in the following year. It is necessary to file a statement on the abandonment of the green card.
- If an individual has become resident of a country with which the US has entered into a double taxation treaty and the individual wants to claim the tie-breaker clause, certain Internal Revenue Service (IRS) forms are required to be filed.
- US domicile for transfer tax purposes is lost when a new domicile abroad is established. In addition, for transfer tax purposes, treaty tie-breaker provisions may apply depending on the particular treaty.
- The US imposes an expatriation tax (exit taxation) on certain US citizens and green card holders who have been a lawful permanent resident for eight out of 15 years prior to expatriation; this expatriation tax can apply if a treaty tie-breaker provision can be invoked. The expatriation tax imposes detrimental US income and transfer taxation on the expatriating individual.

UK

For individuals to *lose residence*, the days spent in the UK may be reduced to fall below the statutory threshold. A person no longer a UK resident will cease to be a UK taxpayer, with the exception of income taxation on UK source income and capital gains tax (CGT) on UK residential (and possibly in the future also commercial) property.

Domicile is lost in the following scenarios:

- a person deemed domicile for inheritance tax purposes has left the UK and has been a non-resident for three full (UK) tax years ('deemed domiciled');
- domicile of choice is lost after leaving and severing ties with the UK and being a non-resident for three full (UK) tax years; and
- domicile of origin is lost by acquiring domicile of choice in new jurisdiction and after being a non-resident for three full (UK) tax years.

ITALY

Residency for tax purposes may be lost if the following conditions are met:

- an individual deletes himself/herself from the register of Italian resident population (if registered there), and, in case of Italian nationals, registers himself/herself for the greatest part of the year in the register of Italian population resident abroad (Anagrafe degli Italiani Residenti all'Estero (AIRE)); and
- the individual effectively moves, for the greatest part of the year, his/her residence or domicile to a state or territory other than a blacklisted jurisdiction.

Upon the loss of Italian residency for tax purposes, individuals are no longer subject to Italian *personal income tax* on their worldwide income, but only their Italian-sourced income. Italy does not levy an exit tax or recapture rules on leaving individuals.

SWITZERLAND

From a Swiss perspective, Swiss tax residence remains in place until a new domicile/tax residence is established and evidenced vis-à-vis the Swiss authorities in the case of them challenging such a new residence. In this context, it is recommended to make a 'clear cut', and to plan for a visible shift of centre of vital interests.

Switzerland does *not levy exit taxation* on individuals leaving Switzerland. Owners of Swiss real estate after their relocation to a new location outside of Switzerland continue to be subject to a limited tax liability in Switzerland.

As far as formalities are concerned, deregistration from Switzerland is recommended, and the individual's residence status will need to be communicated *vis-à-vis* banks and other service providers.

**Back to Taxes Committee publications**

## Our London office

International Bar Association
4th Floor, 10 St Bride Street
London, EC4A 4AD
United Kingdom

Tel: +44 (0)20 7842 0090
Fax: +44 (0)20 7842 0091