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Introduction to Swiss Tax Law

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Fiscal Sovereignty: 3 Levels of Taxation

- ~ Confederation:
Authority in all areas in which it is empowered by the Federal Constitution → the Confederation must only levy taxes to which it is authorised by the Federal Constitution
- ~ Cantons (26 Cantons):
Authority in all areas that are not reserved to the Confederation → the cantons are authorised to levy any type of tax as long as they do not infringe upon the exclusive authority of the Confederation or upon the Federal Constitution and Federal Law
- ~ Municipalities (approx. 2600 Municipalities)
Authority in all areas that are entrusted to them by the Canton → the municipalities must only levy taxes within the bounds of the authority delegated to them by the respective cantonal law



Principal Taxes on the Federal Level

Taxes on income

- " Income tax (individuals)
- " Tax on net profit (legal entities)
- " Withholding tax on certain items of income of certain taxpayers (e.g. salary income of short term residents without Swiss citizenship and of non-residents)
- " Withholding (Anticipatory) tax on certain income on movable capital assets

Taxes on goods and services

- " Value Added Tax
- " Stamp duties
- " Tobacco tax
- " Beer tax and tax on distilled spirits
- " Mineral oil tax
- " Motor vehicle tax
- " Customs duties



Principal Taxes on the Cantonal or/and Municipal Level

Taxes on income and on net wealth

- All cantons
- " Income and net wealth tax (individuals)
 - " Tax on net profit and on capital (legal entities)
 - " Real estate capital gains tax
 - " Withholding tax on certain items of income for certain taxpayers

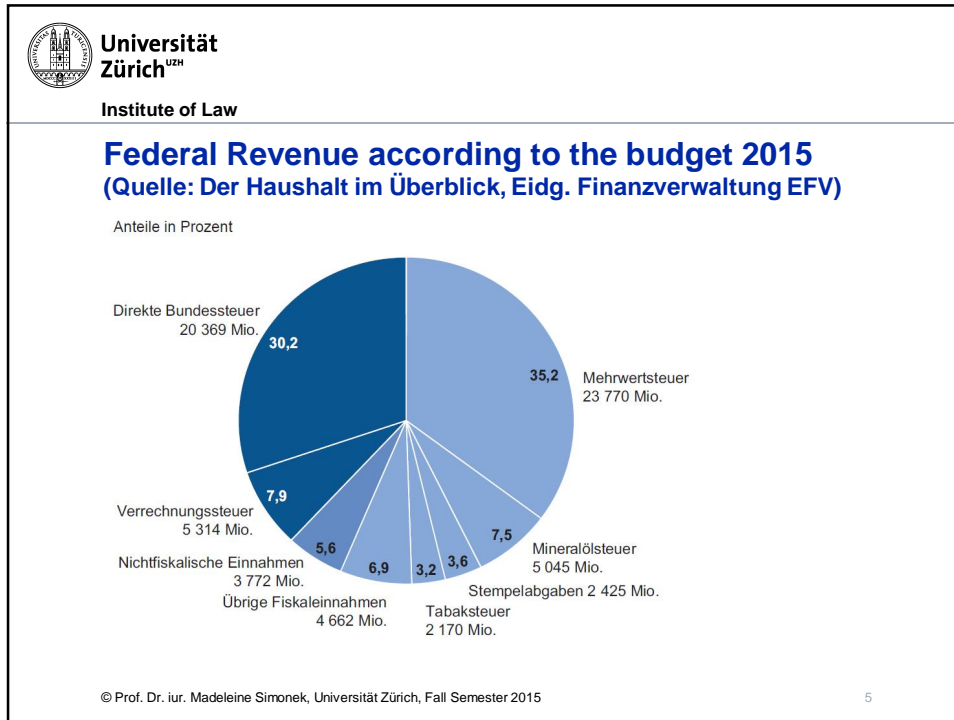
Not all cantons

- " Inheritance and gift tax
- " Lottery income tax
- " Real estate tax

Taxes on goods and services

Not all cantons

- " Taxes on transfer of immovable property
- " Motor vehicle tax
- " Stamp duties
- " Dog tax
- " Entertainment tax
- " Visitor's tax



