

Swiss Federal Supreme Court holds, owning permanent residence in a state does not necessitate tax-residency

Mr. A [TS-758-FC-2020(SWTZ)]

Brief Facts

The taxpayer, Mr A, was a United States ('US') citizen residing in the United Kingdom ('UK'). The taxpayer received dividends from Swiss companies during the years 2008, 2009, 2010 and 2012 after tax withholding at the rate of 35% under Swiss domestic laws. As per Article 10(2)(b) of the tax treaty between the United States of America and the Swiss Confederation ('tax treaty'), dividend income was taxable at a lower rate of 15%, and the taxpayer claimed a refund for the excess tax withheld. On January 13, 2011, the taxpayer made an application (with the UK address) to the Swiss tax authorities in Form 82 I to refund excess tax of 20% for 2008 and 2009. The tax authorities processed the said application and granted the refund on June 20, 2011.

On August 12, 2012, the taxpayer filed another application (with the UK address) with the Swiss tax authorities in Form 82 I to refund excess tax of 20% for the year 2010. The tax authorities returned the application form on November 15, 2012, and asked the taxpayer to make a claim under the tax treaty between UK and Swiss Confederation. The tax authorities also sought additional information, such as mentioning all details in Form 82 I and the taxpayer's status in the UK. On January 16, 2013, the taxpayer reverted that he has a non-domiciled status in the UK and was required to pay tax only on the income remitted in the UK. Accordingly, the taxpayer was not entitled to invoke the tax treaty between the UK and the Swiss Confederation. The taxpayer further mentioned that he is a US citizen and is liable to pay tax in the US on his worldwide income. On May 3, 2013, the tax authorities asked the taxpayer to submit proof regarding how he satisfied the criteria of being a US tax resident, as mentioned in Article 4(1)(a) of the tax treaty. The taxpayer reverted that he has a permanent home in the US since 1987, and accordingly, he is a resident of the US as per tax treaty. On November 28, 2014, the tax authorities opined that the taxpayer did not satisfy the criteria given in Article 4(1)(a) of the tax treaty and thus not entitled to invoke the tax treaty. The tax authorities further asked the taxpayer to pay back the amount of tax refund received for the years 2008 and 2009 along with 5% interest.

On June 4, 2015, the taxpayer filed a further application (with the US address) with the Swiss tax authorities in Form 82 I to refund excess tax of 20% for the year 2012. The said application also contained a footnote emphasising that the taxpayer erred earlier in not mentioning that he is also a UK tax resident. On February 5, 2016, the tax authorities rejected the said refund application on the same reasoning.

The taxpayer filed an appeal before the Federal Administrative Court against the decision of the tax authorities. The Federal Administrative Court observed that the criteria mentioned in Article 4(1)(a) could not be interpreted literally to mean that the conditions (i.e. substantial presence, permanent home or habitual abode) mentioned therein are independent alternative conditions due to presence of the word 'or' but needs to be interpreted in a sense that shows there is a strong nexus with the US. In this background, the Federal Administrative Court held that the taxpayer was neither present in the US for sufficient days nor had a habitual abode in the US. Thus, the criteria of the *substantial presence or habitual abode* mentioned in Article 4(1)(a) of the tax treaty doesn't get satisfied. The Administrative Court further held that since the taxpayer did not have a strong nexus with the US, he cannot be said to have a permanent home in the US. Accordingly, the Federal Administrative Court dismissed the taxpayer's appeal.

and held that the taxpayer is not a US tax resident entitled to invoke the lower rate on dividends mentioned in Article 10(2)(b) of the tax treaty.

Against the dismissal of appeal by the Federal Administrative Court, the taxpayer appealed before the Federal Supreme Court.

Issue Before the Court

Before the Federal Supreme Court, the issue was whether the taxpayer was a resident of the US and thus eligible to invoke the tax treaty.

Decision of the Court

The Federal Supreme Court of Switzerland noted that the taxpayer did not meet the substantial presence or habitual abode criteria required to trigger tax residency in the US. The Federal Supreme Court agreed with the Federal Administrative Court's conclusion that in the absence of strong nexus with the US, the mere possession of a home in the US would not satisfy the *permanent home* criteria. The Federal Supreme Court noted that the factual circumstances, like the taxpayer being an active trader in the UK and possessing home in the UK reveal that the taxpayer has stronger ties with the UK than the US.

In light of the above, the Federal Supreme Court held that the taxpayer cannot be treated as a tax resident of the US and cannot invoke the lower tax rate on dividends as per Article 10(2)(b) of the tax treaty. Accordingly, the Federal Supreme Court dismissed the appeal and directed the taxpayer to pay back the withholding tax refund received for 2008 and 2009 along with interest.

Taxsutra Note:

Convention between the United States of America and the Swiss Confederation

Article 4 – Resident

1. For the purposes of this Convention, the term “resident of a Contracting State” means:
 - a. any person who, under the laws of that State, is liable to tax therein by reason of his domicile, residence, nationality, place of management, place of incorporation, or any other criterion of a similar nature, except that a United States citizen or alien lawfully admitted for permanent residence (a “green card” holder) who is not a resident of Switzerland by virtue of this paragraph or paragraph 5 shall be considered to be a resident of the United States **only if such person has a substantial presence, permanent home or habitual abode in the United States**; if, however, such person is also a resident of Switzerland under this paragraph, such person also will be treated as a United States resident under this paragraph and such person's status shall be determined under paragraph 3;
3. Where by reason of the provisions of paragraph 1 an individual is a resident of both Contracting States, then his status shall be determined as follows:
 - a. he shall be deemed to be a resident of the State in which he has a permanent home available to him; if he has a permanent home available to him in both States, he shall be deemed to be a resident of the State with which his personal and economic relations are closer (center of vital interests);

- b. if the State in which he has his center of vital interests cannot be determined, or if he has no permanent home available to him in either State, he shall be deemed to be a resident of the State in which he has an habitual abode;
- c. if he has an habitual abode in both States or in neither of them, he shall be deemed to be a resident of the State of which he is a national;
- d. if he is a national of both States or of neither of them, the competent authorities of the Contracting States shall settle the question by mutual agreement.

Article 10 – Dividends

1. Dividends derived and beneficially owned by a resident of a Contracting State may be taxed in that State.
2. However, such dividends may also be taxed in the Contracting State in which the dividends arise according to the laws of that State, but if the beneficial owner of the dividends is a resident of the other Contracting State, the tax so charged shall not exceed
 - a. 5 percent of the gross amount of the dividends if the beneficial owner is a company which holds directly at least 10 percent of the voting stock of the company paying the dividends;
 - b. 15 percent of the gross amount of the dividends in all other cases

Subparagraph b) and not subparagraph a) shall apply in the case of dividends paid by a person which is a resident of the United States and which is a Regulated Investment Company. Subparagraph a) shall not apply to dividends paid by a person which is a resident of the United States and which is a Real Estate Investment Trust, and subparagraph b) shall only apply if the dividend is beneficially owned by an individual holding an interest of less than 10 percent in the Real Estate Investment Trust. This paragraph shall not affect the taxation of the company in respect of the profits out of which the dividends are paid.