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NEWSLETTER

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Adjustments to tax at source – the view of artax

Dear Ladies and Gentlemen

Switzerland is one of the few countries that basically do not deduct taxes directly from employees' wages. Rather, it trusts its citizens and leaves it up to them to self-declare their income and to pay the ensuing taxes. Strictly speaking, however, this applies only to Swiss citizens and foreign nationals with a category C residency permit. All other foreign nationals, on the other hand, are taxed at source.

Some of the regulations for tax at source are several decades old and, in contrast to ordinary taxation, have never been harmonised throughout Switzerland. This means that in many cantons, people with an income of over CHF 120'000 therefore have to submit a tax return to which tax at source will then be credited, whereas in the cantons of Aargau and Solothurn, for example, buying property means an immediate end to tax at source, and ordinary tax assessment comes into effect. The canton of Geneva has an upper limit of CHF 500'000 as income for tax at source. Many cantons obstinately tax at source on a monthly basis, whereas others, particularly in the west of Switzerland, calculate each month back to the whole year, thus taking fluctuations in income (e.g. 13th month salary, overtime compensation or bonus) into account.

During the last few years, artax has increasingly specialised on the taxation of natural persons with an international background, and thus has gained considerable expertise in this field. As a consequence, this has allowed us – either mandated by large international corporations or directly by clients – to deal with the taxation of around 800 people taxed at source.

Whilst doing so, we have increasingly noticed that the system of taxing at source is no longer up to current requirements. What was more than adequate a few decades ago, for only a small number of mainly low-skilled seasonal workers, is now more or less insufficient for what is now a large number of highly qualified and often very mobile workforce and top managers. Additionally, in large cities (by Swiss standards) like Basel around a quarter of all taxpayers are now taxed at source.

One of the large problems is how to deal with those taxed at source who move from one canton to another during a calendar year. Under ordinary tax law, taxes are due where a taxpayer is resident at the end of the year – however, this does not apply for those who are taxed at source even if they have to subsequently hand in a tax return. Instead, the taxation period is split up, with each canton claiming tax for a part of the year. If identical splitting regulations were applied in all cantons, it would only lead to an increased administrative effort, but at least the end result could be deemed correct.

In reality, however, 25 cantons have simply split the annual income proportionally, according to the number of days, whereas Basel-Stadt has taken the actual day of payment of wages, additional income and deductions as basis. In the case of a move from Basel-Stadt to Basel-Land, for example, this can lead, in breach of constitutional rights, to a double taxation of the same income. We also have occasionally experienced cases in which taxes of CHF 10'000 in excess of those actually due have been illegally levied. As both cantons involved refused a pragmatic solution and rejected appeals according to their own legal systems, one such case actually went as far as the Federal Supreme Court. Last year it delivered its judgement and, as expected, eliminated this double taxation. However, not only did the Federal Supreme Court order that the administratively inefficient and rather complex system of Basel-Stadt be applied, it also made this system binding for all other cantons. At the same time the verdict left so many questions of detail open to interpretation (e.g. does only the income taxed at source have to be split up according to day of payment, or does this also apply for payments into social security pillar 3a and to property maintenance, etc.) that inconsistencies and double taxations are bound to happen again sooner or later. And absurd situations remain when taxpayers are moving during a calendar year and at a later stage receive the residency permit C, which means that they also move from a system of split taxation to that of full taxation at their place of residence at the end of the year. Then the change of the canton responsible to levy taxes does not happen on the day of the move, but rather on the day the taxpayer received the C-permit.

The taxation of international weekly commuters is a complete shambles. International commuters are married persons who, due to their work, move to Switzerland while the partner and, if that be the case, their children, remain abroad. Depending on distances to their home country these people see their families on weekends only, or even less. According to international tax regulations Switzerland is allowed to raise taxes only on income generated through work, anything else is taxed by their home country.