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- ### Principal International Agreements
- ~ **Double Taxation Treaties**
Wide net of double taxation treaties concluded by Switzerland (as per 1 January 2015 approx. 95 treaties on income taxes, a few also on net wealth taxes)
 - ~ **Bilateral Agreements with the European Union, from a tax perspective in particular of relevance**
 - Agreement on free movement of persons
 - Agreement on taxation of savings income in form of interest payments (new agreement signed, not yet ratified, introduction of an automatic exchange of information instead of a withholding tax on savings income; entering into force presumably per January 2018)
 - ~ **Withholding Tax Agreements between Switzerland and Austria and Switzerland and the United Kingdom**
 - ~ **Multilateral Convention on Mutual Administrative Assistance in Tax Matters (signed, not yet ratified)**
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Constitutional Principles of Taxation (I)

Art. 127 Federal Constitution

- 1 The general principles of taxation, particularly the circle of taxpayers, and the object of the tax and its calculation, shall be established by statute
- 2 To the extent that the nature of the tax allows it, the principles of universality and equality of tax treatment and of taxation according to economic capacity shall be followed
- 3 Intercantonal double taxation is prohibited. The Confederation shall take the necessary measures



Constitutional Principles of Taxation (II)

“ Principle of universality

- Prohibition of a privileged treatment of certain taxpayers or group of taxpayers
- Prohibition of discrimination and of more burdensome taxation of certain taxpayers or group of taxpayers

“ Principle of equality and ability-to-pay principle

- Each taxpayer must contribute to the fiscal revenue of the state according to his/her economic and personal resources
- Horizontal equality: taxpayers who are in the same economic and personal situations and derive the same amount of taxable income must be taxed identically
- Vertical equality: taxpayers who are in different economic and personal situations and derive a different amount of taxable income must be taxed differently



Constitutional Principles of Taxation (III)

- “ Ability-to-pay principle: Examples of ongoing discussions in Switzerland
 - Exemption of capital gains on private assets from the taxable income tax base: article 16 (3) FDTA
 - Equal effective tax burden of married couples who are taxed together and cohabiting partners who are taxed separately: article 9 and 36 FDTA
 - Lump-sum taxation of non Swiss citizen who do not work in Switzerland: article 14 FDTA
 - Reduction of the double tax burden on dividend distributions; partial dividend taxation: article 18b and 20 (1^{bis}) FDTA



Constitutional Principles of Taxation (IV)

Ability-to-pay principle: Decision of the Federal Supreme Court of 1 June 2007, 2P.43/2006, ATF 133 I 206 on the constitutionality of degressive income tax rates

- “ The Canton of Obwalden introduced the following income tax rates:

Taxable Income	Tax (in CHF)	in %
50'000	5'784	11.57
100'000	3'834	13.83
300'000	46'311	15.43
500'000	65'824	13.16
1'000'000	117'650	11.77

- “ The Federal Supreme Court ruled that such tax rates infringe the ability-to-pay principle; the income tax rate must at least be proportional



Prohibition of Intercantonal Double Taxation (I)

- “ Prohibition of intercanton double taxation: actual and potential double taxation
- “ Principle of non-discrimination:
 - a taxpayer who is only taxable in a canton with a part of his income shall not be treated differently from a taxpayer who is taxable with all of his income in that canton
 - Applicable for both the canton of residence and the canton of source



Prohibition of Intercantonal Double Taxation (II)

- “ Main allocation rules
 - Immovable property may only be taxed by the canton where the property is situated
 - A permanent establishment or an enterprise (carried out by a sole proprietor or a partnership) may only be taxed by the canton where the permanent establishment or enterprise is situated
 - All other kinds of income may only be taxed by the canton where the taxpayer is a resident of (including income from employment and income from movable assets)
- “ Unlike the double taxation treaties, the rules on the prohibition of intercanton double taxation comprise rules on the calculation of the tax base as well



Harmonisation of Direct Taxes (I)

Art. 129 Federal Constitution

- 1 The Confederation shall establish principles on the harmonisation of direct taxes of the Confederation, the Cantons and the Municipalities; it shall take into account the efforts of the Cantons to harmonise their taxes.
- 2 The harmonisation shall concern tax liability, tax object, taxation period, and procedural and criminal law on taxation. Harmonisation shall not cover tax scales, tax rates, and tax-exempt amounts
- 3 The Confederation may issue regulations against arrangements granting unjustified tax advantages



Harmonisation of Direct Taxes (II)

