The Inward Investment and International Taxation Review

Thirteenth Edition

Editor
Charles C Hwang

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THE INWARD INVESTMENT AND INTERNATIONAL TAXATION REVIEW

THIRTEENTH EDITION

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Charles C Hwang

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PREFACE

I am pleased to bring to you the 13th edition of *The Inward Investment and International Tax Review*. This annual publication provides tax summaries for investment into 23 countries around the globe. While intended to provide readers with accurate and up-to-date analysis on the main tax considerations of investing in each of the jurisdictions covered, this publication is not a substitute for tax advice tailored to your unique circumstances.

From the onset of the covid-19 pandemic, governments around the world used their respective tax laws to help support their economies and raise the funds needed to provide this support. These support initiatives have ranged from robust government-backed loan programmes and individual stimulus payments to postponed tax deadlines and deferred tax payments. Some governments have largely ended these initiatives and now look to replenish their coffers or avoid further deficits, whether by increasing tax rates, increasing enforcement activities, or enacting altogether new taxes. Other governments continue to implement tax reduction policies to mitigate the negative impacts of the pandemic. For example, the Chinese government implemented a VAT credit refund, which will lead to an estimated 1.5 trillion yuan in total tax refunds, to improve businesses' cash flows. The Chinese government also implemented a 100 per cent super deduction for corporate basic research investments to promote corporate R&D. (By contrast, because of legislative inaction, the parallel US deduction for research expired and was replaced by a five-year amortisation rule (15 years for certain foreign research) effective for tax years beginning after 31 December 2021.)

Other themes were present before but have been brought to the forefront by the pandemic – namely remote work and global tax reform. Advances in technology continue to enable workers to perform their duties from anywhere in the world. Many of these workers do not realise the tax ramifications of remote work for themselves and their employers, and governments are stepping up their enforcement efforts. As for tax reform, the OECD continued making progress on its Two-Pillar Solution during 2022, but significant work still remains. The digitisation of the global economy continues, and until a global consensus is achieved on the OECD's Pillar 1, countries continue to pursue digital services taxes as a unilateral measure to protect their respective tax bases.

In 2022, the OECD made significant progress with its Pillar 2 15 per cent minimum tax project. In early 2022, the OECD released the commentary for the model rules for the 15 per cent tax. In February 2023, the OECD released administrative guidance related to the model rules. The effective tax rate in each jurisdiction in which a multinational group operates would be compared to the 15 per cent standard. To the extent that the 15 per cent minimum tax is not paid, a top-up tax equal to the shortfall would be paid to the jurisdiction of the ultimate parent of a multinational group that is within the scope of these rules. Each jurisdiction could choose to enact its own top-up tax. If such top-up tax conforms to the model rules, that tax would be creditable against the 15 per cent minimum tax assessed against the parent.

The United States has taken, to date at least, a different path from the OECD framework. The Inflation Reduction Act of 2022 was signed into law by the President on 16 August 2022. This Act provides for a number of tax credits and other policies aimed at bolstering energy and environmental policies as well as fostering investment in the United States. Prior to the Inflation Reduction Act of 2022, the United States had a minimum tax regime in the form of the base erosion and anti-abuse tax (BEAT). The Inflation Reduction Act introduced a second corporate minimum tax for large, publicly traded taxpayers. This new minimum tax is based on book income and is calculated as 15 per cent of adjusted financial statement income. Unfortunately, neither BEAT nor the new minimum tax on book income conforms to the OECD framework. Some of the United States' trading partners have also portrayed the tax credits enacted by this US legislation as being protectionist in effect.

The EU has enacted a new regime that extends the rules governing aid from EU governments (known as state aid) to non-EU governments as well. In June 2022, the European Parliament approved the Foreign Subsidy Regulation, which would require multinationals making an acquisition or forming a joint venture in the EU, or bidding on a government contract from a member of the EU, to disclose financial contributions from non-EU governments in certain circumstances. Tax benefits are included in the definition of financial contributions, though the mechanics of identifying and computing tax benefits are as yet unclear.

Governments also continue to enhance transparency in the beneficial ownership of private business entities and crack down on illicit finance. For example, beginning on 1 January 2024, new entities formed under US law, as well as foreign legal entities that register to do business with a state government or Native American tribe, will be required to register with the Financial Crimes Enforcement Network (FinCEN) (a bureau of the US Treasury Department with responsibility for enforcing US laws on money laundering, terrorist financing and other financial crimes). This registration will disclose all beneficial owners who directly or indirectly own or control 25 per cent or more of the equity of the entity or have substantial control over the entity. While there are a number of exemptions, such as for public companies and large operating entities, many expect the new beneficial ownership reporting rules to have a substantial effect on investment into the United States. Entities formed before 1 January 2024 will have until 1 January 2025 to also register. The database containing the information collected by FinCEN under these regulations is intended to be used only by law enforcement.

These are just a sample of the many developments that are discussed in the summaries that follow. I hope you find this updated guide helpful in following the current trends in taxation and the inward investment environment.

