The Inward Investment and International Taxation Review

Eleventh Edition

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Tim Sanders

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THE INWARD INVESTMENT AND INTERNATIONAL TAXATION REVIEW

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PREFACE

This edition has been revised to describe domestic tax changes that have occurred in each jurisdiction since the last edition, including those made, and proposed, in response to the covid-19 pandemic. Where appropriate, the contributors also update the progress made in their respective jurisdictions in implementing laws to comply with the Base Erosion and Profit Shifting (BEPS) Actions.

The pandemic's economic impact has been profound, and while temporary reliefs have been introduced in many countries, and are described, at this stage it is unclear how countries will change their tax laws in the longer term and balance the need to recover the enormous costs of the pandemic with the desire to stimulate economic growth in contracting economies. How this conflict will evolve and be resolved seems likely to be the major tax story of 2021. This preface will make some tentative observations in this area.

As will be seen from the chapters herein, in 2020, countries continued to implement changes to their domestic laws to comply with BEPS Actions notably in respect of hybrid entities and instruments, controlled foreign companies and transfer pricing. One key area highlighted last year, which has progressed in 2020, is the taxation of the digital economy. In October 2020, the OECD published two blueprints and launched a public consultation as part of its work on the taxation of the digital economy. These blueprints are key developments in the international conversation on the challenges of taxing the digital economy. However, although the OECD has progressed efforts in 2020 to find a consensus, many countries, frustrated by the lack of concrete law, are progressing their own unilateral measures to tax the digital economy. For example, Spain's 'Google Tax' is due to come into force on 16 January 2021 and the United Kingdom has already introduced a Digital Services Tax. Pressure for unilateral action is likely to increase as countries look for new tax sources to recover revenue spent on fighting covid-19. Potentially taxation of digital companies allows many economies to raise material amounts of tax revenue without an adverse economic impact on the recovery in their own jurisdictions, where the digital taxpayers often have minimal presence and pay little tax. However, that analysis must factor in whether the US, that has most to lose (as many of the largest digital companies are US-based), will take retaliatory action. The previous political regime showed that it is willing to impose tariffs on goods imported from countries that unilaterally impose a digital tax. This is an area to watch carefully in 2021. The increased pressure to tax the digital economy because of the covid-19 pandemic has been acknowledged by the OECD, with the OECD Secretary-General stating on an online press conference on 12 October 2020 that digital businesses that are thriving during the pandemic would 'be the targets' of countries looking for resources to 'make ends meet'.

Many countries have introduced packages of short-term tax measures to help businesses and individuals through the pandemic. These may comprise deferring tax payments and

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extending filing deadlines, to subsidies such as those afforded to businesses that furloughed staff and measures allowing more generous loss carry-back. The question countries must face in 2021 is how long they can afford to provide these short-term reliefs and what will replace them. There is a lot of pressure to help certain sectors particularly hard hit by the pandemic such as tourism and hospitality and, for example, Austria's reduction in VAT to 5 per cent on restaurants, and admission to cultural events for 2021 is the sort of measure one might expect to be introduced elsewhere.

The wider question is how countries can reconcile the desire to provide economic support and stimulus for growth after the pandemic with the need to recover the budget deficit caused by covid-19 pandemic-related costs: how to raise additional tax from shrinking economies, without stifling any recovery. As referred to above, one obvious target is to tax the digital economy; another possible avenue is to introduce measures that encourage inward investment. It is also likely that in the drive to increase tax revenues, many tax authorities will take a far more aggressive and proactive approach to recover tax and penalties from tax payers regarded as non-compliant or participating in perceived tax avoidance. However, it would be naïve to imagine that these sorts of measures alone will be enough and even if one factors in tax changes in areas such as personal capital taxes, it seems likely that some increase in business and personal income taxes will be needed.

How US tax reform in 2021, post the presidential election, evolves is another factor likely to impact the wider tax landscape and is an area that needs to be kept under review.

It is hoped that this volume will prove to be a useful guide to the tax rules in the jurisdictions where clients conduct their businesses. Each chapter aims to provide topical and current insights from leading experts on the tax issues and opportunities in their respective jurisdictions. While specific tax advice is always essential, it is also necessary to have a broad understanding of the nature of the potential issues and advantages that lie ahead; this book provides a guide to these.

I should like to thank the contributors to this book for their time and efforts, and above all for their expertise. I would also like to thank the publisher and the team for their support and patience. I hope that you find the work useful, and any comments or suggestions for improvement that can be incorporated into any future editions will be gratefully received.