**1 January 2001:
Federal Tax Harmonisation Act (FTHA) took
effect (Steuerharmonisierungsgesetz, SR 642.14)**

Coordination only based on constitutional principles: cantonal tax law differed considerably

- “ Prohibition of intercantonal double taxation
- “ Principle of equality
- “ Ability-to-pay principle

Coordination based on the FTHA

- “ Harmonisation of tax subject, tax object, tax period, tax procedure, tax penal law
- “ Harmonisation on the horizontal and vertical level
- “ No harmonisation of tax allowances and tax rates



Federal Income Tax

Legal basis: Federal Act on the Federal Direct Tax (FDTA) of December 14, 1990 (Bundesgesetz über die direkte Bundessteuer [DBG], SR 642.11)

- ~ Federal income tax on the income of individuals
- ~ Federal corporate tax on the net profit of legal entities
- ~ Source Tax levied on the income of certain individuals and legal entities



Federal Individual Income Tax (I)

Subjects to the Federal Individual Income Tax – Two categories of taxpayers (I)

- ~ Taxpayers with **personal** attachment → Swiss residents → **unlimited** tax liability (world-wide income tax principle)
 - Swiss residence (Art. 3 (1) FDTA)
 - Abode of at least 30 days (with gainful activity) or 90 days (without gainful activity) (Art. 3 (3) FDTA)
- ~ Exception from the world-wide income tax principle: enterprises, permanent establishments and real estate situated abroad are unilaterally exempt from income taxes (Article 6 (1) FDTA)
 - Unilateral exemption method with progression (Article 7 (1) FDTA)



Federal Individual Income Tax (II)

Subjects to the Federal Individual Income Tax – Two categories of taxpayers (II)

- ~ Taxpayers with **economic** attachment → non-residents
→ **limited** tax liability (source principle) (Art. 4 and 5 FDTA)
 - real estate in Switzerland
 - permanent establishment in Switzerland
 - gainful activity without temporary abode
 - board members or directors of Swiss corporations
 - pensions and similar remunerations paid by Swiss institutions/insurance
- ~ Taxation of the Swiss source income
- ~ Ordinary tax assessment or withholding tax



Federal Individual Income Tax (III)

Main income taxing principles

- ~ Principle of totality: overall income taxation (no baskets, no schedules)
- ~ Taxation of the effective income (in principle no taxation of fictitious income)
- ~ Taxation of the net income
 - Deduction of any expenses connected and necessary to derive the taxable income
 - Personal allowances taking into account the individual situation of a taxpayer



Federal Individual Income Tax (IV)

Taxable income

Principle of taxation of the overall income, including:

- ~ income from dependent and independent services (incl. compensatory income)
- ~ income from movable and immovable property
- ~ income from insurances and seniority allowances

Exceptions:

- ~ capital gains on movable and immovable assets if not realized on business assets, e.g. realized on private assets (Article 16 (3) FDTA)
- ~ Inheritance and gifts; some kind of insurances payments; financial aids for low-income people (Art. 24 FDTA)



Federal Individual Income Tax (V)

Deductible Expenses and Allowances

- ~ All expenses related to the earning of income, e.g. professional expenses; expenses for the maintenance of immovable property; expenses for the administration of securities, etc.
- ~ Interest payments, particularly mortgage interest payments
- ~ Payments to company pension plans; insurance fees (partly)
- ~ Allowances for children, dependents and double income couples



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Cantonal Individual Income Tax and Net Wealth Tax

Cantonal Income Tax

- ~ Principle of taxation of the overall income and, unlike the Federal Income Tax, inclusive of capital gains on immovable properties, exempt are however capital gains on movable private assets
- ~ Deductible expenses and allowances: identical to the Federal Tax
- ~ Capital gains on immovable private properties are taxed with a separate real estate capital gains tax (certain cantons including capital gains on immovable business properties)

Cantonal Net Wealth Tax

- ~ Principle of taxation of the overall net wealth including real estate, movable capital assets, annuity insurances and business assets
- ~ Deduction of all debts and deduction of personal allowances



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Income tax rates for individuals

Assumption: single person, taxable income CHF 100,000 or CHF 300,000; tax year 2015

Taxable income	CHF 100,000	CHF 300,000
Federal income tax: (maximum tax rate: 11.5 %)	2.87 %	8.92 %
Cantonal income tax (incl. municipal income)		
~ Berne (City of Berne)	20.89 %	25.64 %
~ Lucerne (City of Lucerne)	14.50 %	17.73 %
~ Zurich (City of Zurich)	13.81 %	21.49 %
~ Zug (City of Zug)	9.81 %	11.36 %