The views expressed in this book are those of the authors and not of their firms, the editor or the publishers. Every effort has been made to ensure that the contents of this edition were current as of the date of publication.

Charles C Hwang
Washington, DC
February 2023

Chapter 20

SWITZERLAND

Fabian Sutter and Beat Baumgartner[1]

I INTRODUCTION

Switzerland is a federal republic consisting of 26 cantons. The federal government, cantons and communes are entitled to levy taxes and therefore corporate income and personal income taxes are levied on all three levels.

Switzerland is a liberal and open society with a strong focus on a business-friendly legislation and environment. It avails of very limited restrictions on foreign investments, notably on Swiss residential property.

The overall tax burden (tax-to-GDP) is comparatively low and below the Organisation for Economic Co-operation and Development (OECD) average. The availability of direct democratic instruments (e.g., popular votes on specific legislative proposals) makes Switzerland a very stable and predictable economic environment. Tax authorities aim at close collaboration with the taxpayer, by way of open communication and advance tax rulings, to ensure legal certainty and reduce administrative costs and tax litigation.

International tax developments, however, required Switzerland to amend its tax landscape as recently implemented by way of the Swiss corporate tax reform bill as of 1 January 2020 and are continuing to impact Switzerland by way of the OECD GloBE Pillar 2 proposal (Pillar 2).

II COMMON FORMS OF BUSINESS ORGANISATION AND THEIR TAX TREATMENT

i Corporate

Typical corporate structures include the forms of companies limited by shares (Ltd) and limited liability companies (LLC). Outside of a US multinational context the company limited by shares is the most frequently used legal form.

The minimum nominal share capital requirements for a company limited by shares is 100,000 Swiss francs and for the LLC 20,000 Swiss francs. At least one individual resident in Switzerland needs to be able to sign on behalf of the company (e.g., single signature authority or joint signature authority with another Swiss resident). This individual does, however, not need to be a member of the board.

1 Fabian Sutter and Beat Baumgartner are partners at Loyens & Loeff Switzerland LLC.

Corporate entities are viewed as having legal personality and are treated as separate taxpayers. As such they are subject to corporate income and annual capital tax (net wealth tax for corporations) as well as withholding tax, stamp tax and value added tax (VAT) (all as applicable).

ii Non-corporate

Typical non-corporate entities include the ordinary partnership as well as forms of the limited partnership.

Partnerships are treated as transparent for tax purposes and income and assets being directly allocated to the partners. The same tax treatment notably applies to the majority of collective investment vehicles (CIVs) such as the contractual fund, the investment company with variable capital, investment company with fixed capital and limited partnership for collective investments. The sole exception is real estate funds (i.e., funds with direct ownership in real estate).

Unlike regular partnerships, CIVs are, however, subject to dividend withholding tax.

III DIRECT TAXATION OF BUSINESSES

i Tax on profits

Determination of taxable profit

The taxable profit is determined based on the statutory stand-alone Swiss generally accepted accounting principles (GAAP) financial statements. Switzerland generally taxes worldwide income with exclusion of assets and income pertaining to a foreign permanent establishment (PE), foreign business enterprise and foreign real estate (unilateral exemption).

In principle, Swiss GAAP accounts recognise income on an accrual basis and expenses (including tax expenses) are tax deductible to the extent they are commercially justified. Tax authorities may conduct tax adjustments if the accounting treatment violates Swiss GAAP or if a specific tax provision allows for a correction (e.g., differing rates of amortisation under GAAP and tax law, exclusion of certain items from deduction for tax purposes such as fines).

For related-party transactions, tax adjustments can be made if a transaction is not made on arm's-length terms. The difference between the actual consideration and the arm's-length price will be considered a deemed dividend for tax purposes, triggering an upward adjustment for corporate income tax and will additionally be subject to 35 per cent dividend withholding tax (reduction under treaty may apply).

Capital and income

As a general rule, income and capital profits are subject to corporate income tax. Switzerland applies a participation reduction system (indirect exemption) for income from dividends and capital gains stemming from qualifying participations.

For dividends: qualifying participation means a participation of at least 10 per cent in the share capital or profits in a subsidiary or a participation with a fair market value of at least 1 million Swiss francs. For capital gains: qualifying participation means that the Swiss company sells a participation of at least 10 per cent, which has been held for at least 12 months.

The participation reduction system reduces corporate income tax in the amount of net participation income to total taxable profit. To the extent that this results in a reduction of 100 per cent, other income (e.g., licence fees, interest income) will equally be exempt from taxation.

Participation reduction does not apply on hybrid payments (tax deductible dividends on the source state), on partnerships or if the distributing company qualifies as a CIV.

Cantons may levy a real estate capital gains tax on profit resulting from the sale of property located in the canton. Currently, nine cantons levy a separate real estate capital gains tax. In the remaining cantons and on federal level, capital gains on real property are taxed with the regular corporate income tax.

Losses

Tax losses can be carried forward for seven years (first in/first out). There is no tax loss carry-back system.