The views expressed in this book are those of the authors and not of their firms, the editor or the publishers. Every endeavour has been made to ensure that what you read is the latest intelligence.

Tim Sanders
London
January 2021

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Chapter 28

SWITZERLAND

Frédéric Neukomm and Floran Ponce[1]

I INTRODUCTION

Switzerland is a federal democracy. As such, corporate taxes are levied on the federal, cantonal and communal levels.

Switzerland is a stable, liberal country with a business-friendly environment, relatively low corporate income tax and an extensive double tax treaty (DTT) network.

Unlike 2020, which saw major changes to Swiss tax law with the Tax Reform and Social Security Funding Act (the Tax Reform Act) entering into force on 1 January 2020, major changes are not planned for 2021.

Although, the Tax Reform Act abolished the special cantonal statuses for holding companies and administrative companies, Switzerland has remained attractive to businesses and businesses have been able to benefit from new advantages introduced under the Tax Reform Act, such as IP boxes, as well as lower corporate income tax rates in many cantons.

Additionally, tax rulings allow businesses to secure a specific tax treatment prior to relocating to Switzerland. Additionally, tax rulings may inform businesses of the tax consequences related to specific transactions.

II COMMON FORMS OF BUSINESS ORGANISATION AND THEIR TAX TREATMENT

i Corporate

The most common corporate structures in Switzerland are the company limited by shares and the limited liability company (LLC). However, large companies, with the exception of US multinational enterprises (MNEs) (check the box), generally do not use LLCs.

Companies limited by shares require a minimum share capital of 100,000 Swiss francs, while LLCs require a minimum share capital of 20,000 Swiss francs.

Although less common than the two aforementioned types of companies, Swiss law also permits partnerships limited by shares.

Companies are legal persons, and thus are subject to Swiss taxes. Direct corporate taxes include federal and cantonal corporate income tax and cantonal capital tax. Companies are also responsible for collecting withholding tax on dividend distributions.

1 Frédéric Neukomm and Floran Ponce are partners at Lenz & Staehelin.

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ii Non-corporate

Non-corporate entities include general partnerships and limited partnerships. They are rarely used by large businesses, because general partners must be individuals.

Collective investment schemes include investment companies with variable capital (open-end), fund contracts (open-end) and limited partnerships for collective investments (closed-end).

The above structures are transparent for income tax purposes (except for real estate funds), so the assets and income derived therefrom are attributed to the partners or fund participants based on their share of the partnership or fund; Swiss collective investment schemes must pay withholding tax on the income they realise (irrespective of whether that income is distributed or accumulated).

III DIRECT TAXATION OF BUSINESSES

i Tax on profits

Determination of taxable profit

Corporate taxpayers are subject to corporate income tax on worldwide income, with the exception of income from foreign immovable property, permanent establishments and business enterprises. Corporate income tax is levied on the net profit.

In principle, the taxable income is the same as the profit listed in statutory financial statements, which is determined on an accrual basis. Generally, all expenses are deductible, provided they are commercially justified. Corrections are allowed when tax law stipulates that a value different from that in the books of account should be used. For instance, if the tax authorities consider depreciations or provisions excessive, they will be reduced or denied.

Companies may record depreciations using either the declining-balance method or the straight-line method, but for tax purposes, certain minimum rates must be respected (e.g., for industrial buildings, 3–4 per cent using the declining-balance method and 1.5–2 per cent using the straight-line method, for intangibles, 40 per cent using the declining-balance method and 20 per cent using the straight-line method).

A provision for one-third of the inventory value is permitted for federal and cantonal tax purposes. Further provisions for liabilities and dubious receivables are allowed if commercially acceptable. The standard amount is 5 per cent for Swiss receivables and 10 per cent for foreign receivables.

If a company concludes a contract with a shareholder or related party, it must be at arm's length. If not, consideration in excess of the arm's-length consideration is reclassified as a constructive dividend. Amounts reclassified as constructive dividends are not considered justified expenses, so they cannot be deducted from the company's taxable profit. Additionally, withholding tax (35 per cent) may be levied on the constructive dividend.[2]

Capital and income

As a rule, both income and capital profit are subject to federal, cantonal and communal corporate income taxes.

However, income (e.g., dividends) from and capital gains on qualifying participations benefit from participation relief.

