OVERVIEW OF THE SWISS TAX SYSTEM

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Image
Tax analysis, stock image

The Swiss tax system mirrors Switzerland's federal structure, which consists of 26 sovereign cantons with 2,202 independent municipalities. Based on the constitution, all cantons have full right of taxation except for those taxes that are exclusively reserved for the federal government. As a consequence, Switzerland has two levels of taxation: the federal and the cantonal/communal level. The reform of the income tax system implemented in recent years provided for harmonization of the formal aspects of the various cantonal tax laws, for example, determination of taxable income, deductions, tax periods, and assessment procedures. The cantons and municipalities still have significant autonomy for the quantitative aspects of taxation, however, particularly with respect to determining the applicable tax rates. Consequently, the tax burden varies considerably between cantons/municipalities.

10.1 TAXATION OF CORPORATE TAXPAYERS

10.1.1 Corporate Income Tax – Federal Level

The Swiss federal government levies corporate income tax at a flat rate of 8.5% on profit after tax of corporations and cooperatives. For associations, foundations, and other legal entities as well as investment trusts, a flat rate of 4.25% applies. At the federal level, no capital tax is levied.

Taxable Persons

Taxable persons include Swiss resident legal entities, i.e. Swiss stock corporations, limited liability companies, and partnerships limited by shares, cooperatives, clubs and foundations, and collective investment schemes with direct ownership. Companies which have their registered office or place of effective management in Switzerland are generally considered resident for tax purposes.

Taxable Income

Resident companies are subject to corporate income tax on their worldwide income with the exception of income attributable to foreign permanent establishments or foreign real estate (immovable property). Such income is excluded from the Swiss tax base and is only taken into account for rate progression purposes in cantons that still apply progressive tax rates.

Non-resident companies are subject to tax only on Swiss source income, i.e., income and capital gains derived from Swiss business, permanent establishments, or immovable property, whereas income from immovable property includes income from trading in immovable property.

As a matter of principle, the legally prescribed/statutory accounts of a Swiss company and – in the case of a foreign company the branch accounts – form the basis for determining taxable income. With the exception specific tax adjustments, expenditures recorded pursuant to commercial law are therefore tax deductible, provided that they comply with the dealing-at-arm's-length principle. Revenues from qualifying shareholdings (dividend returns and capital gains) constitute indirect tax exemptions. For tax purposes, losses can generally be carried forward for a maximum of seven years.

Thin Capitalization Rules

The Swiss Federal Tax Administration has issued safe harbor rules for thin capitalization purposes that apply to related party debt. Third-party financing is not affected by these rules. Specifically, a unique asset-based test is used to determine whether a company is adequately financed. The thin capitalization rules require that each asset class must be underpinned by a certain minimum equity portion (generally expressed as a prescribed percent of the fair market value but often the lower book values suffice).

Related-party liabilities exceeding the allowable debt are classified as equity and added back to the taxable capital within the context of the cantonal/communal annual capital tax. Moreover, the allowable interest deductibility on debt is determined by multiplying the allowable debt by the safe harbor interest rates. If interest payments to related parties exceed the amount which can be paid based on the allowable debt, they are added back to taxable profit if market-related prices cannot be proven on an arm's length comparison. In addition, such excessive interest payments are regarded as hidden dividend payments, which are subject to withholding tax.

Group Taxation

Separate entity taxation applies in Switzerland for income tax purposes. It is not anticipated that group taxation will be introduced anytime in the near future.

Group Reorganizations

Reorganization on a tax-neutral basis is generally possible, as long as the applicable tax accounting values of assets and liabilities are adopted, and the obligation to pay taxes in Switzerland continues to exist. However, transaction-specific regulations must also be followed.

10.1.2 Corporate Income Tax – Cantonal and Municipal Level

Due to the harmonization of cantonal and municipal taxes, most of the aforementioned profit determination regulations apply analogously on a cantonal and municipal level (e.g. participation exemption, loss carryforward rules and, in most cases, thin capitalization rules).

Overview of ordinary profit tax rates

Combined effective income tax rates (for direct federal and for cantonal and local taxes) for properly taxed companies in 2020 are between 11.9% and 21.6%, depending on the canton and municipality.

Special Tax Regimes

In contrast to the Swiss federal tax law, all cantonal tax laws provide special tax regimes, in addition to the direct federal tax, which may be obtained provided that the legal conditions of the tax harmonization law are met. Tax proposal 17 will replace the special tax regimes set out below with new measures aimed at underpinning and increasing Switzerland's attractiveness as a location.

www.s-ge.com/corporate-taxation
Facts and figures on Corporate Taxation in Switzerland

Swiss corporate tax reform

To ensure the international acceptance of Swiss corporate tax law with lasting effect, at the end of 2019 several regimes that are no longer internationally recognized were abolished. To guarantee the continued attractiveness of the economic location nonetheless, the abolition of the regimes was accompanied by the replacement measures described below:

A) Reduction of corporate income tax rates
In the course of the tax reform, corporate income tax rates were lowered in most cantons. In some cases, cantons that formerly had high corporate income tax rates compared to Switzerland overall made significant reductions.