In the event of financial restructuring (e.g., negative equity), losses may be carried forward for more than seven years if utilised to recapitalise the company.

Losses are linked to the taxpayer and in principle cannot be utilised by another taxpayer. There is no group loss relief. However, losses may be transferred in intra-group reorganisations (e.g., mergers, demergers). Tax authorities may deny loss transfer under the abuse of law doctrine (anti-avoidance rules).

Rates

The statutory corporate income tax rate on federal level is 8.50 per cent. Cantonal income tax rates vary depending on the canton.

Average effective corporate income tax in Switzerland ranges between 14 and 16 per cent (e.g., canton of Zug, 11.85 per cent; canton of Basel-Stadt, 13.04 per cent; canton of Vaud, 14 per cent; canton of Geneva, 14 per cent; canton of Zurich, 19.7 per cent (18.2 per cent expected as of 2024) – all in capital cities of the respective canton; federal and cantonal income tax combined).

Annual capital tax rates (only levied on cantonal level) range between 0.001 per cent and 0.50 per cent on total equity.

It is expected that cantons will levy a qualified domestic minimum top-up tax of up to 15 per cent pursuant to the OECD Pillar 2 proposal as of 1 January 2024 for Swiss tax resident constituent entities that are in the scope of Pillar 2. Switzerland will hold a public referendum vote to introduce Pillar 2 rules on 18 June 2023.

Administration

Corporate income tax and annual capital tax are levied by the cantons. This includes the federal income tax, which is also levied by the cantons and partially remitted to the federal government.

The Swiss federal tax administration is tasked with levying Swiss withholding tax, stamp taxes, VAT and a radio and TV levy.

For corporate income and annual capital tax purposes, corporate taxpayers file annual tax returns in the year following the respective business year. The due date of the return varies depending on the canton. Federal corporate income tax is generally due on the 31 March of the following year. The due date for cantonal corporate income tax varies for each canton. Taxpayers are required to present the relevant facts and circumstances; the tax authorities determine the applicable legal provisions. Cantonal tax authorities issue tax assessments after reviewing the corporate income tax returns annually. Tax assessments can be challenged with two cantonal courts and in most cases with the federal supreme court.

For withholding tax, stamp tax and VAT purposes, taxpayers are subject to a self-assessment tax procedure (i.e., they are fully responsible to duly declare, file and pay any tax owed to the federal government). The Swiss federal tax administration does not issue tax assessments (except for VAT purposes). Taxes levied by the Swiss federal tax administration can be challenged with the federal administrative court as well as with the federal supreme court.

Both cantonal and federal tax authorities may conduct tax audits. They are legally required to notify the other authority if they encounter irregularities that would likely also lead to a tax adjustment by the other authority.

Switzerland has a strong advance tax ruling practice. Taxpayers may request confirmations from the competent tax authority about the tax consequences of a specific transaction. It is market standard to obtain advance tax rulings for any complex dealing, typically from multiple authorities and for multiple applicable taxes. Once confirmed, the tax authority is legally bound by the confirmation and cannot conduct a differing tax assessment even if the tax ruling confirmation would be incorrect.

Tax grouping

Switzerland does not apply a tax consolidation regime (except VAT grouping). Swiss tax law follows a strict separate-entity approach.[2]

ii Other relevant taxes

Annual capital tax

The cantons levy an annual tax on the equity of a corporate taxpayer (i.e., nominal share capital, share premium and capital as well as profit reserves). Tax rates among cantons range from 0.001 per cent and 0.50 per cent.

Most cantons allow for specific reductions from the tax basis for qualifying participations (i.e., participations of at least 10 per cent), patents subject to the patent box regime, goodwill subject to a step-up in basis as well as intra-group loans. Some cantons also allow for a full or partial tax credit of corporate income tax against capital tax (e.g., cantons of Geneva and Vaud). Debt that is recharacterised as equity under thin capitalisation rules is also subject to annual capital tax.

Note on salary withholding taxes

Personal income taxes are typically assessed based on the annual individual income tax return and paid directly by the individual taxpayer. Switzerland only applies a salary withholding tax on payments made by a Swiss employer to (1) a non-resident performing work in Switzerland and (2) Swiss tax resident employees who are neither Swiss citizens (or married to a Swiss citizen) nor avail of a regular residence permit (C permit).

Similarly, to the extent that there is no Swiss employer, a foreign employer is in principle not required to register for salary withholding tax in Switzerland for Swiss employees, but the employees will be required to file a regular annual tax return.

2 For loss transfer, see Section III.i, 'Losses'.

Dividend withholding tax

Switzerland levies a 35 per cent dividend withholding tax on actual and deemed dividends. The tax has to be deducted by the Swiss payor and remitted to the Swiss federal tax administration. For Swiss tax resident beneficiaries, the withholding tax is fully refunded if the beneficiary declares the respective income in the tax return. For non-Swiss tax resident beneficiaries, the tax can be fully or partially refunded or reduced based on an applicable double tax treaty.