Now, for correct taxation the worldwide income and wealth would determine the tax rates, and only the tax factors allocated to Switzerland would then be taxed here at that rate. As this is rather complicated many cantons have come up with a pragmatic solution. To simplify matters these people are considered sole earners in these cantons and are taxed at source there according to their actual number of children, while occasionally additional requirements are to be applied for this solution. For example the canton of Zurich only applies the sole earner tax rates if the international commuter's spouse earns a maximum of CHF 25'000 per year. In many cantons it is also possible to file a simplified tax return (rate adjustment) and claim deductions for weekly commuter costs and allowances for pillar 3a and voluntary pension plan contributions. Until a few years ago Basel-Stadt completely refused to accept these deductions, but was then forced by the Federal Supreme Court to admit such a rate adjustment at least in certain cases.

Now the administration has come up with a creative solution to still be able to refuse those tax deductions to as many people as possible. First the option of such a rate adjustment was restricted to EU citizens whose families live in the EU, as the judgement by Federal Supreme Court only found a breach of the Agreement with the EU on the Free Movement of Persons. And handing in a complete tax declaration is still not an option open to international commuters. Next the terms "quasi-resident" and "assumption of perception" were created, plus a completely arbitrary, but nevertheless formally legitimated, obstacle was erected: Only the "quasi-resident" marriage partner that is earning at least 90% of the family's income can claim tax deductions. Not only is this extremely difficult to prove with foreign tax assessments (as married couples are taxed separately in many countries), but even a small income by the spouse often means that the main earner cannot comply with the 90% threshold anymore, thus making any claims for deductions on Swiss taxes impossible. Very often the only solution is for us to recommend our clients to move to the canton of Basel-Land as this canton does not impose this obstacle and allows rate adjustments for all international weekly commuters. One might be allowed to ask whether Basel-Stadt can really call this a location policy it can write home about.

Originally the actual number of children served as basis for the tariff to tax at source, and it their existence could be shown by whatever evidence was available. Some time ago both Basel cantons considerably tightened regulations in this respect, and since then, tax at source is wilfully tied to child allowance paid in Switzerland. Rather inconveniently, any employment by the spouse or partner in their home country – where the children live as well – most often leads to child allowance being paid there. As a consequence, our international weekly commuter will now be taxed as if he had no children at all.

Early in 2014, in order to "streamline the administrative process and to allow for the option of electronic filing", new tariffs for tax at source were introduced throughout the whole of Switzerland – which, quite incidentally, now means that the tariffs for tax at source for double-income families need to be applied for international weekly commuters as well. As a consequence, this leads, in some cases, to tax rises of over 60% (as we reported in one of our previous newsletters).

Meanwhile a silver lining has appeared on the horizon: The Federal Government has recognised the many complex problems with tax at source, and recently proposed new legislation to harmonise and optimise tax at source. It proposes that the income threshold be lowered for compulsory and subsequent submission of the tax declaration, yet allows persons with an income below this threshold, on a voluntary basis, still to hand in their tax declaration. Additionally, persons taxed at source are now to be taxed for the whole year at their place of residence at the end of the year, which would mean that all the problems with split taxation periods including increased administrative efforts and the risks of double taxation, as described above, would then cease to exist. artax welcomes these proposals and regards them as a considerable and welcome improvement to the current situation.

Unfortunately, the proposals also include keeping the status of "quasi-residents", and it would also both cement the unfortunate 90% threshold and make it applicable throughout Switzerland, which in currently generous cantons like BL would lead to a worsening of the position for those affected. We strongly believe that this threshold should be abolished or at least drastically lowered, or alternatively another model for the taxation of international weekly commuters needs to be developed.

As is usually the case the draft proposals are undergoing the statutory consultation process, and all parties interested have until 27 March 2014 to raise objections and add their views. As we believe that our job is do more than just delivering the best possible consultations according to existing laws, we also actively campaign for the reform of the legal framework – that is why artax has summarised its views and delivered its opinion to the Federal government. All documents pertaining to the consultation process and our address to the Federal government (in German) are available here:

- [legislative proposal](#)
- [report to the legislative proposal](#)
- [our address to the Federal government](#)

We do hope that our extensive experience with tax at source will be taken into account during the legislative process, and that we can contribute to help optimise this draft legislation, which at least seems to be going into the right direction. Either way, we are trying to stay on the ball and to keep you up to date with this newsletter.

Best regards,
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