Federal Corporate Income Tax (I)

Types of legal entities Æ Two categories

- “ Corporations: Share Company (AG/SA), Limited Liability Company (GmbH/Sarl), Cooperative Society
- “ Other legal entities: Association, foundation and other legal entities that are treated as legal entities, e.g. investment trusts with direct real estate ownership



Federal Corporate Income Tax (II)

Subjects to the Federal Corporate Tax Æ Two Categories of taxpayers

- “ Taxpayer with **personal** attachment → Swiss residents → **unlimited** tax liability (Art. 50 FDTA); except of enterprises, permanent establishment and real estate abroad (Art. 52 (I) FDTA)
 - Registered office (statutory seat)
 - Place of effective management
- “ Taxpayer with **economic** attachment → non-residents → **limited** tax liability (Art. 51 FDTA)
 - real estate in Switzerland
 - permanent establishment and enterprises (carried out by sole proprietor or partnership) in Switzerland



Federal Corporate Income Tax (III)

Determination of the taxable profit

- ~ In principle, the financial statement is authoritative for corporate tax purposes provided that the financial statement corresponds with the Swiss accounting rules
- ~ Adjustments of the financial statement for corporate tax purposes are only allowed if expressly stated in the tax law, e.g.
 - constructive dividends to a shareholder or an affiliated person
 - commercially unjustified expenses or depreciations
 - earnings not entered into the financial statement



Federal Corporate Income Tax (IV)

Determination of the taxable profit - Example for tax adjustments

- ~ Peter is the main shareholder of P. SA. He granted a loan of CHF 500,000 to P. SA which agreed to pay interest on the loan of 8% per year
 - The interest of 8% is not arm's length, an interest of max 3% would be arm's length (according to the standard interest rates published by the Federal Tax Administration for 2015). Consequences:
 - Based on Art. 58 (1) (b) FDTA, the tax administration will adjust the taxable profit of P. SA
 - P. SA must deduct withholding (anticipatory) tax on the excessive amount of interest (Art. 4 (I) (b) WHTL)
 - In the excessive amount of interest, Peter does not derive income from a loan, but income from a participation in a company (Art. 20 (I) (c) FDTA)



Federal Corporate Income Tax (V)

Relation between the individual shareholder and the company Classic system of economic double tax burden

- ~ Taxation of the profit of the company on the corporate level with the corporate income tax
- ~ Taxation of the profit of the company on the shareholder level with the income tax provided that the profit is distributed to the shareholder

Since 2009: Partial taxation of dividends on the individual shareholder level

- ~ 40 % resp. 50 % of the dividend income from qualifying participation (shareholder holds at least 10 % of the paying company's stock) is exempted from federal individual income tax, i.e. only 60 % (private shareholder) or 50% (business shareholder) of the dividend is taxable (Art. 20 (1^{bis}) and 18b FDTA)
- ~ Similar reliefs are provided in the cantonal tax laws
- ~ Corporate Tax Reform III: Increase of taxation of dividends to 70% intended



Ordinary Corporate Income Tax Rates

Assumption: Company with a taxable profit of CHF 1,000,000; tax rates 2015

Federal corporate tax:

- ~ on the after tax deduction basis 8.5 %
- ~ on the before tax deduction basis (depending on the deductible cantonal tax) ca. 6.7 . 7.2 %

Cantonal corporate tax (incl. municipal and parish tax)

- ~ Zurich (after tax/before tax) 18.3 % / 14.4 %
- ~ Zug (after tax/before tax) 8.2 % / 7.0 %

After tax/before tax: the corporate income tax and the capital tax are deductible from the taxable profit. The tax rate after tax is the statutory tax rate that refers to the tax rate after deduction of the tax. The tax rate before tax refers to the tax rate before deduction of the tax.



Cantonal Corporate Tax & Special tax regimes: Dispute with the EU (I)

Tax «dispute» Switzerland & EU: Political demands of the EU:

~ **Alleged infringement of Article 23 of the Free Trade Agreement from 1972 (receded into the background in the meantime)**

The following are incompatible with the proper functioning of the Agreement in so far as they may affect trade between the Community and Switzerland:

[ō]

(iii) any public aid which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods.