Interest withholding tax

Switzerland levies a 35 per cent interest withholding tax on certain debt instruments qualifying as 'bonds' for Swiss tax purposes. A 'bond' means any debt instrument issued by a Swiss tax resident entity if: (1) a debt instrument is issued to more than 10 non-bank lenders in a single transaction under identical or similar terms and in an amount exceeding 500,000 Swiss francs; or (2) debt instruments are issued in total to more than 20 non-bank lenders on variable terms and in an amount exceeding 500,000 Swiss francs; or (3) issued to more than 100 non-bank lenders exceeding 5 million Swiss francs (Swiss 10/20/100 non-bank lender rules).

Issuance stamp tax

Switzerland levies a 1 per cent stamp tax on equity contributions made by the direct shareholder. For increase in nominal share capital, an exemption up to 1 million Swiss francs applies. Contributions to reserves against no consideration (no issuance of shares) are in any event subject to 1 per cent stamp tax. Exemptions apply notably to corporate reorganisations such as contributions of shares.

Securities transfer stamp tax

Switzerland levies a securities transfer stamp tax of up to 0.3 per cent on the transfer of taxable securities (shares, bonds etc.) if a Swiss securities dealer is a party or intermediary to the transaction and no exemption applies. The definition of Swiss securities dealer includes any Swiss resident bank, securities dealer or intermediary as well as any Swiss resident legal entity holding taxable securities in the amount of at least 10 million Swiss francs in its Swiss GAAP accounts.

VAT

Switzerland levies a 7.7 per cent VAT on the transfer of goods and provision of services (regular rate). A reduced rate of 2.5 per cent applies on essential goods and a special rate of 3.7 per cent applies to the provision of accommodation.

Radio and TV levy

Switzerland also levies a general radio and TV levy also applicable to businesses regardless of whether radio or TV offerings are consumed if such business has a global turnover of at least 500,000 Swiss francs and is subject to Swiss VAT.

The levy is dependent on the turnover of the business, with the maximum levy being 49,925 Swiss francs.

OECD Pillar 2: top-up taxation

On 18 June 2023, Switzerland will hold a public referendum vote to introduce rules aligned with the OECD Pillar 2 proposal, which will introduce a 15 per cent minimum tax (as qualifying domestic minimum top-up tax or IIR).

IV TAX RESIDENCE AND FISCAL DOMICILE

i Corporate residence

A corporate taxpayer becomes resident for tax purposes under domestic law if it either has its (1) statutory seat or (2) place of effective management in Switzerland. For resident taxpayers, corporate income tax is in principle levied on worldwide income.

Tax residency for place of effective management is typically assessed based on where day-to-day operations and central management are conducted. Purely administrative activities as well as the meetings of the board of directors are not viewed as decisive factors.

Under most of Switzerland's double tax treaties, the residency tiebreaker is the place of effective management. Some treaties have been revised to include the OECD multilateral instrument (MLI) standard for residency requiring a mutual agreement procedure (e.g., treaty with Mexico).

ii Branch or permanent establishment

A non-resident corporate taxpayer will be subject to limited tax liability in Switzerland if it avails of (1) a permanent establishment or place of business or (2) real property in Switzerland.

The definition of a permanent establishment is largely in line with the international tax standard definition ('fixed place of business through which the business of an enterprise is wholly or partly carried on').

Switzerland has not applied the new MLI or OECD MC 2017 definition of permanent establishment in new treaties and has currently no tax policy goal to do so.

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

i Holding company regimes

The holding company regime was abolished effective as of 1 January 2020. However, holding companies benefit from the Swiss participation reduction system both at the federal and cantonal level, and can also apply a special reduction for annual capital tax purposes in most cantons.

Holding activities are further viewed as entrepreneurial activity and therefore entitled to a full input VAT deduction.

ii IP regimes

Cantons offer a patent box regime that is fully in line with the OECD's nexus approach. The tax relief applies to up to 90 per cent of qualifying income with an uplift on qualifying expenditure of 30 per cent. The amount of the relief varies depending on the canton. Typically, cantons with a low regular effective tax rate apply a low patent box deduction as the overall rate is already low. In any event, any deduction introduced by the Swiss corporate tax reform is subject to a base erosion limitation of 70 per cent of taxable income (i.e., 30 per cent of taxable income will be imposed as minimum tax basis).

Separately, patents qualifying for the patent box may also lead to a special reduction for annual capital tax purposes.

iii State aid

Switzerland (both at federal and cantonal level) offers tax holidays if certain requirements are met.

On a federal level, only specific regions of Switzerland may offer a tax holiday for federal income tax purposes that are linked to job creation and preservation. Tax holidays are capped at 95,000 Swiss francs per job created and 47,500 Swiss francs per job maintained, and can be granted for a maximum duration of 10 years.