B) Patent box
Revenues from patents and comparable rights that are based on qualifying expenditure for research and development can be included in the tax calculation basis with relief applied. The introduction of the patent box is mandatory for cantons, but the level of relief differs from canton to canton and amounts to a maximum of 90%.

C) Additional deduction for research and development
For research and development expenditure that occurs in Switzerland, cantons can provide for an additional deduction of up to 50%. The additional deduction for research and development is optional for cantons.

D) Equity financing deduction
Cantons can provide for a notional interest deduction on the portion of taxable capital exceeding the equity capital required in the long term (so-called security equity capital). This essentially equates to the returns for 10-year government bonds. Where the security equity capital is allotted to internal group loans, an arm's length interest rate can be applied. At present, the equity financing deduction can only be applied in the Canton of Zurich.

E) Relief limit
The cantons must set a limit for the relief from all replacement measures (with the exception of the special rate solution). The maximum relief must not exceed 70% of profits, but the cantons are free to set a lower relief limit.

10.1.3 Capital Tax

Annual capital tax is only levied at cantonal/communal level. The basis for the calculation of capital tax is in principle the company's net equity (i.e. share capital, paid-in surplus, legal reserves, other reserves, retained earnings). The taxable base of companies also includes any provisions disallowed as deductions for tax purposes, any other undisclosed reserves, as well as debt that economically has the character of equity under the Swiss thin capitalization rules. Some cantons provide for crediting the cantonal corporate income tax against capital tax.

The tax rates vary from canton to canton. In 2020 the range lies between 0.0010% and 0.51%. Cantons can grant a reduction on the taxable capital that is allotted to qualifying shareholdings, patents, and loans to group companies.

10.1.4 Tax Relief

Tax relief can be granted at cantonal and communal level and in explicitly defined regions at federal level for qualified new investments for up to 10 years.

Federal Level

The federal government has defined economically weaker regional community centers and regions which are entitled to grant business incentives including partial or full corporate income tax breaks for up to 10 years (see section 14.2.2).

Tax breaks are provided for investment projects that meet certain requirements. Besides the creation of new production-related workplaces or investing, these also include conditions, for instance, that a competitive situation among existing companies should not arise.

Cantonal and Municipal Level

Most cantons offer partial or full tax breaks for cantonal/communal tax purposes for up to 10 years on a case-by-case basis. In particular, incentives may be obtained for creating a new presence or for an expansion project with particular economic relevance for the canton. Practice differs in the individual cantons. Most importantly, however, business incentives are generally granted in connection with the creation of new jobs locally, i.e. requirement of at least 10 to 20 new jobs in most cantons.

10.2 TAX RATE IN INTERNATIONAL COMPARISON

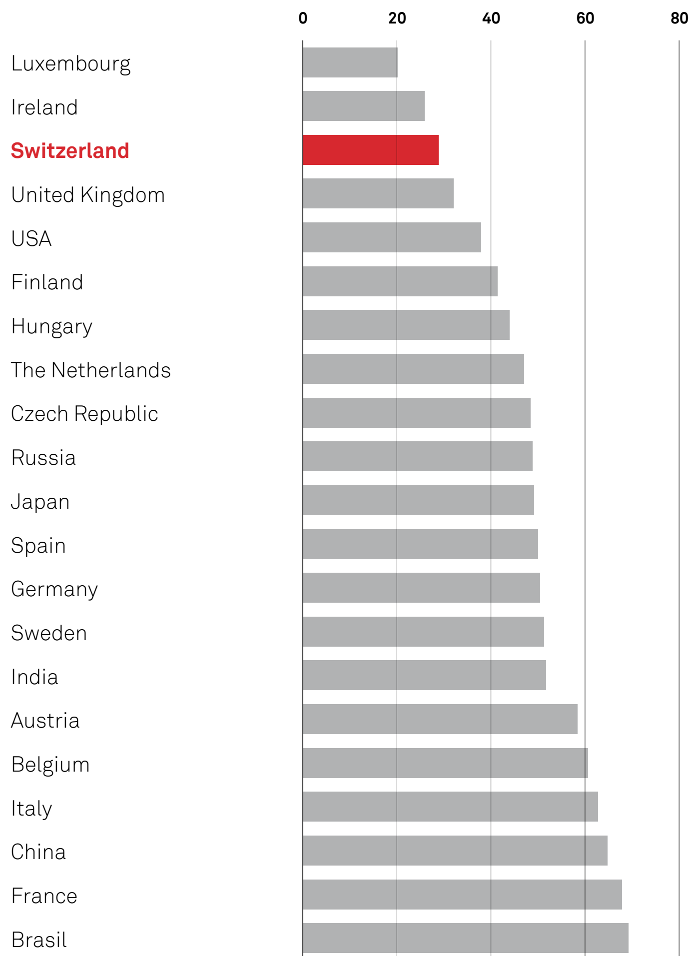
The international comparison of the total tax rate shows that Switzerland has a tax system which is consistently extremely competitive compared with other highly developed industrial countries. The total tax rate measures the amount of all taxes and mandatory contributions borne by the business and is expressed as a percentage of commercial profits. The total amount of taxes borne is the sum of all the different taxes and contributions payable after accounting for deductions and exemptions.