2 See Section VI.i.

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Participation income is eligible for participation relief if the receiving company owns at least 10 per cent of the equity in the distributing company, if the participation is worth at least 1 million Swiss francs (for dividends) or if the receiving company is entitled to at least 10 per cent of the distributing company's profit and reserves. Participation relief is granted for capital gains if one of the above conditions is fulfilled and the participation has been held for at least one year.

Additionally, some cantons levy a separate real estate capital gains tax on gains arising from the sale of real estate in lieu of ordinary cantonal and communal corporate income tax.

Losses

Under Swiss tax law, losses may be carried forward for seven years; there are no provisions for carry-back. Losses must be carried forward using the first in, first out (FIFO) method.

Older losses (more than seven years) may be carried forward during a financial restructuring because of insolvency, if carrying forward said losses will allow the company to balance its books of account.

Losses survive changes in ownership. Additionally, in the event of a merger, the losses from both companies may be carried forward, except in the case of tax avoidance or abuse of a right (e.g., merger with a company that has liquidated most or all of its assets).

Rates

The federal corporate income tax rate is 8.5 per cent on profit after tax; cantonal and communal corporate income tax rates vary.

Following the Tax Reform Act's entry into force on 1 January 2020, many cantons lowered their corporate income tax rates. Current effective rates (federal, cantonal and communal taxes included) are: 13.04 per cent in Basle; 13.99 per cent in Geneva; 13.79 per cent in Lausanne (Vaud); 11.91 per cent in Zug; and 18.19 per cent in Zurich.

Administration

The federal tax authority is the Federal Tax Administration (FTA). The FTA is responsible for federal taxes, including withholding tax. Each canton has its own tax authorities; the cantonal tax authorities are responsible for income tax, including federal income tax.

Taxpayers are required to file an annual tax return during the three months following the close of the business year; extensions may be requested.

Both the tax authorities and the taxpayer participate in the tax assessment process; taxes are assessed based on the tax return submitted by the taxpayer.

The tax authorities are responsible for determining relevant facts and applicable legal provisions. They are allowed to conduct investigations, including inspections of the books of accounts and any supporting documents. The tax authorities determine the taxes due; this decision is communicated to the taxpayer in writing and includes the tax basis, tax rate and taxes due.

Tax assessments can be challenged before the tax authorities (formal complaint). If the dispute is not resolved, the taxpayer can appeal; the matter then goes to court (federal or cantonal, depending on the matter being appealed). The Swiss Federal Supreme Court is the highest Swiss court.

Tax rulings are very common in Switzerland. However, certain types of rulings are now subject to spontaneous exchange under spontaneous exchange of information agreements and in accordance with the base erosion and profit shifting (BEPS) rules.

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Tax grouping

Swiss tax law does not allow for tax consolidation (except for VAT). Companies that are part of a group are taxed as individual companies, subject to ordinary tax rules.

ii Other relevant taxes

Capital tax

Capital tax is a direct tax that is levied on companies' net equity (paid-up capital, as well as open reserves and taxed hidden reserves). Capital tax is levied annually, and rates vary (0.001–0.525 per cent) between cantons. Some cantons permit corporate income tax to be credited against capital tax, meaning capital tax is levied only if it exceeds the cantonal corporate income tax due. There is no federal capital tax; it is only levied by the cantons.

In the event of thin capitalisation, the part of the loan reclassified as equity is subject to capital tax.[3]

Issuance stamp duty

Issuance stamp duty is levied on capital contributions from shareholders to Swiss companies, meaning it is levied on both the initial creation of share capital as well as subsequent increases of share capital and contributions without issuance of new shares. Stamp duty is levied at 1 per cent. The first 1 million Swiss francs in share capital is exempt from stamp duty. Exemptions are also granted following a merger or similar restructuring.

Transfer stamp duty

Transfer stamp duty is levied when there is a transfer against consideration of a security subject to stamp duty and the transfer involves a Swiss securities dealer. Securities subject to stamp duty include Swiss and foreign bonds, shares, participation certificates, dividend rights certificates and units in collective investment schemes. A Swiss securities dealer is defined as a bank, securities trader or professional intermediary (individual or legal person) or a company holding over 10 million Swiss francs in taxable securities. Transfer stamp duty is levied at 0.15 per cent for securities issued by Swiss residents and 0.3 per cent for foreign securities.

VAT

The ordinary VAT rate is 7.7 per cent. VAT on accommodation is 3.7 per cent and VAT on essential goods is 2.5 per cent.

Payroll taxes

A social security contribution of 10.25 per cent is levied on employment income; half is paid by the employer and half is paid by the employee (via withholding). Unemployment insurance is also levied on employment income.