On a cantonal level, all cantons may grant tax holidays for a duration of up to 10 years. The cantonal tax holidays are not restricted to certain areas or regions and are independent from federal income tax (e.g., the canton may also grant a tax holiday even if no tax holiday is or can be granted at the federal level and cantons my limit holidays to certain types of taxes, for example, capital tax instead of corporate income tax). Cantonal requirements for tax holidays are linked to the investment amount and jobs created in the process. To the extent that the requirements are not fulfilled for the entire duration of the tax holiday, cantons may recapture tax amounts.

iv General

Switzerland provides for internationally rather low corporate income tax rates, a very stable political environment and an independent economic policy that is not automatically linked (e.g., with EU Member States).

Swiss tax authorities generally approach taxpayers with a client mentality and are very approachable for new investments. Switzerland avails of a broad tax treaty and bilateral investment treaty (BIT) network and is in the process of abolishing many tax hurdles for foreign investments (e.g., abolishing of stamp taxes and interest withholding taxes).

VI WITHHOLDING AND TAXATION OF NON-LOCAL SOURCE INCOME STREAMS

i Withholding outward-bound payments (domestic law)

Switzerland levies a 35 per cent withholding tax on federal level on dividends distributed by Swiss tax resident legal entities, on certain interest payments on debt instruments issued for collective financing as well as on distributions of Swiss collective investment vehicles.

Dividend withholding tax applies on any distribution of a Swiss company including distribution of share premium (to the extent not qualifying for a domestic law exemption, see below), liquidation proceeds and deemed dividends (non-arm's-length transactions between related parties). Most double tax treaties reduce the withholding tax rate to zero per cent (for intra-group dividends) or 15 per cent in all other cases. Switzerland, however, only applies an exemption at source (notification procedure) for intra-group dividends.

In principle, Switzerland does not levy a general interest withholding tax except on certain debt instruments issued for collective investments (bonds, debentures). A bond or debenture for Swiss tax purposes exists if (1) a Swiss entity issues debt to more than 10 non-bank lenders at identical terms (within the same transaction) in excess of 500,000 Swiss francs (10 non-bank lender rule); (2) a Swiss entity issues debt to more than 20 non-bank lenders in total on variable terms in excess of 500,000 Swiss francs (20 non-bank-lender rule); or (3) a Swiss entity issues debt to more than 100 non-bank lenders in excess of 5 million Swiss francs (100 non-bank lender rule). Most double tax treaties will provide for a zero per cent rate for treaty lenders. Switzerland does, however, not apply an exemption at source and requires lenders to request a refund of 35 per cent withholding tax. The interest withholding tax can typically be avoided if structured properly.

Switzerland does not levy withholding taxes on royalties or services performed.

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

Swiss tax resident beneficiaries (individual or corporate investor) will receive a full refund of Swiss withholding tax provided the respective income is duly declared in the individual income tax return or recognised as income in the respective Swiss GAAP accounts.

Non-Swiss tax resident beneficiaries may claim a full or partial refund or reduction under an applicable double tax treaty. Intra-group dividends may benefit from an exemption at source provided all requirements pursuant to the treaty are fulfilled (i.e., holding period and thresholds).

Repayment of nominal share capital and qualifying capital reserves are exempt from Swiss withholding tax regardless of the tax position of the beneficiary. Qualifying capital reserves (share premium) are exempt from Swiss dividend withholding tax provided that such amounts have been contributed by the direct shareholder and have been approved by the Swiss federal tax administration by filing of Form 170.

iii Double tax treaties

Switzerland has an extensive treaty and BIT network with over 90 countries being covered. This notably includes all European jurisdictions, the United States, Canada, Russia, China, certain countries in the Middle East, and several countries in South and Central America (e.g., Brazil).

The Swiss federal tax administration applies substance requirements in order for foreign corporate shareholders to be eligible to treaty benefits and apply the reduced or zero per cent rate for intra-group dividends.

To benefit from the reduced Swiss dividend withholding tax rate, the direct parent entity needs to meet the following substantive conditions as per the practice of the Swiss federal tax administration:

a fulfil the standard conditions of the treaty (residence, minimum participation quota, minimum holding period (if applicable), beneficial ownership); and

b avail of sufficient substance for tax purposes consisting of:
- financial substance;
- physical substance and staff; and
- functional substance.

The substance requirements are subject to a facts and circumstances test (i.e., no check-the-box test) but cover the following items.

a Financial substance: equity ratio of at least 30 per cent, i.e., continuously financed with at least 30 per cent equity on a stand-alone (non-consolidated) basis (pursuant to local statutory GAAP accounts, based on book values, calculated on the basis of total assets).

b Physical substance and staff: availability of actual infrastructure and qualified staff, including, but not limited to, local directors with professional knowledge required to perform their duties, key decision making made in this jurisdiction, undertaking of day-to-day management, link of the wider group to respective jurisdiction (e.g., other group companies in this state with sufficient substance), non-tax reasons for using a company in this state (i.e., real business reasons), employees on the payroll (strong indication of local substance), own office infrastructure (i.e., own office space or offices space provided by third-party service provider). Pure reliance on corporate service provider is considered as a weak position and will require additional substance requirements to be fulfilled.

c Functional substance: function as regional or international holding company holding several investments in other operating entities and which are substantial in nature compared with the Swiss investment.