The taxes and contributions included can be divided into the following categories:

- profit or corporate income tax
- social contributions and labor taxes paid by the employer (for which all mandatory contributions are included, even if paid to a private entity such as a pension fund)
- property taxes
- sales taxes (and cascading sales taxes as well as other consumption taxes such as irrecoverable VAT)
- other taxes (such as municipal fees and vehicle and fuel taxes)

It should further be noted that the Swiss tax system is not only attractive for corporate taxpayers but also for individual taxpayers as it provides for a modest tax burden in international comparison as well.

Total Tax Rate, 2018
(% profit)
(FIG. 38)



Source: PricewaterhouseCoopers, 2020

The Swiss tax system is not only attractive for corporate taxpayers but also for individual taxpayers as it provides for a modest tax burden in international comparison.

10.3 TAXATION OF INDIVIDUAL TAXPAYERS

10.3.1 Personal Income Tax

Taxable Persons

Individuals are subject to taxation on federal and cantonal/communal levels if they have their permanent or temporary residence in Switzerland. Temporary residence is given provided the individual, regardless of any temporary interruptions, stays in Switzerland for a) at least 30 days carrying out gainful employment or b) for at least 90 days without pursuing any gainful employment. According to the Swiss tax system, partnerships are transparent; hence each partner is taxed individually.

The income of spouses is added together in accordance with the principle of family taxation. The same applies to any registered civil partnerships. The income of children who are minors is added to that of the person/persons with parental custody. An exception is income earned by minors that is subject to a separate tax.

The assessment and charging of personal income taxes is carried out by the responsible cantonal tax administration. Depending on the canton, the municipality of residence may also be responsible for cantonal and communal taxes.

Individuals who do not establish a domicile or place of residence in Switzerland are liable to taxes in Switzerland to a limited extent if an economic relationship exists between them and certain tax objects located in Switzerland (e.g. land, permanent establishment).

Taxable Income

Resident individuals are subject to tax on their worldwide income. However, revenues derived from business conducted abroad, from permanent establishments, and from immovable property situated abroad are exempt and are taken into account only for the determination of the applicable personal income tax rate (exemption with progression reservation). The total income includes, in particular, income derived through gainful activities, both as an employee and when self-employed, income from movable and immovable property, and income from pensions. Taxable income also includes the notional rent value of property that the resident lives in.

Certain types of income such as inheritance, gifts, matrimonial property rights, subsidies paid from private or public sources, etc. are by law excluded from income tax, however, they could be subject to other taxes such as gift tax or inheritance tax (see Chapter 10.3.6). Individuals can deduct so-called costs of acquisition from their gross income, e.g. professional outlays such as travel costs between their place of residence and their place of work (to a limited extent) or extra costs for refreshments away from home. Social insurance contributions and contributions to occupational pension funds as well as restricted private pensions are likewise deductible. Additional deductions can be asserted for children entitled to maintenance. Married couples (with one or two incomes) can likewise claim an additional deduction. The extent of deductions allowed may vary greatly on a cantonal level. Debt interest in connection with gainful self-employment is fully deductible. In contrast, the deductibility of private debt interest on taxable earnings from movable and immovable private property is limited to a maximum of the total investment income plus 50,000 Swiss francs. For value-retaining property expenditure, an effective or flat-rate deduction may optionally be claimed.

Individual tax rates are typically progressive, whereas a maximum tax rate of 11.5% applies at the federal level. The cantons may set their own tax rates. The applicable cantonal tax rates therefore vary significantly from canton to canton (highest tax rates for cantonal capitals around 10.33% to 27.09%). For married persons and persons living in the same household with children, special tariffs exist.

Capital Gains

Depending on whether a capital gain is realized on personal or business property or on movable or immovable property, such gain is taxed differently. Gains on movable personal property are exempt from taxation whereas gains realized on movable business property are attributed to ordinary income.

Losses

Contrary to personal losses, business losses are tax deductible and may be carried forward for a maximum of seven years, if they cannot be offset against the taxpayer's other taxable income in the respective tax period.

Distribution of Capital Contributions

The repayment of qualifying capital investments is tax-free. It is subject to neither withholding tax (chapter 10.4) nor personal income tax on the part of the receiving individual.

Tax at Source

Foreign employees with their residence/domicile in Switzerland who do not, however, possess a residence permit are taxed on their earned income by a tax deduction at source. The employer is required to deduct the tax owed from the wages and to pay it to the tax authorities. If the source-taxed income exceeds 120,000 Swiss francs (500,000 Swiss francs in Geneva until the end of 2020) per annum, a tax declaration has to be submitted. In all other cases, the tax at source is definitive. The employee can, however, assert special deductions in a separate process. From 2021, persons whose income is below 120,000 Swiss francs can submit a tax return upon application (deadline March 31 of the year following the tax year). Once applied for, this also applies for subsequent years. Without an application, no additional deductions are granted.

Employees who have retained their residence abroad are taxed on their earned income at the source, regardless of their nationality, and in general cannot submit a tax declaration in Switzerland for their earned income. An exception applies from 2021 for persons who have their residence abroad but gain their income almost exclusively from Swiss sources, or whose situation is comparable with those of taxable persons resident in Switzerland. Here too, without an application, no additional deductions are granted.