Additionally, employers are required to levy tax at source on salaries paid to employees not resident in Switzerland or to foreign employees without a long-term resident permit.

3 See Section VII.i.

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IV TAX RESIDENCE AND FISCAL DOMICILE

i Corporate residence

Companies with either their statutory seat or their place of effective management in Switzerland are considered Swiss tax residents for tax purposes.

A company is considered to have its place of effective management in Switzerland if its economic centre is located in Switzerland.

In determining the economic centre, the tax authorities consider a variety of factors and the presence of multiple connecting factors with Switzerland is sufficient to consider that the place of effective management is in Switzerland. The predominant factor is the place where management is carried out (i.e., the day-to-day actions required to carry out the company's statutory purpose). Secondary factors include the place where fundamental decisions are made and the place where administrative work (e.g., accounting, correspondence) is carried out. A passive company's (e.g., a group financing company) place of effective management is where its strategic decisions (e.g., decisions about refinancing, loans and loan conditions) are made.

The place of effective management for companies created by individuals for asset management purposes is the jurisdiction in which the controlling individual or individuals reside.

ii Branch or permanent establishment

Non-resident companies are liable to Swiss corporate income tax and capital tax on income and capital allocated to a Swiss permanent establishment.

For Swiss direct tax purposes, the definition of permanent establishment is similar to the definition in the Organisation for Economic Co-operation and Development (OECD) Model Tax Convention on Income and on Capital (the OECD MC). It is defined as a 'fixed place of business through which the business of an enterprise is wholly or partly carried on' (Article 51, Paragraph 2 of the Swiss Federal Income Tax Act of 14 December 1990). Examples include branches, factories, dependent agents with a fixed place of business and construction projects lasting at least 12 months.

Switzerland has an extensive network of DTTs, most of which follow the OECD MC, which provide allocation rules for permanent establishments.

Swiss tax rules stipulate that the direct (objective) method should be used when determining a Swiss permanent establishment's profit. The Swiss permanent establishment's profit is thus based on its books of account and is independent of the entity's total profit.

Switzerland does not levy branch profit tax. Consequently, the remittance of branch profits to a foreign company with its place effective management outside of Switzerland is not subject to Swiss withholding tax.

V TAX INCENTIVES, SPECIAL REGIMES AND RELIEF THAT MAY ENCOURAGE INWARD INVESTMENT

i Holding company regimes

Previously, holding companies were exempt from most cantonal and communal corporate income taxes. However, this was abolished when the Tax Reform Act entered into force on 1 January 2020. Nevertheless, companies continue to benefit from participation relief for qualifying participations.

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Federal corporate income tax participation relief

As explained above, qualifying participation income and capital gains on qualifying participations benefit from participation relief.[4]

ii IP regimes

The Tax Reform Act introduced a mandatory cantonal patent box regime as a replacement measure for the elimination of the special tax statuses. The patent boxes are limited to patents and similar rights; copyrighted software is not included.

The cantonal patent boxes use the OECD-compliant modified nexus approach, which requires a direct nexus between the income taxed at the preferential rate and the activity that generated that income; the patent boxes allow for an up-lift of qualifying expenditure. The cantonal tax boxes may provide tax relief for up to 90 per cent of patent-related income. For instance, the cantons of Basle-City, Zug and Zurich grant tax relief for 90 per cent of patent-related income, while the canton of Geneva grants tax relief for only 10 per cent; the canton of Vaud has yet to publish its patent box provisions. However, total tax relief from Tax Reform Act deductions (e.g., patent box, R&D deductions, step up) is limited to 70 per cent of a company's taxable profit.

iii State aid

State aid is granted in the form of federal and cantonal tax holidays. The Swiss Federal Act on Regional Policy provides federal tax incentives for creating or preserving jobs in certain regions of Switzerland. Tax relief is limited to an annual amount of 95,000 Swiss francs per job created or 47,500 Swiss francs per job preserved, for a maximum of 10 years. The companies profiting from such tax relief and the number of jobs to be created or preserved are made public.

Cantonal tax holidays are granted for up to 10 years, but contrary to the federal tax holidays, cantonal tax holidays are not restricted to specific economic sectors or geographical areas. Cantonal tax holidays are based on the nature of the planned investment, its economic importance to the canton and the number of new jobs the company will create. Tax relief can take the form of a full or partial exemption from cantonal and communal corporate income and capital taxes.