If direct parent entity belongs to a multinational enterprise (MNE) and is directly or indirectly held by an operating company in a treaty jurisdiction, mere financial substance is typically accepted.

If the direct parent entity does not belong to a MNE but, for example, to a high-net-worth individual or private equity structure, the Swiss federal tax administration generally checks for financial substance and personal substance (e.g., infrastructure of family offices, investment platforms, staff and relevant decisions making for private equity structures).

Entities in an offshore jurisdiction with which Switzerland does not have a double tax treaty (e.g., Cayman Islands, British Virgin Islands, Jersey, Monaco) or an ultimate beneficial owner that is not entitled to treaty benefits (e.g., Monaco, UK non-domiciled status) may disqualify the direct parent from accessing the treaty benefits because of treaty shopping concerns.

Please find below an overview of the most relevant tax treaties.

Country	**Dividends**				**Interest (%)**	**Royalties (%)**
	Regular treaty rate (residual) (%)	**Intra-group dividends (%)**	**Investment threshold (%)**	**Holding period (y) (%)**		
European Union (AEOI Agreement)*	–	0	25	2	0	0
Canada	15	5	10	–	10	10
China	15	5	25	–	10	9
Brazil	15	10	10	1	10 / 15	15 / 10
Germany	15	0	10	1	0	0
France	15	0	10	–	0	5
Luxembourg	15	0 (5 in the first 2Y)	10	2	0	0
Netherlands	15	0	10	–	0	0
Russia	15	5	20	–	0	0
United Kingdom	15	0	10	–	0	0
United States	15	5	10	–	0	0

* AEOI Agreement = Agreement between the Swiss Confederation and the European Union on Automatic Exchange of Information.

iv Taxation on receipt

Switzerland generally applies the exemption method to eliminate double taxation under treaties. Ordinary tax credits apply to non-refundable withholding tax on dividends, interest and royalties (i.e., subject to tax test) if Switzerland has a double tax treaty with the source state.

VII TAXATION OF FUNDING STRUCTURES

i Thin capitalisation

Switzerland applies an asset-based ratio test to determine the maximum permissible debt for related-party debt (e.g., maximum debt for cash is 100 per cent, for receivables 85 per cent, participations 70 per cent, etc.). The sum of all maximum permissible debt per asset class determines the maximum permissible debt for a taxpayer.

Related-party debt exceeding the maximum permissible debt is (1) added to the annual capital tax basis and interest paid on such debt; (2) not deductible for corporate income tax purposes; and (3) subject to 35 per cent withholding tax (deemed dividend).

Switzerland does not apply an earnings before interest, taxes, depreciation and amortisation test as applied in most European countries.

ii Deduction of finance costs

Interest expenses incurred from independent third parties are generally tax deductible.

Interest expenses incurred from related parties are tax deductible provided the respective interest rates are at arm's-length. The Swiss federal tax administration publishes annual minimum and maximum safe harbor interest rates for related party loans denominated in Swiss francs and certain foreign currencies (e.g., US$, euros, £, etc.). Taxpayers may deviate from safe harbour rates provided that they can substantiate a lower (for minimum interest rates) or higher (for maximum interest rates) interest rate on related party loans.

Switzerland prevents finance cost deduction in certain cases based on abuse of law doctrine (e.g., debt push-down in leveraged acquisitions and certain intra-group reorganisations).

iii Restrictions on payments

Swiss corporate law prohibits the distribution of interims dividends (i.e., dividends paid out of profit of the current financial year). Dividends can only be paid out of retained earnings. The upcoming revised corporate law will explicitly allow for the distribution of interim dividends and is expected to enter into force in 2023.

Further, for intra-group dividends, Swiss auditors accept the distribution of dividends up a chain of controlled entities based on the in-phase dividend recognition mechanism (i.e., recognition of dividend income received from a subsidiary in the financial statements of the previous financial year as a transitory item to allow for an immediate distribution up the chain of controlled entities). The in-phase dividend recognition mechanism, however, strictly requires recognition as a transitory item in the financial statements of the parent entity to avoid 35 per cent dividend withholding tax being levied.

iv Return of capital

From a legal perspective, nominal share capital can be repaid applying a formal procedure for capital reduction (triggering notably a six-month waiting period). Share premium can be distributed as a regular dividend in the same manner as profit.

As outlined above, nominal share capital and qualifying capital reserves can be repaid without Swiss withholding tax.

The granting of up- or cross-stream loans to related parties may block distributable equity in the amount of the loan if the respective loan is non-arm's-length. Swiss auditors may therefore refuse to permit a dividend distribution in excess of the amount of such non-arm's-length up- or cross-stream loan.

VIII ACQUISITION STRUCTURES, RESTRUCTURING AND EXIT CHARGES

i Acquisition

Swiss or foreign acquisition vehicle

Acquisitions in Switzerland can be structured either through a domestic or foreign acquisition vehicle.