10.3.2 Wealth Tax

Net wealth tax is only levied at the cantonal/communal level in accordance with the respective cantonal tax laws and rates. The tax is based on net assets. Net assets include immovable and movable assets (e.g. securities and bank deposits, cash, redemption of life insurance, cars, shares of non-distributed inheritances etc.). Shareholdings in foreign businesses and plants are not subject to wealth tax, nor are properties abroad. These assets are, however, taken into account for the calculation of the applicable wealth tax rate, if it is a progressive rate (tax exemption with progression). Individuals can deduct debts from the gross assets, as well as tax exemptions, which vary from canton to canton and according to marital status and whether the person in question has children.

The wealth tax is progressive in most cantons, whereby the cantons can set their own tax rates. The maximum tax burden therefore varies considerably and ranges from 0.135% to 0.870%. The federal government does not charge wealth tax.

10.3.3 Expatriates

Qualifying expatriates are foreign managers and certain specialists (e.g. IT specialists) who are temporarily seconded to Switzerland by their employer for a period of up to five years, i.e. the (secondment) contract may only be limited in time for a maximum of five years. Expatriates may claim tax relief on work-related expenses incurred due to their stay in Switzerland.

The following expenses incurred by expatriates are deductible:

1. necessary relocation costs including travel costs to and from Switzerland,
2. reasonable accommodation costs in Switzerland, if the residence abroad is still maintained for personal use (i.e. no renting during secondment),
3. costs for children of school-going age attending a private school provided that residence is in Switzerland and if local state-funded schools cannot offer adequate educational provisions in their language. Instead of identifying the actual costs for relocation and accommodation, the taxpayer may claim a monthly lump-sum deduction which may vary from canton to canton. Any reimbursement from the employer of work-related costs incurred by the expatriate must be declared in the employee's payslip.

The entitlement to benefit from expatriate status for tax purposes ceases once temporary employment is replaced or superseded by a permanent position.

10.3.4 Cross-Border Commuters

Cross-border commuters are those people who live abroad and work in Switzerland and who commute from home to work and back each day.

The Swiss taxation of such individuals differs, depending on their place of work and domicile (home country/country of residence). The double tax treaty with Germany, for example, provides for an apportionment of the taxation rights between the two countries. The country of work is limited to a flat-rate withholding tax of 4.5% of the gross salary of the cross-border commuter. Such partial taxation of cross-border commuters in the country of work does not relieve the commuter from taxation of the earned income at the place of residence (e.g. taxation with credit). The cross-border commuter status is abandoned if the employee cannot return to his/her domicile abroad on more than 60 working days per year for business reasons. Cantonal agreements vary for cross-border commuters from France.

10.3.5 Lump-Sum Taxation

Both federal and most cantonal tax regulations provide for the possibility to make use of a special tax arrangement often referred to as lump-sum taxation. Under this, qualifying taxpayers resident in Switzerland are taxed on the basis of expenditure and living costs in Switzerland (instead of on the more customary basis of total income and total assets).

Qualifying taxpayers who may apply for lump-sum taxation are individuals who do not have a right to Swiss citizenship who take up temporary or permanent residence in Switzerland for the first time or after an absence of at least ten years and who do not carry out any gainful occupation in Switzerland. The lump-sum taxation provisions are tailored to financially independent persons who are not seeking to work in Switzerland.

In case of spouses moving to Switzerland, the requirements for benefiting from lump-sum taxation must be satisfied by both spouses. As a rule, it is not possible for one spouse to be taxed on a lump-sum basis while the other spouse is taxed on an ordinary basis.

The basis of taxation is calculated annually on the expenses incurred by the taxpayer in Switzerland and abroad. The calculation not only considers the expenses of the taxpayer but also those of the spouse and dependent children as long as they live in Switzerland. Expenses usually taken into account are food, clothing and accommodation, education, leisure activities, and all other expenses linked with the standard of living. The exact calculation is determined together with the relevant tax authorities of the canton in which the person wishes to become a resident. In any case, the measurement base must correspond either with a) at least seven times the rent paid on rental property or the rental value of the taxpayer's property if he lives in his own house or apartment or b) three times the annual costs of lodging if the taxpayer lives in a hotel or similar accommodation. If the taxpayer owns or rents more than one property, the most expensive will be taken into account. A minimum taxable income of 400,000 Swiss francs applies for direct federal tax from January 1, 2016.

Generally, individuals who apply for lump-sum taxation are considered Swiss residents and may also apply for treaty relief on their foreign-source income. Some double taxation treaties, however, allow for treaty benefits only if all income from the source country is subject to ordinary taxation in Switzerland. The abolition of lump-sum taxation continues to be the subject of political debate. Lump-sum taxation remains an option in the following cantons: Aargau, Appenzell Inner Rhodes, Bern, Friborg, Geneva, Glarus, Grisons, Jura, Lucerne, Neuchatel, Nidwalden, Obwalden, St. Gallen, Solothurn, Schwyz, Thurgau, Ticino, Uri, Vaud, Valais, and Zug.