Manufacturing and industrial businesses typically qualify for tax holidays. Other businesses (e.g., commercial, finance, services) may qualify if they complement existing local business and industries and create significant new employment opportunities.

Further, like many governments around the world, the Swiss government has approved aid packages to provide assistance to businesses badly affected by covid-19. For instance, Switzerland introduced a 40 billion Swiss franc guaranty programme to facilitate bank lending to Swiss SMEs. Under the covid-19 loan programme, businesses can apply for a loan of up to 500,000 Swiss francs and under the covid-19 plus loan programme, businesses can apply for a loan of between 500,000 Swiss francs and 20 million Swiss francs; loans are limited to 10 per cent of a company's annual turnover. Further, the Swiss government introduced additional measures to aid Swiss start-ups. Under these measures, cantons can

4 See Section III.i.

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provide a guaranty programme granting loans of up to one million Swiss francs to start-ups; 65 per cent is guaranteed by the federal government and 35 per cent is guaranteed by the canton.

iv General

Switzerland has relatively low corporate income tax rates and most cantons further lowered their corporate income tax rates when the Tax Reform Act entered into force on 1 January 2020 (to compensate for special cantonal statuses being abolished).

Further, Switzerland's extensive DTT network eliminates many instances of double taxation, and dividends paid by Swiss resident companies are often eligible for a full or partial refund under a relevant DTT.

Additionally, the Tax Reform Act included a step up for foreign companies relocating to Switzerland, so companies can disclose their unrealised gains without Swiss tax consequences and additional depreciation deductions are granted during the initial few years following relocation to Switzerland.

VI WITHHOLDING AND TAXATION OF NON-LOCAL SOURCE INCOME STREAMS

i Withholding on outward-bound payments (domestic law)

Swiss companies must levy a 35 per cent withholding tax on profit distributions (including constructive dividends and liquidation proceeds) to shareholders or related parties, irrespective of whether the beneficiary is a Swiss tax resident.

Although interest on bonds and other debt certificates issued by Swiss companies is subject to Swiss withholding tax, generally, withholding tax is not levied on interest paid on private loans.

Under the 10/20/100 non-bank rule, loans from 10 non-bank lenders with identical terms (loan debentures) and loans from 20 non-bank lenders with variable terms (cash debentures) are treated as bonds, provided that the financing exceeds 500,000 Swiss francs. Exceptions exist for intercompany loans.

Further, a company shall be deemed a bank for withholding tax purposes if it has at least 100 non-bank lenders or private placements, or both, and its financing or placements, or both, exceeds 5 million Swiss francs. Interest paid by banks is subject to withholding tax; some exceptions apply.

Royalty payments are not subject to withholding tax.

ii Domestic law exclusions or exemptions from withholding on outward-bound payments

Swiss taxpayers (companies and individuals) may request a withholding tax refund. The refund will be granted if certain conditions are fulfilled (e.g., the taxpayers have fulfilled all of their reporting obligations).

Non-resident taxpayers may claim a partial or total refund of Swiss withholding tax if there is a DTT between Switzerland and their country of residence.

A simplified notification procedure can be requested for intra-group distributions to Swiss parent companies or to parent companies resident in a DTT country.

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iii Double tax treaties

Switzerland has an extensive network of DTTs, most of which closely follow the OECD MC. Switzerland has concluded treaties with over 80 jurisdictions, including most European countries, the United States, Russia, Japan and China. In 2020, Switzerland signed protocols with Cyprus, Liechtenstein and Malta amending the DTTs to bring them up to the minimum BEPS standards. Further, the Swiss Federal Council adopted key measures concerning a new DTT with Bahrain, as well as amendments to the DTT with Kuwait.

Additionally, an agreement between Switzerland and the European Union eliminates withholding tax if the parent company has directly held 25 per cent or more of the subsidiary's share capital for at least two years.

To qualify for treaty benefits, certain conditions must be met. The foreign parent company must be the beneficial owner of the dividend income. Further, the withholding tax refund will not be granted if the FTA determines that there is DTT abuse. In assessing whether a structure is abusive, the FTA examines whether there is sufficient capitalisation (30 per cent) and whether the parent company has substance (personnel and premises) in its country of residence. Generally, holding companies must demonstrate that they hold multiple companies, not just the Swiss company requesting treaty relief.