For acquisitions structured through a foreign acquisition vehicle, investors should ensure that the foreign entity is entitled to double tax treaty benefits, notably to a zero per cent rate on outbound dividends.

For a Swiss acquisition vehicle, previous structures relied on specific funding structures relying on funds that are out of scope or exempt from Swiss dividend withholding tax (e.g., debt, qualifying capital reserves or nominal share capital). However, as a result of the increased scrutiny of the Swiss federal tax administration on (alleged) abusive tax structuring, Swiss acquisition vehicles in principle only work if the outbound shareholder structure also benefits from double tax treaty benefits. Otherwise, the structure risks being viewed as abusive and the Swiss federal tax administration might levy 35 per cent withholding tax on distributions of the target to the Swiss acquisitions vehicle under its current doctrine on 'international transposition'. While the Swiss federal tax administration tends to grant a refund of Swiss withholding tax up to an amount of the residual withholding tax of the previous shareholding structure, recent case law appears to indicate that there should in any event be a 35 per cent non-refundable tax, provided that a specific structure is viewed as abusive.

With respect to the acquisition of a Swiss target, the Swiss federal tax administration applies an anti-avoidance rule for withholding tax purposes if the acquisition leads to an improved withholding tax refund position for the purchaser (e.g., if the seller would not be entitled to a full or partial refund of Swiss withholding tax, the purchaser would inherit such potential withholding tax risk (tainted reserves or old reserves doctrine)). Originally designed for intra-group reorganisations and classic treaty shopping structures, the Swiss supreme court recently confirmed that this doctrine may also be applied in a third-party sale. Purchasers may seek to counter the doctrine by implementing a purchase price adjustment. This practice in certain cases can make it less attractive for foreign investors to choose a Swiss acquisition vehicle as the outbound structure would in any event need to benefit from double tax treaty entitlement.

Share vs asset deal

Acquisitions in Switzerland can be structured either as an asset or as a share deal. Asset deals will trigger corporate income tax on any built-in gains or goodwill and (in certain cases) VAT but allow the purchaser to benefit from a stepped-up basis.

Share deals are typically preferred if the seller is a Swiss tax resident individual because of the possibility to achieve a tax-free capital gain for individual income tax purposes. Share deals may also trigger securities transfer stamp tax of 0.15 per cent (for Swiss target shares) if a Swiss securities dealer is a party or intermediary to the transaction. The stamp tax is typically either fully borne by the purchaser or shared 50:50.

If the seller is a Swiss tax resident individual holding shares as a private asset for tax purposes, the seller may achieve a tax-free capital gain. However, the tax-free capital gain can be re-characterised as a taxable dividend under the 'indirect partial liquidation doctrine', which will also impose some restrictions on the purchaser.

The indirect partial liquidation requires that (1) a Swiss tax-resident individual sells shares of at least 20 per cent (also taking into account acting in concert) to (2) a purchaser either qualifying as a company or an individual holding the shares as business assets and (3) within five years after the sale target distributes excess cash (funds not required for business operations) that was available at the time of the sale to the purchaser (4) to the extent such excess cash or funds could have been distributed as a result of sufficient freely distributable equity at the level of the target. This rule will require the purchaser to accept an indemnity in the share purchase agreement covering the seller for any such future distribution and therefore restricts the purchaser's ability to extract cash from the target. However, in practice there are various options available to the purchaser to achieve a similar outcome (e.g., distribution of funds of the ongoing financial year, etc.).

Funding

Acquisitions can be structured either by debt or equity. Outside of thin capitalisation rules, debt and equity instruments are strictly qualified based on their Swiss GAAP accounting treatment. Perpetual or profit participating loans will therefore still qualify as debt.

Switzerland levies a 1 per cent stamp tax on equity contributions. The stamp tax can be avoided by way of indirect contributions (i.e., contributions made by an indirect shareholder).

Debt instruments by shareholders or related parties are subject to transfer pricing rules (i.e., interest rates must be at arm's length to be tax deductible and not be viewed as deemed dividends subject to withholding tax).

For Swiss acquisition vehicles, as shares should be financed with at least 30 per cent equity, the 70:30 debt-to-equity ratio is rather common. However, to the extent that shareholder debt is provided as an interest-free loan, a breach of thin capitalisation rules technically has very limited impact and is also often used if the extraction of interest is not the primary goal.

Foreign acquisition vehicles should be financed with at least 30 per cent equity to be entitled to treaty benefits due to the Swiss federal tax administration substance requirements.

Financing costs are generally tax deductible. A debt push-down transaction structured as a merger of the acquisition vehicle with target will be viewed as abusive and interest deduction will be denied. However, in practice there are several tested structures to achieve a debt push-down.

ii Reorganisation

Switzerland allows tax neutral intra-group reorganisations such as mergers, demergers, spin-offs and intra-group transfers provided that the transaction occurs at the current tax book value and assets remain subject to tax in Switzerland.