10.3.6 Inheritance and Gift Tax

Inheritance and gift taxes are not harmonized. Consequently, the cantons are free to levy such tax and the various cantonal laws differ considerably in almost every respect. With the exception of the canton of Schwyz, all cantons levy inheritance and/or gift taxes for certain asset transfers if the deceased or donor had been resident of the respective canton or if real estate located in the canton is transferred.

Inheritance and gift tax rates are mostly progressive and are usually based on the degree of relationship between the deceased or donor and the beneficiary and/or the amount received by the beneficiary. In all cantons, spouses are exempt from inheritance and gift taxes; most cantons also exempt direct descendants.

10.4 WITHHOLDING TAX

A federal withholding tax is levied at source on the gross amount of dividend distributions by Swiss companies, on income from bonds and similar indebtedness by Swiss issuers, as well as on certain distributions of income by Swiss investment funds, and interest payments on deposits with Swiss banking establishments.

Since the capital contribution principle came into effect on January 1, 2011, repayments of capital contributions made by the shareholder after December 31, 1996, and declared and accounted for correctly are now treated the same as repayments of nominal capital. This means that repayments of capital contributions declared and identified accordingly are not subject to withholding tax and for individuals (if shares are held as private assets) now no longer represent taxable income (see chapter 10.3.1).

Also subject to withholding tax are profits from gambling, lotteries, and the like, which are not exempt from personal income tax, as well as insurance benefits.

Generally, the debtor is liable for the tax and is required to withhold the amount due, irrespective of whether the recipient is entitled to a full or partial refund. A refund is only possible provided that the respective revenues have been properly declared for the purposes of personal/corporate income taxation and the recipient is entitled to use the revenues subjected to withholding tax. The aim is to prevent tax evasion. For corporate taxpayers, withholding tax is reimbursed by way of a refund, whereas for individuals resident in Switzerland, the tax is credited against total tax liability through the regular taxation procedure.

For non-resident taxpayers, the withholding tax generally represents a final tax burden. However, a partial or total refund may be granted based on an international double tax treaty or a bilateral agreement concluded by Switzerland with the country in which the recipient of the earnings is residing.

It should further be noted that a reporting procedure may be applied for certain qualifying dividend distributions, replacing the withholding and refund procedure.

Thanks to a number of double taxation treaties and bilateral agreements, taxpayers resident outside of Switzerland can be reimbursed for all or part of their withholding tax.

10.4.1 Domestic Rates

The tax rate applied on dividend distributions including deemed profit distributions and interest payments relating to bonds and bond-like debt instruments as well as on interest payments made by banks or bank-like institutions to non-banks is 35%. No withholding tax is levied on interest payments for corporate credit agreements that do not qualify as bonds or bond-like debt instruments. There is no withholding tax on interest payments relating to qualifying ordinary company loan agreements. Provided that royalties, licenses, and service and similar fees payable by Swiss individuals or corporations are at arm’s length, no withholding tax is levied.

10.4.2 Treaty Rates

Most double taxation treaties provide for a reduction of the normal 35% rate on dividends. The reduced rate is usually 15% for portfolio investors and 0%, 5%, or 10% for substantial corporate owners. Some treaties require the taxation of Swiss-source income in the recipient’s country of residence. Otherwise no relief will be granted. With regard to interest income, most treaties allow for a reduction as well, typically up to 10%. In some treaties a full refund is granted.

However, a reduction is only possible if the person applying for treaty benefits is actually entitled to claim the treaty.

10.4.3 Bilateral Agreements with the EU

In May 2004, Switzerland and the European Union (EU) concluded eight bilateral agreements ("Bilateral Agreements II") in addition to the seven existing bilateral agreements ("Bilateral Agreements I," in force since June 1, 2002).

One of the agreements is the Savings Tax Agreement providing for measures equivalent to those laid down in the EU Savings Tax Directive. To entice Switzerland to enter into the Savings Tax Agreement, the same agreement also incorporated language that was practically identical to the version of the EU Parent/Subsidiary Directive and the EU Interest/Royalty Directive in effect at that time.

Accordingly, dividend, royalty, and interest payments between Switzerland and the member states of the EU have not been subject to withholding tax since July 1, 2005, provided conditions such as minimum shareholding and holding period are fulfilled.

As of 2017/18, the Interest Taxation Agreement was replaced by the Agreement for the Automatic Exchange of Information on Tax Matters (AIA Agreement). This not only includes interest returns but all types of capital returns and also trusts and foundations.

The withholding tax exemption of cross-border payments of dividends, interest, and royalties between affiliated companies enshrined in the Savings Tax Agreement will continue to apply.

In general, the bilateral agreements, including the AIA Agreement, also apply to new EU member states joining the EU after July 1, 2005 (e.g. Bulgaria, Romania or Croatia).

The application of the above-mentioned benefits from the AIA Agreement can be denied in cases of abuse or fraud because of the explicit reservation made in the AIA Agreement as to the use of domestic or agreement-based provisions for the prevention of fraud or abuse, both by Switzerland and by the individual EU member states.

Double tax treaties between Switzerland and EU member states with more favorable tax treatment of dividend, interest, and royalty payments remain unaffected. In practice, this means that taxable persons can choose between reference to the AIA Agreement or the applicable double taxation treaty.

