

# UK/SWISS TAX AGREEMENT - KEY POINTS SUMMARY



The Swiss Government has come under increasing international pressure as a result of its bank secrecy laws and recent years have seen some significant developments in its thinking (such as agreeing to allow Exchange of Information provisions to be incorporated into its treaties). Most recently negotiations have taken place with the German and UK Governments with a view to addressing the problem of non-tax compliant funds held by Swiss banks.

The negotiations with Germany concluded on 10 August 2011 with the announcement of an agreement. The UK agreement was ratified in principle on 24 August 2011. There appear to be some fundamental similarities between these, with both addressing historic non-compliance and the position going forward. The differences between the tax systems of Germany and the UK mean, however, that the agreements differ in significant details. Most notably, the withholding tax rates in the UK agreement are higher.

The UK/Swiss agreement is being hailed by both sides, with the HM Treasury press release referring to “an historic agreement with Switzerland” that will secure billions in unpaid tax, and the Swiss Finance Minister stating that the agreement will show Switzerland “is serious about implementing its white money strategy.”

The two Governments anticipate signing the agreement within the next few weeks. The complete text of the agreement will be published after it has been signed. Until that time there is uncertainty with respect to the detail.

It is clear, however, that all UK domiciled residents with funds in Swiss accounts will need to consider their position before the agreement comes into force (see the special section below for the position for UK resident foreign domiciliaries). If nothing is done by the deadline date (see below) the Swiss banks will assume that the funds are non-compliant. This means that they will deduct from the account and pay over to HMRC:

- a significant one-off lump sum tax payment with respect to historic non-compliance; and
- on an on-going basis, withholding tax on future income and capital gains.

Current information indicates that UK domiciled residents will have five months from the date that the agreement comes into force (expected to be early in 2013 but there could be slippage if the ratification procedures take longer than envisaged) to make a decision as to whether to suffer the fixed tax deductions or authorise on-going disclosure of income and gains information to HMRC.

As a show of good faith the Swiss banks have agreed to pay an initial CHF500 million when the agreement enters into force. This will be recouped by the Swiss banks from the tax deducted from account holders.

## 1. FOREIGN DOMICILIARIES

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The official material released to date does not make clear how the agreement will impact on foreign domiciliaries. The HM Treasury press release is silent on the subject. The Swiss Federal Department Release, however, states that “the agreement contains special rules for non-UK domiciled individuals”.

The Swiss Banking Association has published material on the agreement which includes “Questions and Answers” and in these it states that: “In principle, the agreement is not applicable to so called “non-UK domiciled individuals”. No further information is given and it is not clear:

- that the statement is authorised by the Swiss Government; or
- whether it should be taken as meaning the agreement will not apply to a foreign domiciliary regardless of whether he or she is a remittance basis user for the tax year.

The position with respect to the one-off levy will need to be considered separately (with, possibly, the requirement for historic certification of remittance basis usage). It is not clear what will be the position where the individual was a remittance basis user up until 5 April 2008 and has been an arising basis user since then. It is possible that, in such cases, the individual will have to opt for disclosure of information since 6 April 2008 in order to avoid the levy.

As to the way in which the ongoing withholding tax deduction will be applied, there may be some guidance in the way in which Swiss banks currently apply the EU Savings Directive. Whilst not determinative, it is instructive to note that Switzerland only exempts those UK resident foreign domiciliaries who are taxed on the remittance basis from these provisions (in these circumstances there is neither a deduction of withholding tax nor reporting to the UK authorities).

Whatever specific provisions the agreement contains, it seems clear that there will need to be a comprehensive process for identifying foreign domiciliaries which, if only remittance basis users are to be exempt, may have to be renewed annually. We presume that this will extend (and possibly formalise) the current measures with respect to certification which are used by the Swiss banks for the purposes of the EU Savings Directive.

## 2. REGULARISATION OF UNTAXED ASSETS IN SWITZERLAND

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As explained above, the default position is that, where the Swiss account was open at 31 December 2010 and remains open on 31 May 2013, a one-off levy will be deducted where the holder is UK domiciled and resident. The HM Treasury press release states that the deduction will be taken to settle UK Income Tax, Capital Gains Tax, Inheritance Tax and VAT liabilities in relation to the funds in the account. It is not, however, entirely clear from the information so far released whether the payment:

- only covers investment income and gains resulting from the funds managed by the Swiss banks; or
- regularises the position with respect to ALL non-compliant funds regardless of when they were deposited in the account and from what source they came.

It is specified that the one off levy will not absolve assets originating from criminal sources, or where a tax enquiry has been opened, or in cases where the taxpayer has previously participated in a disclosure facility. In such cases the levy will merely be seen as a payment on account.