Certain limitations apply notably to demergers, where Swiss tax practice requires that both the transferring as well as the receiving entity maintain a 'business unit' for tax purposes (i.e., the demerger of non-operational business or assets would not be tax neutral). Separately, intra-group transfers are limited to business or operational assets as well as participations of at least 10 per cent or 20 per cent (as applicable) to achieve tax neutrality.

The Swiss federal tax administration is expected to issue a revised practice circular on intra-group reorganisations applicable as of 1 January 2022. Although the new guidance will not entail material changes to current practice, some reorganisation structures may require additional or different steps in the future to achieve tax neutrality.

iii Exit

Switzerland levies exit tax in the event of a liquidation, winding-down or transfer of assets abroad on built-in gains and goodwill (if any) for corporate income tax purposes, and on the distributable profit reserves and unrealised reserves for withholding tax purposes.

The transfer of functions assembled workforce and similar intra-group asset transfers have to be at arm's length. Switzerland generally follows the OECD transfer pricing guidelines, including the chapter on intra-group reorganisations.

IX ANTI-AVOIDANCE AND OTHER RELEVANT LEGISLATION

i General anti-avoidance

Switzerland applies general anti-avoidance rules (GAAR) under the abuse of law doctrine both under domestic law and with respect to treaty law.

Swiss case law tests abuse of law under three general requirements that are assessed based on all facts and circumstances of a case: (1) a specific tax structure is inappropriate or artificial (objective criterion); (2) the structure was implemented with the intention to avoid taxes (subjective criterion); and (3) the structure would indeed lead to a substantial tax saving if accepted by the authorities.

The GAAR rules are applied regardless of whether a domestic law or a double tax treaty contains a specific reference to anti-avoidance rules. Swiss case law has confirmed that the GAAR is inherent to both domestic and treaty law.

ii Controlled foreign corporations

Switzerland does not apply controlled foreign corporations rules. Swiss tax authorities may, however, challenge low substance or offshore structures with PE or place of effective management rules.

iii Transfer pricing

Swiss tax law contains very limited references to transfer pricing. However, the Swiss federal tax administration as well as all cantonal tax authorities adhere to the OECD transfer pricing guidelines.

Swiss domestic law also does not explicitly require transfer pricing documentation. Neither master nor local files are required under Swiss law. However, as taxpayers need to be in a position to substantiate applied transfer pricing it is common to maintain transfer pricing documentation, including transfer pricing policies and benchmarks to the extent necessary.

The Swiss federal tax administration has implemented a transfer pricing unit that can be approached, for example, for advance tax ruling confirmations, thus providing legal certainty for material intra-group dealings. Mutual agreement procedures and bilateral advance pricing agreements are handled by the Swiss state secretariat for international finance matters.

iv Tax clearances and rulings

Swiss tax authorities have a long-standing practice of issuing advance tax rulings to confirm the tax analysis for a specific transaction or fact pattern prior to its implementation. It is therefore very common for taxpayers to approach the tax authorities for these requests. Tax litigation is therefore also less frequent.

Tax authorities typically issue rulings within two to four months after receipt of the request, although timing may vary among cantons (with Swiss German-speaking cantons typically issuing replies significantly quicker). Tax authorities do not levy fees or charges for issuing rulings.

Under the OECD base erosion and profit shifting project, Switzerland also committed to spontaneous exchange on tax rulings for certain cross-border tax rulings (i.e., rulings on preferential tax regimes, cross-border transfer pricing rulings, unilateral downward adjustment rulings and tax residency or PE rulings).

X YEAR IN REVIEW

The year 2022 saw an increase in corporate reorganisations both in inbound and exit scenarios as well as an increased focus on transfer pricing matters. For instance, during tax audits or information requests, transfer pricing documentation is a regular item requested from tax payers, and experience indicates that taxpayers are well advised to prepare such documentation in advance. Typically, transfer pricing challenges pertain to financial transactions and the justification of arm's-length margins (e.g., for trading operations).

During popular votes, both the abolishing of the 1 per cent issuance stamp tax and the abolishing of the 35 per cent interest withholding tax was rejected, and these taxes continue to apply. However, owing to already existing practice and exemptions, the rejected votes have a limited impact on existing business operations.

Finally, in view of the upcoming OECD Pillar 2 proposal, MNE groups started to review existing structures and tax positions to avoid double taxation, which may occur under Pillar 2 if not properly implemented. Separately, the Swiss tax system provides for specific features that require a thorough analysis under Pillar 2. These notably include the participation reduction system (indirect reduction) as well as tax neutral step-up in basis (e.g., if no deferred tax asset has been recognised in the past or if a deferred tax asset is recognised in connection with a harmful transaction under the transitional rules).

XI OUTLOOK AND CONCLUSION

We expect that 2023 will entail a significant increase in reviews as a result of Pillar 2 as well as further inbound transactions as almost all business locations will levy a 15 per cent minimum tax as of 2024. Switzerland may benefit from these developments as it will be in compliance with Pillar 2 but not levy a tax in excess of the minimum tax.

Appendix 1

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