10.5 VALUE ADDED TAX

Although Switzerland is not an EU member state, its value-added tax (VAT) system was structured in accordance with the sixth EU VAT Directive ("Sixth Council Directive on the harmonization of the laws of the Member States relating to turnover taxes" whereby turnover refers to revenue) as a non-cumulative, multi-stage tax that provides for deduction of input tax. As a result, Swiss VAT is levied as an indirect tax on most goods and services at the federal level only and applies to each stage of the production and distribution chain. It is designed as a tax owed by the supplier of goods or services (i.e., the tax liability is based on the payment made by the recipient of the goods or services).

10.5.1 Taxable Persons

Any legal entity or individual, establishment, partnership without legal capacity, institution, etc. (i.e. irrespective of legal form, purpose, and intention to make a profit) that operates an enterprise (obtains revenues for a long period of time through independent commercial or professional activity and appearance in one's own name) is essentially liable for tax. There is a VAT registration obligation if global taxable turnover exceeds 100,000 Swiss francs per year. All domestic establishments of a Swiss corporation form one taxable entity together with the headquarters. All domestic establishments of a foreign corporation are also classed as one taxable entity. On the other hand, the domestic establishments and the foreign headquarters are each considered a separate taxable entity.

A so-called acquisition tax obligation (no VAT registration obligation) also exists for recipients within Switzerland who are not liable for taxation, provided that, within the calendar year, they acquire services subject to acquisition tax amounting to a total of more than 10,000 Swiss francs. Such services include those acquired from non-resident enterprises that are not entered in the register of taxable persons, provided that the place of service provision in accordance with the recipient location principle is the domestic market, with the exception of telecommunications or electronic services for recipients not liable to taxation.

Recipients liable for taxation are also subject to the acquisition tax obligation. They must declare acquisition tax within the context of their regular value added tax calculations.

If the revenues of a taxable entity (global turnover from taxable supplies and services) amount to less than 100,000 Swiss francs within the year (for sport and cultural associations and charitable institutions 150,000 Swiss francs), it is exempt from the tax obligation. However, any such entity may also waive exemption from tax liability. Upon registration with the Swiss Federal Tax Administration, the taxpayer receives a VAT number that is essentially based on the company identification number. VAT is added to the company identification number (e.g. CHE123.456.789 VAT).

A special regulation exists for holding companies. In general, the acquisition, holding, and selling of shareholdings is a commercial activity within the meaning of Swiss VAT legislation. Shares of capital in other companies amounting to over 10% are classed as shareholdings, which are held with the intention of long-term investment and have a considerable influence.

Holding companies would generally not be subject to value added tax, as their turnover usually comes from shareholdings and does not therefore fall under taxable supplies. The qualification of the holding activity as a commercial activity means, however, that the holding company can be voluntarily registered for value added tax due to the waiving of the exemption from tax.

The advantage of registration is that input tax claims can be asserted, which accrue within the context of their commercial activity providing an entitlement to input tax deduction. Exempt services for which no tax option is taken or can be taken do not provide an entitlement to input tax deduction (see chapter 10.5.5). In the area of monetary and capital transactions, for example, trading in securities and shares in corporations is a service exempt from taxation, for which an input tax correction is necessary.

10.5.2 Taxable Supplies

Services provided by taxable persons domestically in return for remuneration are subject to domestic tax, provided that they are not exempt or released from taxation. A service that is considered to be provided abroad in accordance with value added tax principles is not subject to domestic taxation. Value added tax is levied on the following types of services:

1. supplies in Switzerland (including other customs areas counting as domestic, e.g. Liechtenstein),
2. provision of services in Switzerland (including other customs areas counting as domestic, e.g. Liechtenstein),
3. services and supplies from non-resident enterprises subject to acquisition tax and
4. import of goods.

Services whose place of performance is abroad, as well as supplies of goods abroad, are not subject to Swiss value added tax. Exports of goods from Switzerland are taxable but are exempt from value added tax. The supply of goods in a value added tax sense is not limited to goods supplies according to Swiss commercial law. The value added tax law provides for a number of transactions which, in the sense of value added taxation, are considered to be supplies, such as the maintenance of machinery, the rental or leasing of property, the sale of electricity, etc.

10.5.3 Taxable Amount

The basis for the calculation of the taxable amount for supplies and the provision of services is the agreed upon or the collected gross remuneration (in cash or in kind). An claim for input tax, i.e. the tax paid on services acquired, can in principle be asserted by the person registered for value added tax in the periodic value added tax calculation and can be deducted from the sales tax owed, provided that the person liable to taxation is entitled to full input tax deduction. Consequently, only the value added is taxed (net all-phase principle).

10.5.4 Tax Rates

Since January 1, 2018, the standard rate has been 7.7% on all taxable supplies of goods or services. A reduced rate of 3.7% is applicable for accommodations. A reduced rate of 2.5% applies on certain categories of goods and services for certain basic needs such as water supply, food and non-alcoholic beverages, cattle, poultry, fish, cereals and grain, books and newspapers, services of non-commercial radio and TV broadcasts, etc.

