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NEWSLETTER

12.04.2016 **Fabian Jeker**
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OPA – saving taxes by withdrawing capital

Dear Sir or Madam,

Anyone in Switzerland who wishes to retire can withdraw the available retirement savings capital of the 2nd pillar as either a pension or as a lump sum. Pension asset investments withdrawn as a lump sum are subject to a separate taxation treatment. Direct federal taxation of lump sum withdrawals attracts a fifth of the regular income tax rate (the so-called "pension rate"). Due to their tax sovereignty, cantons raise their own tax rates, and this offers major opportunities to save as a result of the tax competition. To exploit tax advantages sustainably and in the best possible way, precise pension and financial planning is required.

Tax optimisation
Pension vs. lump sum withdrawal
A lump sum withdrawal of retirement assets is only possible once, upon reaching ordinary retirement age (for exceptions, see paragraph about partial retirement). In this situation you must individually weigh the pros and cons of a lump sum withdrawal and, if necessary, opt for a mixed solution. The Occupational Pension Act (OPA) allows anyone entitled to pension to withdraw at least 25% of their retirement assets as a lump sum. Beyond that, pension funds are allowed to introduce different regulations. Here it is necessary to note the various time limits which pension funds have set when it comes to announcing lump sum withdrawals. A partial withdrawal of retirement assets, in the form of a one-off lump sum, offers significant tax advantages; the withdrawn capital is freely available, although it becomes subject to wealth tax.

Place of residence
Generally, capital payments are subject to tax in the borough and the respective canton where entitled persons are domiciled at the time of the withdrawal. Thus the potential for tax optimisation is, among other things, dependent on the various tax rates differing from canton to canton. It is impossible to name a canton with the lowest tax rates as some of these vary immensely depending on the amount being paid out. By timely and early planning of capital payment, in combination with flexibility when it comes to domicile, enormous tax reliefs are possible.

Single					Married, 2 children				
	BS	SZ	ZG	VD		BS	SZ	ZG	VD
	Basel	Wollerau	Zug	Lausanne		Basel	Wollerau	Zug	Lausanne
100'000	5'325	1'810	3'517	7'473	100'000	5'144	1'160	2'123	5'967
250'000	20'782	11'109	12'914	26'827	250'000	20'562	7'708	12'511	23'103
500'000	47'382	32'319	30'874	63'490	500'000	47'062	24'980	30'768	57'196
1'000'000	99'750	78'500	65'962	136'179	1'000'000	99'750	67'479	66'175	130'207

When comparing cantons and boroughs, the various tax amounts can differ massively from one another, often by a multiple of the tax amount that one canton or borough would levy. The tax rates can equally vary depending on the amount of capital withdrawn. As a result, some councils have low taxation with low capital payment, other councils have favourable taxes with high capital payment.

Anticipated life expectancy
In 2014, the remaining life expectancy (after retirement) of men aged 65 at the time was 19.4 years, and that of women 22.4 years. The individual life expectancy actually matters when it comes to choosing the option of withdrawing retirement savings. Generally, drawing a pension is quite an attractive option with a larger-than-average life expectancy. The most significant influencing factor is the minimum conversion rate for the compulsory section according to OPA, currently at 6.80%. The conversion rate represents the annual pension paid out as percentage of the accrued retirement capital. Without considering other factors like taxes and possible interest earnings, it is worth drawing a pension on the compulsory part with a conversion rate of 6.80% if your remaining life expectancy is above 15 years. In this situation the rent paid out would be higher than the accrued OPA capital. Should the life expectancy be below 15 years a lump-sum withdrawal would be the preferable option. On top of that, previously withdrawn capital becomes part of the estate and, in the event of death, will be inherited by relatives. 2nd pillar assets not withdrawn at that moment are not part of the estate; however, under certain circumstances, a widow's or widower's pension will be paid out.

Development of interest rates
The legal minimum rates for interest on the compulsory retirement savings capital have steadily gone down since the introduction of the OPA. According to the OPA the level of the legal minimum rate is set by taking into consideration the development of government bonds and the expected return on the capital and property market. It is safe to conclude that currently high returns on investments are statistically unlikely and difficult to realise.

Parallel to the development of the interest rates of OPA retirement capital, the interest rates on bank deposits are at a record low. With adequate economic knowhow there is the option of making an early lump-sum withdrawal of retirement savings in order to invest this privately on the capital market and realise returns that are above the OPA minimum rate of 1.25%. As private capital gains are tax free in Switzerland, parallel to all gains on OPA retirement capital, there are no disadvantages in relation to the taxation of gains on this capital.

Partial retirement
When opting for a partial retirement, the retirement capital can be withdrawn in tranches as capital. With regard to the number of permitted payouts, and regulatory requirements, differences exist from canton to canton – all of which must be considered in advance. Generally, workload needs to be reduced step-by-step to enable withdrawal

of capital in tranches. By splitting these capital withdrawals, the progressive taxation can be interrupted – thus the whole tax burden can be reduced. Partial retirement also has advantages from the point of view of wealth tax as by making phased withdrawals only small tranches of capital tailored to the actual capital requirement are paid out so that at the year's end only small assets subject to tax remain unused. Precise and sustainable financial planning is required to ensure the ability to pay during retirement. In any case registration periods for capital withdrawals, varying from canton to canton but usually three years, have to be complied with (as long as no differing regulation regarding registration period is set down in the pension fund guidelines).

Prognosis
With the lowering of the legal minimum rate and the possible reduction of the conversion rate, withdrawing retirement capital as a lump sum becomes increasingly attractive compared to drawing a monthly pension. The Federal Council has decided to lower the legal minimum interest on the compulsory part of pension fund assets from 1.75% to 1.25% as of 1 January 2016. For comparison: Since passing the OPA in 1985 and up to and including 2002, the legal minimum interest had been set at 4%. This means that the minimum interest rate has now reached an historic low in 2016. Following the development of the legal minimum interest, it can also be expected that the percentage of lump-sum withdrawals will increase.

Kind regards
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