~ **Demand for an implementation of the Code of Conduct on Business Taxation**

Demand for an abolishment of all harmful tax regimes

~ **Similar demands are made by the OECD**




Cantonal Corporate Tax & Special tax regimes: Dispute with the EU (II)

Primarily criticised tax regimes (due to «ring fencing»)

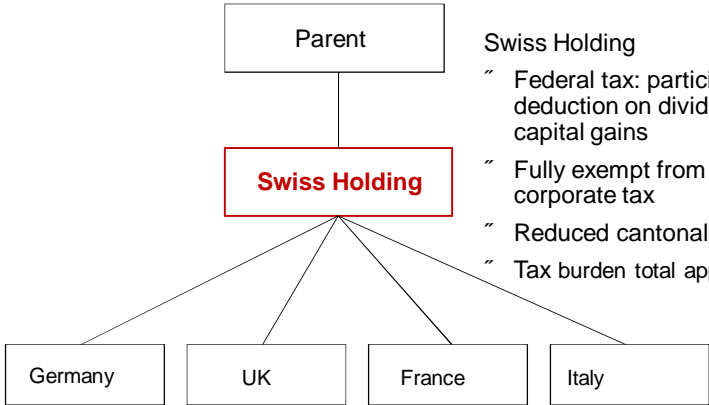
~ **Holding companies:** companies whose purpose is mainly the holding and administration of participations and which refrain from exercising a business activity in Switzerland are (after fulfilment of some additional quantitative requirements) exempted from the cantonal corporate income tax.

~ **Domicile companies** (Administrative company or mixed company): companies which exercise only administrative and/or auxiliary activities in Switzerland are taxed on the profits made abroad only at a rate of 0%-25%, depending upon the importance of the activities in Switzerland.


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Cantonal Corporate Tax – Special tax regimes (III)


Example: Swiss Holding Company: holding company regime



Swiss Holding

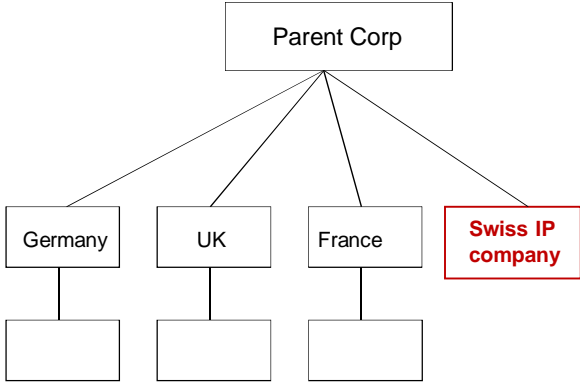
- ~ Federal tax: participation deduction on dividends and capital gains
- ~ Fully exempt from cantonal corporate tax
- ~ Reduced cantonal capital tax
- ~ Tax burden total approx. 0-3 %

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Cantonal Corporate Tax – Special tax regimes (IV)

Example: Swiss IP group company: mixed company regime



Swiss IP company owns the IP of the group; receives royalties from group companies

Taxation:

- ~ On the federal level ordinarily taxed
- ~ Cantonal corporate tax on approx. 5 - 25 % of the income derived abroad (royalties)
- ~ Tax burden total approx. 7 - 11 %

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Proposed Corporate Tax Reform III

- “ Switzerland will abolish the criticised tax regimes
- “ Switzerland will introduce other measures that are in line with EU law and the OECD project on Base Erosion and Profit Shifting (BEPS)
- “ Proposed alternatives; all proposals concern the cantonal corporate tax:
 - Introduction of a patent box (by all cantons)
 - Introduction of multiple deductions of research and development expenses (optional)
 - Introduction of a notional interest deduction on equity capital (similar to the Belgian or Liechtenstein system; disputed)
 - General reduction of the ordinary corporate income tax rate for all companies to a competitive level (around 12 . 15%; including the federal direct tax)
- “ The legislative proposal was published on 5 June 2015 (Botschaft zum Unternehmenssteuerreformgesetz III, BBl 2015, 4733, 4875); debate in the parliament in 2015 and 2016



Cantonal Tax on the equity capital of corporations (capital tax)

Tax on the share capital, reserves and retained earnings

- “ Thin capitalisation rules must be observed
- “ Tax rate 0.03 . 0.5 % depending on the Canton