The Federal Tax Administration offers further simplified VAT accounting for small businesses with turnover of below 5.005 million Swiss francs (incl. VAT) and a tax liability of 103,000 Swiss francs (calculated according to the applicable net tax rate) or less per year. Small businesses may opt to submit VAT based on a balanced tax rate which is lower than the standard rate of 7.7% if they, in return, waive the standard procedure for input VAT accounting, which would otherwise be deducted from the VAT levied on revenue (input VAT deduction). This simplified taxation method must be approved by the Swiss Federal Tax Administration and maintained for at least a tax year. Contrary to the normal case of quarterly billing, a VAT return has to be submitted only twice a year.

10.5.5 Exemptions

The law differentiates between VAT-exempt revenue and revenue excluded from VAT (so-called turnover exempt from taxation and turnover released from taxation). No VAT is levied in either case, but a distinction is made regarding the input VAT deduction.

In cases of exclusions, no input tax deduction is possible for the taxes paid in generating the revenue excluded from VAT. Excluded activities are the healthcare sector, education, culture, sport, social care, most banking and insurance activities, rental and sale of real estate, as well as gambling and lotteries. However, for most of these excluded revenues, it is possible to opt for voluntary taxation. This option is, however, not possible in the case of banking and insurance revenue, as well as the renting and purchase of real estate exclusively for residential use. In contrast to activities excluded from VAT, exempt activities allow for an input VAT deduction for all taxes paid in generating the revenue in question (true exemption). An example of an activity exempt from tax is the export of goods (see also section 10.5.7).

Business activities abroad are not subject to Swiss VAT. These types of revenue are generally the result of international business models. A typical example is a Swiss trading company that buys products from a foreign manufacturing company and sells them to customers in a third country, shipping the products directly to those customers. Activities involving the supply of goods or services abroad only entitle the taxpayer to deduct input tax if the revenue does not qualify as VAT exempt.

10.5.6 Deduction of Input Taxes

An enterprise registered for VAT is liable for VAT on all supplies (sales tax) and will incur VAT on purchases for the business (input tax). In most cases, input taxes may be deducted from the amount of total value added taxes due, and so do not generally represent an additional burden for a business. VAT is a genuine expense only for the end consumer or for a business involved in transactions for which no input tax can be recovered (businesses with excluded income such as banks and insurance companies).

10.5.7 Exports

In addition to exported goods, certain services – if rendered to a recipient domiciled abroad – are also exempt from Swiss VAT (with credit).

However, the Swiss VAT law includes a list of services that are either taxable where the service provider is domiciled or are subject to special provisions according to this list (e.g., services in connection with real estate, hotel and restaurant services; services in relation to culture, sports, and the arts; passenger transport, etc.). Services not included in this list that are provided to a foreign recipient are not subject to Swiss VAT (a catch-all provision – the "place of supply is where the recipient is established" – is applied).

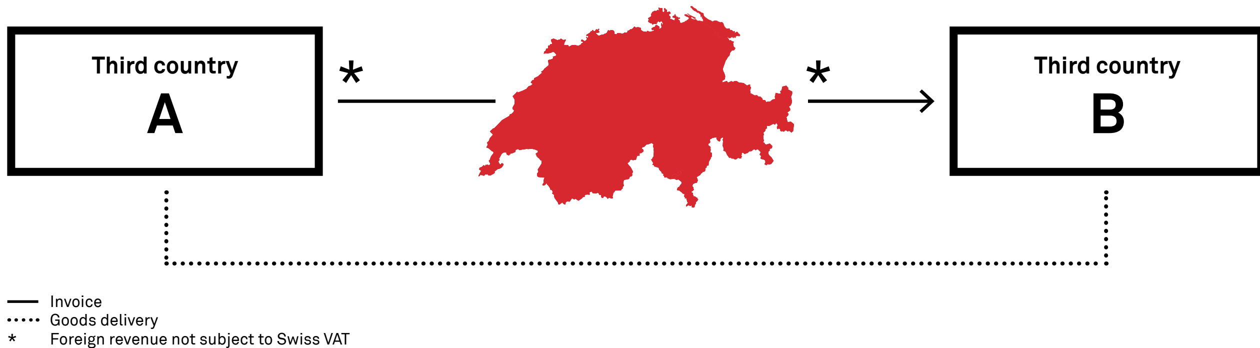
However, the VAT-exempt or non-taxable nature of such services must be proven by the underlying documents such as invoices, agreements, etc. The same applies to export shipments, where a customs export/import certificate is required for tax exemption.

10.5.8 International Business Activity

The basic VAT rules described above have the following effect in the case of a Swiss trading company that buys products from a foreign manufacturing company and sells them to customers in a third country, shipping the products directly to those customers:

International Business Activity

(FIG. 39)



—— Invoice
····· Goods delivery
* Foreign revenue not subject to Swiss VAT

Sources: Illustration by PricewaterhouseCoopers

10.5.9 Non-Resident Enterprises

Foreign businesses supplying goods or certain services to or within Switzerland wishing to waive the exemption from tax liability or with corresponding sales revenues in excess of the threshold stated in chapter 10.5.1 are required to appoint an authorized VAT representative based in Switzerland. Such entrepreneurs may claim input VAT directly. Exempted from compulsory VAT duties are foreign companies that only provide services in Switzerland exempt from tax or recipient-centered services (except telecommunications or electronic services to non-taxable recipients), or deliveries of electricity in pipelines, gas via the natural gas distribution network, and district heating to taxable persons in Switzerland.