Maximum withholding tax rates

State	Dividends				Interest	Royalties
	Ordinary maximum (per cent)	Maximum on distributions from a subsidiary (per cent)	Minimum required ownership in subsidiary (per cent)	Holding period (years)		
China	10	5	25	N/A	10	9
France	15	0	10	N/A	0	5
Germany	15	0	10	1	0	0
Italy	15	15	N/A	N/A	12.5	5
Japan	10	5/0	10/50	N/A	10	0
Luxembourg	15	0	10	2 (5 per cent if less)	10	0
Netherlands	15	0	10	N/A	0	0
Russia	15	5	20 (at least 200,000 Swiss francs)	N/A	0	0
United Kingdom	15	0	10	N/A	0	0
United States	15	5	10	N/A	0	0

iv Taxation on receipt

As a rule, Swiss treaties use the exemption method to eliminate double taxation; however, the credit method is used for foreign source dividends, interest and royalties.

As previously explained, participation relief is available under certain conditions.[5] No credit is granted if the income is exempted under participation relief provisions.

5 See Section III.i.

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VII TAXATION OF FUNDING STRUCTURES

i Thin capitalisation

Swiss federal and cantonal tax rules contain thin capitalisation safe harbour provisions (maximum debt rule per asset class based on their book or fair market value); for example, 100 per cent for cash, 85 per cent for accounts receivable and inventory, 70 per cent for investments in subsidiaries, 50 per cent for furniture and equipment, 70 per cent for property and plants (commercially used) and 70 per cent for intangibles.

Furthermore, the FTA publishes annual safe harbour interest rates for loans granted to related parties. Interest paid on debt exceeding the maximum allowable debt and interest rates exceeding the safe harbour rates are reclassified as constructive dividends if paid to a shareholder or related party. Consequently, such interest is not a deductible expense for federal and cantonal income tax purposes and is subject to withholding tax at a rate of 35 per cent (which may be reduced under an applicable tax treaty).

However, the rules set out above are merely safe harbour rules and the taxpayer may prove that a different arm's-length debt-to-equity ratio or interest rate should be used.

ii Deduction of finance costs

As mentioned above,[6] companies may not pay interest on loans from shareholders or related parties in excess of what would be paid to an unrelated third party. Generally, there are no other restrictions on interest deductions. In particular, Switzerland has not adopted BEPS Action 4 limiting interest deductions.

In the case of a leveraged acquisition, the absence of consolidated taxation for company groups means interest on the acquiring company's debt cannot be deducted by the target company if the latter does not have operational income. Further, the Swiss tax authorities may treat debt push-down strategies in a leveraged acquisition as tax avoidance.[7]

iii Restrictions on payments

Swiss company law states that dividends 'may be paid only from the disposable profit and from reserves formed for this purpose' (Article 675 of the Swiss Code of Obligations). Thus, interim dividends are not permitted.

Swiss accounting rules permit a parent company to temporarily record dividends paid by a subsidiary in the business year in which the subsidiary earned the profit distributed as dividends, rather than in the year in which the subsidiary decided on the dividend amount. This practice is accepted by the Swiss tax authorities provided that, upon distribution, the dividends are recorded in the income statement and certain procedural conditions are met.

iv Return of capital

Repayments of capital contributions are not subject to withholding tax and are tax-exempt for individuals who are Swiss tax residents; this includes both share capital and share premium. Share premium can be distributed without capital reductions. However, share premium must be listed in a clearly marked capital contribution reserve and validated by the FTA.

6 See Section VII.i.

7 See Section VIII.i.

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Further, under the Tax Reform Act, listed companies cannot distribute capital contribution reserves unless they first distribute an equal or greater dividend, or the capital contribution reserves were created during an inbound relocation (to Switzerland).

VIII ACQUISITION STRUCTURES, RESTRUCTURING AND EXIT CHARGES

i Acquisition

Acquisition vehicle

Acquisitions can be carried out using a local or non-local entity.

When using a foreign parent company to acquire a Swiss company, investors should ensure that the foreign parent company is located in a jurisdiction that has a DTT with Switzerland so as to reduce or eliminate withholding tax on dividend distributions. Otherwise, it is advisable to use an intermediary holding company located in a jurisdiction that has a DTT with Switzerland, provided it complies with the criteria for treaty relief.[8]

Additionally, investors should be aware of the 'old reserves theory'. Under this theory, if a foreign shareholder transfers shares in a Swiss company to a shareholder located in a jurisdiction with a more favourable DTT, withholding tax may continue to be levied on distributable reserves existing at the time of the transaction at the same rate applicable to a tax resident of the first jurisdiction if at the time of the transfer, the company had commercially distributable reserves and assets not economically required.

Acquisition structure

Acquisitions may be structured as either a share deal or an asset deal.

