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HIGHLIGHTS

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France Takes Aim at Expats in Switzerland

by Jérôme Delaurière

As of January 1, Swiss residents taxed on a lump sum basis (the *forfait* regime) will no longer benefit from the provisions of the France-Switzerland income tax treaty.

A number of foreign residents living in Switzerland benefit from an advantageous tax regime called *régime du forfait*, an attractive alternative to taxation based on the real income of the taxpayer.

This tax regime applies to taxpayers of foreign nationality who take up residence in Switzerland for the first time but do not carry on business in Switzerland. The taxpayers' income is determined on a lump sum basis calculated on annual costs relative to their lifestyle during the taxation period.

Despite a provision in the France-Switzerland tax treaty excluding individuals taxed under the *forfait* regime in Switzerland, the French tax authorities have agreed since 1972 that such taxpayers could benefit from the treaty provisions subject to the following conditions:

- their taxable basis for federal, cantonal, and communal tax is five times greater than the rental value of the dwelling of the taxpayer or 1.5 times the price of pension costs; and
- the cantonal and communal taxable basis does not deviate considerably from that which is used for the federal taxable basis.

On December 26, however, the French tax authorities updated the provisions of their tax doctrine,[1] adding the following subsection:

> The 1972 tolerance under the tax doctrine DB 14 B-2211 7, updated December 10, 1972, has not been taken up by the tax database-BOFIP reported as of September 12, 2012 and is therefore cancelled as of such date, in accordance with the instruction 13 A-2-12 of September 7, 2012. However, it is recognized that this tolerance will continue to apply to 2012 revenues inclusive.

Thus, as of January 1, French expats subject to the Swiss *forfait* regime will no longer be protected by the provisions of the France-Switzerland tax treaty because the French tax authorities have unilaterally and without notice ended the tolerance that has prevailed for the past 40 years.

Main Consequences

In practice, only the criteria provided by French tax law (article 4B of the French Tax Code) will now apply to determine the tax residence of a French person domiciled in Switzerland who has personal, economic, or professional interests in France, if that person enjoys the *forfait* regime in Switzerland. The residence tiebreaker rules under article 4 of the France-Switzerland tax treaty will no longer apply to a dual residence scenario. This will result in a significantly increased risk for French persons living in Switzerland who are taxed under the *forfait* regime to also be considered tax residents in France if they have retained significant economic or personal interests in France.

Another adverse consequence resulting from this situation is that Swiss tax residents who, directly or indirectly, have homes in France (for example, second homes) may become subject to income tax in France at up to three times the annual rental value of the residence (article 164C of the French Tax Code).

Moreover, persons subject to the *forfait* regime who receive dividends from a French source or capital gains on the sale of substantial shareholdings (greater than 25 percent) will no longer be eligible for reductions or exemptions of withholding tax as provided by the treaty.

It will therefore be more difficult for residents of foreign nationality (including, but not limited to, those of French nationality) residing in Switzerland and subject to the *forfait* regime to continue to benefit from the lump sum scheme while maintaining personal or proprietary interests in France. ◆

♦ *Jerome Delaurière is a lawyer with Gibson Dunn in Paris.*
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[1]Bofip — BOI-INT-CVB-CHE-10-10-20121226.