The basis for the one off levy is to be the capital held in Swiss accounts or deposits on a specific reference date in the past. However, we are also told that the tax rate and basis for assessment will take account of the length of time that assets have been held untaxed in Switzerland. The maximum applicable tax rate will be 34% (with 19% the lowest) and will be based on the duration of the client relationship as well as the initial and final amount of capital. It has been suggested that, for a typical client, the methodology will result in an effective tax rate of between 20% and 25% of total assets.

The one off levy can be avoided by affected UK domiciled residents authorising disclosure of their accounts to HMRC (the position for UK resident foreign domiciliaries is considered above). Compliant taxpayers will obviously want to do this. Non-compliant taxpayers may also prefer this option and pre-empt disclosure by the Swiss authorities by a voluntary disclosure to HMRC. It might be possible to do this through the Liechtenstein Disclosure Facility (a very different initiative which allows taxpayers to regularise the totality of their tax affairs generally on advantageous terms). Where this is not an option and the taxpayer makes an ordinary voluntary

disclosure with respect to his (or her) Swiss accounts it is stated that a voluntary disclosure pursuant to the agreement will not result in prosecution. However, the HM Treasury press release notes make it clear that there will be both interest and penalties (there is no mention of reduced penalties for such disclosures). We will need to see the actual agreement to ascertain the full picture.

Whilst non-compliant taxpayers can transfer funds from Switzerland without paying the one off levy or making a voluntary disclosure, that would seem most unwise. Tax evasion is a crime and it is clear that the Government expects HMRC to come down very heavily on individuals who persist in illegal behaviour.

With the proliferation of tax information exchange agreements, it is likely that over the next few years many (if not all) of the major private banking centres will have agreed to exchanges of information with HMRC. In addition the agreement seeks to mitigate the risk of non-compliant funds being removed from Switzerland to escape the levy by providing that:

- the Swiss authorities have to notify HMRC of the destination of assets belonging to UK residents which are moved from Switzerland (with the likelihood that any jurisdiction to which funds are moved will come under pressure to exchange information if it has not already agreed to do so); and
- HMRC can ask for details with respect to specific individuals if they have reasonable grounds to believe that they have Swiss funds and are non-compliant (see the section below on the further exchange of information provisions ).

### 3. WITHHOLDING TAX FOR THE FUTURE

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The default position will be that, from the date that the agreement comes into force, investment income and capital gains of UK residents with accounts in Switzerland will be subject to a new withholding tax. The rates have been set at 48% on interest income, 40% on dividend income and 27% on capital gains, the small reduction from the highest UK tax rates being justified by the fact that, since the tax is being deducted at source, it is being paid over earlier. The HM Treasury press release states that the deduction of this withholding tax will satisfy UK tax liabilities on the income and gains.

Where tax is withheld as a result of the EU Savings Directive, there should not be double withholding tax. It is understood that tax deducted under the EU Savings Directive provisions will be offset against the withholding tax deducted under this agreement.

A UK resident does not have to suffer the Swiss withholding tax. He or she can opt for the Swiss Federal Tax Administration to provide HMRC with details of their Swiss income and gains.

## 4. FURTHER EXCHANGE OF INFORMATION PROVISIONS

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As part of the agreement the Swiss authorities have agreed to new information sharing commitments. Where HMRC has a plausible reason for thinking a UK resident has not reported all taxable Swiss income and gains it can ask the Swiss authorities to confirm whether the individual has a Swiss account. In principle the Swiss tax authority has to respond to the request by providing details of how many accounts or deposits the individual has with Swiss banks. From the details provided in the Swiss Federal Department of Finance's release, it is apparent that "so-called fishing expeditions" will not be permissible. The agreement will initially limit the number of requests that the British authorities are permitted to make to 500 each year but this maximum may be adjusted for future years, depending upon the results achieved.

## 5. SUNDRY

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In addition to the points summarised above:

- Mutual market access for financial services will be improved.
- The UK has said that it does not envisage further purchases of stolen Swiss bank data.
- The UK has said that criminal prosecution of bank employees as a result of participation in tax offences is unlikely.

## 6. RATIFICATION

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The HM Treasury press release talks of signature in the coming months. The Swiss Government's explanatory material states that the agreement should be signed by both governments in the next few weeks. Once the agreement has been signed the complete text should be published. It will then need to be authorised by the legislative organs of both jurisdictions.

In the UK the agreement will be authorised through the standard parliamentary process. There will be no referendum in the UK. In Switzerland it is not mandatory that a referendum be held to approve the agreement, but it is possible that there will be one, as a referendum on international agreements is required if the requisite number of people and/or Cantons request it. As noted above, the current understanding is that the process in both jurisdictions should be completed so that the agreement can be implemented from 1st January 2013.

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