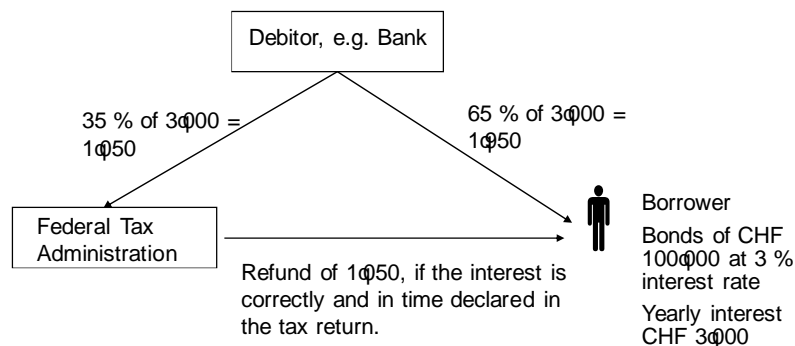
Withholding (Anticipatory) Tax (I)


- ~ Legal basis: Withholding Tax Law of October 13, 1965 (Bundesgesetz über die Verrechnungssteuer [VStG], SR 642.21)
- ~ Tax Rate on dividends and interest: 35 %
- ~ Tax objects: dividends distributed by Swiss companies to Swiss and foreign shareholders; interest paid by Swiss residents on savings accounts, debentures and bonds to Swiss or foreign obligee
- ~ Requirements for a full or partial refund of the withholding tax:
 - Swiss residents: if they correctly and timely fill in their tax returns → full refund
 - Swiss non-residents: if they are entitled to a double taxation treaty or if Article 15 of the Agreement on Taxation of Savings Income between Switzerland and the EU applies → full or partial refund according to the tax treaty or the Agreement



Withholding (Anticipatory) Tax (II)

Concept of the Swiss Withholding Tax on Dividends and Interests



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Proposed Revision of the Withholding Tax System for Interest: Change to the Paying-Agent-Tax system

Debtor: Any Swiss or foreign
- bank
- company
etc.

Debtor of the interest → Gross amount of interest → Paying agent (Bank/financial institute)


2. Payment of 35 to FTA

2. Payment of 65 to S.

ESTV → 3. Refund of 35 to S., if entitled → S.

- “ Interest payments from Swiss and foreign debtors to Swiss residents will newly be subject to the anticipatory tax
- “ Interest payments from Swiss debtors to foreign residents will no longer be subject to the anticipatory tax

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Stamp Tax

- “ Legal basis: Stamp Tax Law of June 27, 1973 (Bundesgesetz über die Stempelabgaben [StG], SR 641.10)
- “ Three kind of stamp taxes
 - Stamp tax on the issuance of shares in Swiss corporations
 - Stamp tax on the transfer of domestic and foreign securities
 - Stamp tax on insurance premiums
- “ Tax rate on the issuance of shares: 1 %
- “ Abolished per January 1, 2013:
 - Tax on the issuance of debentures
 - Tax on the issuance of medium term notes and money market papers
- “ Tax exemption in the case of reorganization, e.g. spin-offs, mergers, change of the legal structure, etc.

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Value Added Tax (VAT)

- ~ Legal basis: Value Added Tax Law of 12 June 2009 (Bundesgesetz über die Mehrwertsteuer [MWStG], SR 641.20)
- ~ Consumption tax mainly following the principle of the EU directive on VAT levied on all phases of production and distribution as well as on the import of goods, domestic service industry and the import of services from abroad
- ~ Tax rates 2015
 - Standard tax rate 8 %
 - Reduced tax rate on certain categories of goods, e.g. food, medicine, books 2.5 %
 - Special reduced tax rate for hotel and lodging industry 3.5 %
- ~ On-going parliamentary discussion: simplification of the VAT, e.g. only two tax rates instead of three, abolishment of certain exemptions



Inheritance and Gift Tax (Cantons)

- ~ Taxpayer: Beneficiary of the inheritance or the gift
- ~ Assessment basis: market value of the assets (reduced values for real estate and businesses)
- ~ Spouses are exempt from the inheritance and gift tax in all Cantons
- ~ Descendants are exempt from the inheritance and gift tax in all Cantons, except of 4 Cantons
- ~ Tax rates depend on the degree of relatedness of the deceased/donor to the beneficiary and on the amount of the inheritance/gift; maximum tax rate up to 40 % for non-related persons