

Client Memorandum

October 2014

Lump-sum taxation regime in the canton of Geneva

The lump-sum taxation has been a subject of debate in Switzerland for a number of years. Two initiatives aiming at the abolition of such taxation regime have been filed in 2012, resp. 2013, at a Federal level as well as in the canton of Geneva. In Geneva, the City Council has referred the case to the tax commission in order for the latter to develop a counter-initiative. Such counter-initiative proposes to maintain the lump-sum taxation regime, but to tighten the eligibility criteria for benefitting from such a regime, and to increase the minimum allowed amount forming the tax base. The Swiss population, as well as the canton of Geneva will be called to vote on these initiatives on November 30, 2014. The purpose of the present memorandum is to present the proposed modifications to the lump-sum taxation regime on the Federal level (I), as well as on the cantonal level in the light of the contents of the initiative and counter-initiative (II); moreover, the present memorandum briefly describes the different stages of the modification (III) and finally explains the various consequences of such modification (IV).

I. Popular Federal initiative

The Federal initiative which will be presented to the people on November 30, 2014 aims to ban the lump-sum taxation regime.

Should the initiative be accepted, the Confederation will enact the implementing legislation over a period of three years, i.e. until November 30, 2017. Although the Federal Council is favourable to the lump-sum taxation regime, it is technically possible for the law to be enforced prior to the envisaged date, e.g. as from the 1st of January 2016 or 2017.

In parallel, a modification of the Federal Law on harmonisation of income tax (Loi fédérale sur l'harmonisation des impôts directs, LHID) which provides for a tightening of the conditions for granting the lump-sum taxation regime has already been adopted by the Parliament. In substance, the new law provides that the calculation of the living expenses, which allows to determine the amount of Federal income tax to be levied, should now equal seven times the housing expenses (it

was previously five times the housing expenses), but not less than CHF 400'000.

II. Proposed modifications as per the Geneva initiative and its counter-initiative

a) The initiative

The aim of the initiative is the abrogation of Art. 14 of the Cantonal Law on taxation of individuals (*Loi cantonale sur l'imposition des personnes physiques*, LIPP), which allows for the lump-sum taxation regime in the canton of Geneva.

Should the people accept the initiative during the popular vote, such abrogation would be enforced as from the 1st of January, 2015. This would entail, on one hand, that no new lump-sum taxation regime would be granted as from this date, and on the other hand, that those lump-sum regimes previously granted by the Geneva tax administration would no longer be valid (see however IV).

b) The counter-initiative

According to the counter-initiative, the lump-sum taxation

regimes which have already been granted would be maintained for a period of 5 years as from the date on which the modification enters into force.

In addition, the conditions for benefitting from the lump-sum taxation regime would be partially modified as from January 2016. In particular, the counter-initiative differs from the current system on the following points:

1. Abolition of the « mixed regime »; spouses would now be required to separately meet the conditions for benefitting from the lump-sum taxation regime (non-Swiss national and absence of gainful activity in Switzerland).
2. The minimum amount taken into account in view of determining the expenses would be the highest of the following amounts:
 - a. CHF 600'000
 - b. For heads of a family: seven times the annual rent or rental value
 - c. For other taxpayers: three times the annual pension for housing and food
3. The wealth tax is taken into account by way of an increase of 10% of the determined expenses.

III. Stages of the modification

30.11.2014: Vote by the Swiss and Geneva people, who may a.1) Accept both initiatives, a.2) Accept the cantonal initiative only b) Accept the Federal initiative only c) Reject both initiatives and accept the Geneva counter-initiative or d) Reject counter-initiative and both of the initiatives.

01.01.2015: Should the cantonal initiative be accepted, entry into force of the envisaged abrogation. Lump-sum regimes already granted by the administration would cease to be valid.

01.01.2016: Should the counter-initiative be accepted, it will enter into force. It provides for a 5-year period during which the previous regime remains valid for individuals who are already benefitting from such taxation regime.

30.11.2017: Should the Federal initiative be accepted, last deadline for the entry into force of the abrogation of the lump-sum taxation regime.

01.01.2021: End of the transitional period provided by the cantonal counter-initiative in favour of individuals who were taxed on a lump-sum basis upon the entry into force of the counter-initiative.

IV. Consequences

The exact consequences for individuals benefitting from a lump-sum taxation regime will depend on the results of the vote.

Hypothesis a.1) the cantonal and Federal initiatives are accepted

Should the Federal and cantonal laws be modified in such a way that the lump-sum taxation regime is banned, it will no longer be possible to reside in Switzerland under such taxation regime as from a date to be determined, but not later than November 30, 2017.

Hypothesis a.2) the cantonal initiative only is accepted

Should the law be modified as provided for by the cantonal initiative, it will no longer be possible to benefit from the lump-sum taxation regime in Geneva as from the 1st of January, 2015.

The individuals benefitting from such regime would then be taxed on an ordinary basis on the municipal and cantonal levels. However, the initiative does not affect the lump-sum taxation on the Federal level.

In practical terms, beneficiaries of the lump-sum regime would have to choose among the following options:

- > remain in Geneva and be subject to ordinary income and wealth tax as of the 1st of January, 2015,
- > move to another Swiss canton which allows lump-sum taxation (e.g. canton of Vaud) and apply to benefit from this regime prior to December 31, 2015. Insofar as the canton in which the taxpayer is domiciled at the end of the tax period is competent to tax for the whole period, it is likely that the Cantonal Tax Administration will

> decide that newcomers will benefit from the lump-sum taxation regime for the whole 2015 period, provided that they satisfy the subjective requirements.

> Leave Switzerland between November 2014 and the 1st of January, 2015.

Hypothesis b) the cantonal counter-initiative is accepted

The modifications envisaged in the counter-initiative essentially restate the modifications imposed by the Federal law (LHID), which provides that the cantons adapt their respective legislations by the 1st of January, 2016. Thus, the counter-initiative in fact complies with the requirements of the Federal law. The only additional tightening of the law relates to the minimum amount which will serve as the taxable basis: a minimum of CHF 600'000 of taxable basis, whereas on the Federal level, it is CHF 400'000.

Hypothesis c) the initiative and the cantonal counter-initiative are rejected by the people

No changes to the regime on the cantonal level.

Conclusion

For the time being, it is impossible to evaluate the people's response to the initiative, whether such response results in the abrogation of the lump-sum taxation regime, a tightening of such regime, or a status quo.

This being said, the Geneva State Council has largely rejected the abrogation of the lump-sum taxation regime, and has declared itself favourable to the development of a counter-initiative. Hence, while the abrogation of the regime is not the option recommended by a majority of parties and by the government, the counter-initiative seems to gather more supporters – especially since it would allow the canton of Geneva to be in line with the modifications already envisaged by the Federal law.

Please do not hesitate to contact us in case of any questions.

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