Asset deals tend to be more favourable for buyers, because a step-up in basis is allowed, while share deals are beneficial for sellers, in particular for individual sellers, because individuals are not subject to tax on gains arising from private assets, but are subject to income tax on dividends.

Asset deals permit the company to record part of the purchase price as goodwill. Payment in excess of the assets' market value is recorded as goodwill; goodwill can be depreciated.[9]

Transferred assets may be subject to VAT and transfer stamp duty (for transfers of securities).

In the case of a share deal, the purchase price is recorded in the books of account as the share value. This value cannot be decreased (unless the market value decreases). If the buyer or seller is a professional securities dealer then transfer stamp duty will be levied.

Special attention must be paid to rules concerning indirect partial liquidation and transposition during share deals involving sales by individuals resident in Switzerland, because tax-free capital gains can be retroactively reclassified as taxable participation income.

The criteria for indirect partial liquidation are: (1) sale of at least 20 per cent of the share capital in a Swiss or foreign company to a third party; (2) the shares are transferred from the seller's private assets to a company or to the acquirer's business assets (in the case of acquisition by an individual); (3) the target company has commercially distributable reserves at the moment of the transfer and assets beyond those required to run the business; and (4) these assets are distributed to the acquirer during the five years following the acquisition.

8 See Section VI.iii.

9 See Section III.i.

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Generally, indirect partial liquidation can be avoided by adding a clause to the share purchase agreement that prevents distributions during the five years following the transfer.

Transposition occurs under the following conditions: (1) transfer of share capital of a company from the private assets of an individual to a partnership or company in which said individual holds at least 50 per cent of the capital after the transfer; and (2) the consideration is worth more than the nominal value of the transferred shares.

Income resulting from transposition is taxed as participation income, rather than as a capital gain.

Financing structure

Financing can be provided through either equity or debt.

Stamp duty is levied on the creation of equity in excess of the 1 million Swiss francs exemption.[10] Additionally, there is no notional interest deduction.

Ordinarily, interest on debt is a tax-deductible expense.

As previously mentioned, loans granted by shareholders and related parties must be at arm's length. Further, thin capitalisation will result in increased corporate income taxes and capital tax.[11]

As mentioned above,[12] debt push-down in a leveraged acquisition may be regarded as tax avoidance by the Swiss tax authorities, so an acquisition company cannot acquire a target company, merge with it and then deduct interest on loans taken out by the target company. If the Swiss tax authorities consider the debt push-down to be tax avoidance, interest on the loan may not be deducted.

If the acquiring company intends to acquire multiple target companies, one solution is to structure the acquisition as a cascade purchase. In a cascade purchase, a target company first acquires another target company, which in turn acquires another target company, and so on. Because the target companies have operational income and assets that can be leveraged, they can take out loans to fund the acquisition of other target companies and deduct the interest on these loans.

ii Reorganisation

In principle, reorganisations (mergers, demergers, conversions and the transfer of assets) are tax-neutral. The following conditions must be respected for a reorganisation to be tax-neutral: (1) the company remains subject to tax in Switzerland; and (2) there is no re-evaluation of commercial assets.

Additionally, in the event of a demerger, a business unit or part of a business unit must be transferred. Likewise, the intra-group transfer of assets is tax-free, but only for operational assets; there is blocking period of five years (participations and assets that were part of the reorganising cannot be sold for five years).

10 See Section III.ii.

11 See Section VII.i.

12 See Section VII.ii.

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iii Exit

In the event of a reorganisation that leads to downsizing or closing Swiss operations, all transactions between associated enterprises resulting from the reorganisation must be at arm's length, as enumerated in Chapter IX of the OECD Transfer Pricing Guidelines.

Exit tax is levied on hidden reserves upon emigration. Likewise, withholding tax is levied on distributable reserves and hidden reserves. The Tax Reform Act provides a clear legal base for levying exit tax on hidden reserves.

IX ANTI-AVOIDANCE AND OTHER RELEVANT LEGISLATION

i General anti-avoidance

In Switzerland, general anti-avoidance rules (GAARs) are not contained in a specific act. However, the Swiss Federal Supreme Court has developed a general principle of tax avoidance and abuse of rights, applicable to all Swiss taxes. In accordance with this principle, in certain situations, tax authorities have the right to tax a taxpayer's structure based on its economic substance, rather than its legal structure.