Non-resident entrepreneurs without taxable activities in Switzerland are entitled to a refund of Swiss VAT if their foreign activities would qualify as taxable turnover under Swiss VAT law and if the country of residence grants reciprocal treatment to Swiss entrepreneurs (VAT refund).

At 7.7%, Switzerland has the lowest rate of VAT in Europe.

10.6 OTHER TAXES

10.6.1 Stamp Taxes

Generally, the tax liability arises on special legal transactions such as the issuance of shares (issuance stamp tax also known as capital duty) or the trading of securities (securities transfer stamp tax).

The tax on the issuance and the increase of equity of Swiss corporations is 1% on the fair market value of the amount contributed, with an exemption on the first 1 million Swiss francs of the total capital paid in, whether it is made in an initial or subsequent contribution. Amounts contributed without a corresponding increase in the equity of the corporation are likewise subject to tax, and in this case the tax allowance of 1 million Swiss francs does not apply.

The transfer of Swiss and foreign securities in which a Swiss securities dealer participates as a contracting party or as an intermediary is subject to Swiss securities transfer stamp tax (often called "securities turnover tax" whereby turnover refers to revenue). Depending on the issuer's residence (Switzerland or foreign country), the tax rate is 0.15% or 0.3% and is calculated on the consideration of the securities traded.

Swiss securities dealers are defined as any persons professionally engaged in buying or selling securities for their own account or for another person, including Swiss banks and other Swiss bank-like institutions. Furthermore, companies holding taxable securities whose book values exceed 10 million Swiss francs and remote members of a Swiss stock exchange with regard to Swiss titles which are quoted on the Swiss stock exchange are considered Swiss securities dealers.

10.6.2 Real Estate Taxes

Capital gains from immovable property (real estate) in Switzerland are subject to a special cantonal real estate gains tax, provided that the corresponding capital gain is added to the personal assets of an individual. If the capital gain is added to the business assets of an individual or to the assets of a legal entity, it is subject – depending on the canton in which the real estate is located – to normal corporate income tax or likewise to a special cantonal real estate gains tax. On the level of direct federal tax, capital gains from immovable property forming part of the personal assets of an individual are not taxable, whereas capital gains on business assets or on the assets of legal entities are subject to normal corporate income tax.

Furthermore, in some cantons the transfer of real estate is subject to a conveyance tax, whereas on the federal level no taxes of such kind are levied. As a general rule, conveyance tax is assessed on the purchase price or the taxable value of the real estate and is typically paid by the purchaser of the real estate. Depending on the canton, the applicable tax rate varies between 1% and 3%.

Moreover, about half of the cantons levy a special wealth tax on real estate ("real estate tax"). This tax is due every year in addition to the general wealth tax. The tax is levied at the place where the property is situated and is assessed on the market or taxable value of the real estate without allowing for deduction of debts. The applicable tax rate is 0.3%.

10.7 DOUBLE TAX TREATIES

To minimize the effect of double taxation in Switzerland and abroad, Switzerland has concluded tax treaties covering direct income taxes with all major industrial countries and many other countries. Most of these treaties are patterned on the principles of the OECD model convention, which defines where the income or the assets are to be taxed and also describes the method for the elimination of double taxation. Switzerland essentially applies the tax exemption method, exempting income allocable to a foreign country from taxation in Switzerland. The respective income and assets are only considered for the calculation of the applicable tax rate (progression). For certain income streams (dividends, interest, and license fees), Switzerland by contrast generally applies the crediting method. For dividends, interest, and license fees, both states – the state in which the income is earned and the state of the recipient's residence – are typically entitled to tax them. However, the double tax treaty limits the right of taxation of the source state, and the source tax can be credited against the tax levied in the recipient's state of residence. To date, more than 80 tax treaties are in effect, plus also the EU bilateral agreements as of July 1, 2005. As Swiss tax treaties are treated as international conventions, they generally supersede federal as well as cantonal/ municipal tax rules.

Swiss double tax treaties apply to persons (individuals or companies) who are resident in one or both of the contracting states. As already mentioned in chapter 10.3.5, Swiss residents applying for lump-sum taxation generally qualify for treaty relief as well. However, some treaties provide for special conditions to be met in order to benefit from the treaty applied.

Apart from the tax treaties covering direct income taxes, Switzerland also concluded a few tax treaties in the area of inheritance and estate tax. Switzerland has not negotiated any double tax treaties concerning gift taxes so far. Furthermore, there are some special treaties relating to cross-border commuters, taxation of international air and transport services, and the tax situation of international organizations and their staff.

10.8 TRANSFER PRICING RULES

According to Swiss tax law, transactions between group companies must be at arm's length. Switzerland does not have separate transfer pricing legislation and does not plan to introduce such legislation in the near future. Instead, the Swiss tax authorities follow the transfer pricing guidelines of the OECD to determine if a transaction between related parties is at arm's length. In Switzerland, no specific documentation requirements for transfer pricing purposes must be observed. A company doing business in Switzerland should however have the appropriate documentation on file verifying the arm's-length nature of transactions with related parties.

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