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Lump-sum taxation

Within the framework of the lump-sum taxation (or forfait taxation) regime, Switzerland offers certain individuals the opportunity to be taxed based on their annual living expenses instead of their worldwide income and wealth. The regime is open to individuals relocating for the first time to Switzerland and to former residents returning to Switzerland after an absence of 10 years or more, where those individuals neither have Swiss citizenship nor exercise a professional activity in Switzerland. In the case of married couples, both spouses must meet the requirements. The lump-sum taxation regime has not only proven to be highly attractive for newly immigrating high-net-worth individuals (HNWI), but also for entrepreneurs and investors who, for example, have stepped down from their functions and professional activities before relocating to Switzerland.

After a popular vote rejecting the abolition of the lump-sum taxation regime in 2012, Swiss federal and cantonal legislation was updated in 2016 with the aim of strengthening acceptance of the regime. To conclude this process, on July 24 2018, the Swiss Federal Tax Administration (FTA) published new Circular Letter 44 (CL) in which it summarises the legal framework pertaining to the lump-sum taxation regime and provides further guidance to the cantonal tax authorities and to taxpayers on certain practical aspects of the regime. Following this revision process, the lump-sum taxation regime stands even stronger as an attractive tax planning tool for (future) Swiss residents.

Assessment basis within the lump-sum taxation regime

Within the lump-sum taxation regime, an annual comparison of the tax amounts resulting from the following four elements is taken, and the highest serves as the tax basis for a relocating individual:

- the total amount of annual world-wide living expenses of the (future) taxpayer and his/her spouse and dependents;
- seven times the annual rental costs or deemed rental income of the taxpayer's future principal residence in Switzerland, or at least three times the taxpayer's hotel costs in Switzerland;
- a minimum taxable income of CHF400,000 ($410,000) subject to federal income tax, and a minimum taxable income and wealth subject to the respective canton's income and wealth tax; and,
- the control calculation consisting of Swiss-sourced income and assets as well as certain income streams from outside of Switzerland for which a double taxation treaty protection is sought.

Relevant practical aspects

In practice, the relevant tax basis is determined within the framework of a ruling application with the competent cantonal tax authorities. It is within this context that certain case-specific aspects with regard to a relocation candidate can be addressed and reviewed with the cantonal tax authorities. While obtaining a residence permit for EU citizens, generally, is a mere formality, Swiss legislation requires non-EU citizens to be of 'economic interest' to a canton. In practice, the framework of the ruling in view of the application of the lump-sum taxation regime serves to ensure the fulfilment of this requirement by defining the parameters for the new immigrant's future taxation in Switzerland, so that non-EU citizens, by way of an elevated minimum taxation amount, may become eligible for a residence permit.

A Swiss taxpayer applying the lump-sum taxation regime qualifies as a Swiss tax resident from a Swiss domestic perspective, for the purposes of the automatic exchange of information (AEOI) and also for a large number of double taxation agreements (DTA) into which Switzerland has entered. Only a limited number of Swiss DTAs, specifically the Swiss-US and the Swiss-German DTAs, require that all US or German-sourced income is subjected to regular income taxation in Switzerland to allow for the recognition of the Swiss resident individual as a Swiss tax resident from the respective local (US, German) tax authorities' perspective (so-called 'modified lump-sum taxation').

Important updates in the new FTA circular letter

The CL provides further details and important clarifications with regard to certain requirements of eligibility to lump-sum taxation. The following elements are considered particularly relevant in practice:

- Temporary absence from Switzerland: Taxpayers applying the lump-sum taxation regime who leave Switzerland for one tax year or more remain eligible to apply the lump-sum taxation regime after their return to Switzerland, regardless of the duration of their absence. However, in practice, it will still be important to review the permit situation throughout such absence.
- Resumption of lump-sum taxation: A taxpayer who has previously applied the lump-sum taxation regime who waives his/her right to lump-sum taxation for one taxation period (which corresponds to a calendar year) or more (thus being taxed within the ordinary taxation regime in Switzerland) may not apply the lump-sum taxation again.
- Professional activities: The CL provides that candidates for taxation under the lump-sum taxation regime may not exercise a professional main or side activity in Switzerland if this activity leads to compensation payments in Switzerland or abroad. This is typically specifically relevant, and will continue to require a case-by-case analysis, as regards board members, sportspersons, artists and scientists.
- World-wide living expenses: The CL specifies that the taxpayer's world-wide living expenses include, in particular, the individual's and the individual's spouse's and dependent (minor) children's costs for food and clothing, housing costs (including side costs), taxes and social security contributions, expenses for staff, alimony payments, schooling costs, expenses for travel and leisure activities, costs for expensive animals (for example, horses) and maintenance costs for cars, yachts, planes, and so on. Extraordinary and non-periodical expenses such as, for example, a donation of a substantial portion of wealth, generally do not count as living expenses of the taxpayer or his/her family. As such, they will not increase the tax basis for the relocator.

Developments with regard to international taxation aspects

In January 2017, Switzerland enacted its domestic legislation regarding the AEOI and, since 2017, has participated in the AEOI with an increasing number of partner states. Consequently, control calculations submitted by taxpayers will be subject to more scrutiny by Swiss tax administrations with a view to financial information received from foreign jurisdictions.

The same applies to social security contributions, specifically with regard to taxpayers who are partners of non-Swiss partnership structures or members of the boards of non-Swiss companies (in accordance with the CL). Stakes in partnerships may be classified as a (foreign) self-employment activity by Swiss social security administrations. While in some cases not directly detrimental to lump-sum taxation, this may trigger an exposure to Swiss social security contributions. Both circumstances (control calculation and social security aspects) have to be taken into consideration in the context of relocation planning for HNWI and (former) entrepreneurs and investors.

The lump-sum taxation regime – one of many attractions for individuals relocating to Switzerland

Within the framework of the recent developments, updated regulations and practices published by the FTA and cantonal tax authorities, the lump-sum taxation regime proves to remain an interesting and attractive tax-planning instrument for HNWI as well as (former) entrepreneurs and investors. Aside from the pure tax planning aspects and technical advantages of the lump-sum regime, Switzerland remains an attractive place for immigration due to a great variety of other factors, not least its excellent infrastructure, stable economy and legal framework, its central location in the heart of Europe, its high quality of life, and its internationality.

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