According to case law, there is tax avoidance if: (1) the taxpayer has chosen an abnormal structure; (2) it was done with the intention to save on taxes; and (3) the taxpayer would save on taxes if permitted to use the structure.

ii Controlled foreign corporations (CFCs)

Switzerland does not have CFC rules. However, the case law of the Swiss Federal Supreme Court stipulates that a company whose statutory seat is located abroad, but has little or no substance abroad and is effectively managed from Switzerland, may be deemed a Swiss taxpayer.

iii Transfer pricing

The Swiss tax code contains very few rules relating to transfer pricing.

The Swiss tax authorities do not require specific transfer pricing documents, but Swiss tax law states that a company's expenses must be commercially justified and that profits not shown in the company's profit and loss statement still must be included in the taxable profit. Based on these general rules, Swiss tax authorities can correct intra-group transactions that are not at arm's length. In determining whether an intra-group transaction is at arm's length, the Swiss tax authorities follow the OECD Transfer Pricing Guidelines.

It is possible to request an advance pricing agreement from the Swiss tax authorities; the competent authority is the State Secretariat for International Financial Matters.

iv Tax clearances and rulings

Tax rulings are common in Switzerland and help eliminate uncertainty and avoid future disputes.

Generally, it is recommended to request a ruling before entering into a complex transaction or other situation where tax uncertainty could arise.

Rulings concerning tax planning or preferential tax regimes are now automatically exchanged under automatic exchange of information agreements and in accordance with the BEPS rules. This has led to a reduction in the number of rulings, some of which were

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not necessary in the first place. Conversely, rulings concerning the treatment of specific transactions, generally, are not part of the automatic exchange of information and continue to be commonplace.

X YEAR IN REVIEW

2020 started off with major changes to Swiss tax law, with the Tax Reform Act entering into force on 1 January 2020. Although the Tax Reform Act abolished the special cantonal statuses, as well as the principal company reduction, the introduction of IP boxes, R&D deductions and lower cantonal corporate income tax rates means that Switzerland remains attractive to businesses.

2020 also saw the first automatic exchanges of country-by-country reports under the Multilateral Competent Authority Agreement for the automatic exchange of country-by-country reports.

From March 2020 onwards, political and policy discussions have been dominated by covid-19; like many countries around the world, Switzerland had to scramble to introduce emergency aid measures to keep businesses, especially SMEs, afloat. However, the loan guaranty programme rolled out in March and April 2020 has received largely positive feedback.

Switzerland is committed to implementing the BEPS minimum standards and the OECD's Global Forum on Transparency and Exchange of Information for Tax Purposes' 2020 Peer Review Report on the Exchange of Information on Request 'concludes that Switzerland continues to be rated overall Largely Compliant with the international standard'.[13]

In the midst of global, political unrest, as well as uncertainty surrounding the long-term economic effects of covid-19, Switzerland continues to offer a stable, BEPS-compliant environment for companies looking to make inward investments.

XI OUTLOOK AND CONCLUSIONS

We expect 2021 to continue to be dominated by policy discussions about covid-19. As the true economic impacts become known, we would expect the Swiss government to introduce more aid packages to assist struggling SMEs and start-ups and provide aid to hard-hit sectors, such as hospitality and tourism.

Lastly, no tax-related legislative changes are expected, as long as the results of fiscal year 2020 are not known.

13 OECD, *Global Forum on Transparency and Exchange of Information for Tax Purposes: Switzerland 2020* (Second Round) (Paris 2020) 13.

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Appendix 1

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Frédéric Neukomm is a certified tax expert in the Geneva office. His main areas of work are company tax law and tax law for high-net-worth individuals. He also works in the fields of banking and finance.

Enjoying a 'strong experience of transactional tax matters', Frédéric Neukomm is praised by clients for being 'very collegial – truly a team player', 'his experience is extremely extensive' (*Chambers Global* and *Chambers Europe*, 2017). Sources highlight his 'positive attitude and drive for successful outcomes' (*Chambers Global*, 2018).

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Floran Ponce is a lawyer and certified tax expert. He advises Swiss and foreign banks, investment funds and corporations on a broad range of domestic and international tax as well as commercial law matters. He advises them on matters relating to mergers, acquisitions, divestitures, financing transactions and restructurings, as well as on the management of tax affairs and controversies before Swiss tax authorities. He also assists private clients on complex tax matters.

Floran Ponce is a frequent speaker at professional conferences on tax matters. He also teaches specialised tax courses for the master's degree programmes of the University of Lausanne and of the University of Geneva, as well as in the specialised training for the federal tax expert diploma.

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