Deloitte.

International Tax

Switzerland Tax Alert

23 September 2014

Draft legislation on Corporate Tax Reform III published

Contacts

Reto Savoia
rsavoia@deloitte.ch

Jacqueline Hess
jahess@deloitte.ch

Jacques Kistler
jkistler@deloitte.ch

Ferdinando Mercuri
fmercuri@deloitte.ch

Rene Zulauf
rzulauf@deloitte.ch

Diego Weder
diweder@deloitte.com

On 22 September 2014, the Swiss federal government published draft legislation on the Corporate Tax Reform III, the most comprehensive corporate tax reform in more than 50 years. The main objective of the reform, which likely will become effective on 1 January 2019, is to enhance Switzerland’s attractiveness as a location for multinational companies.

Many Swiss companies would benefit from lower taxation under the reform. The proposed measures generally would ensure that companies that currently benefit from a lower tax rate under one of the special tax regimes that would be abolished (see below) effectively could retain their beneficial tax rate for up to 10 years following the reform. Assuming the reform takes effect in 2019, the current tax rate for these companies essentially would be guaranteed up to 2029, i.e. for a period of 14 years, which would offer considerable certainty for affected companies.

The reform would phase out all special corporate tax regimes, such as the mixed, domiciliary, holding and principal company regimes, as well as the Swiss finance branch regime, likely as from 1 January 2019.

A number of measures are included in the Corporate Tax Reform III to compensate for the elimination of the beneficial tax regimes. The main measures that would improve the attractiveness of Switzerland as a location include the following:

- Introduction of a patent box that would apply to all income arising from the exploitation and use of patents;
- Introduction of a notional interest deduction on equity;
- Allowing a step-up (including self-created goodwill) for direct federal and cantonal/communal tax purposes upon the migration of a company to Switzerland;
- Allowing a step-up (including self-created goodwill) for cantonal/communal tax purposes for companies transitioning out of tax privileged cantonal tax regimes (such as mixed or holding companies) into ordinary taxation;
- Reduction of the general tax rates (i.e. the cantonal/communal corporate tax rates) at the discretion of the individual cantons;

- Abolition of the 1% capital issuance tax on equity contributions;
- Transition from an indirect to a direct participation exemption regime on dividends and capital gains to avoid tax leakage, with no minimum threshold and no minimum holding period requirement;
- Extension of the seven-year loss carryforward period to an indefinite period, with 20% of the profit as the minimum tax base;
- Allowing parent companies to assume losses from Swiss and foreign subsidiaries that cannot be used at the subsidiary level; and
- Reduction of the cantonal/communal annual net wealth tax for holding participations, group loans or intellectual property, at the discretion of the individual cantons.

Revenue-raising measures

The main revenue-raising measure would be the introduction of a capital gains tax for individuals on the disposal of shares and other securities, under which capital losses would be available for indefinite carryforward. Only 70% of capital gains on sales of shares and dividends from shares would be taxed, with no minimum ownership threshold. Capital gains tax for individuals also would apply in cases where an individual exits (i.e. migrates from) Switzerland.

Measures to attract companies to Switzerland

Patent box: A broad patent box regime would be introduced that would encompass income that is embedded in the sales price of a product, provided the Swiss company substantially contributed to the development of a patent related to the product (e.g. through a control function in the case of contract R&D). Qualifying patent income would be calculated based on a residual method, i.e. all income of a company would be considered patent income that is not specifically deducted as nonpatent income (nonpatent income would include financing income and income attributable to routine functions). The cantons would be able to exempt up to 80% of the patent income from taxation for cantonal/communal tax purposes, which generally would result in an effective tax rate of between 8% and 10% on qualifying patent income, taking into account the expected general rate reductions for the cantons. (The rate could be even lower taking into account the potential notional interest deduction on equity.) The patent box may be further refined once the recommendations of the OECD are published.

Notional interest deduction on equity: A notional interest deduction would be granted on surplus equity, which would be defined for each asset class. While most companies likely would benefit from the regime, it is designed generally to favor financing companies. The notional interest deduction rate would be equal to the 10-year Swiss government bond rate, plus 50 basis points, but would be no less than 2% (for example, if a Swiss finance company provides loans at a 2% interest rate and the corporate tax rate is 12%, the effective tax rate would be 1.8%).

Step up: A step-up would be allowed for direct federal and cantonal/communal tax purposes (including on self-created goodwill) for companies migrating to Switzerland and companies transitioning out of any of the tax privileged regimes (such as mixed companies). The step-up could be amortized for tax purposes on a straight-line basis over a maximum period of 10 years. The rationale for the step-up is that Switzerland would not tax any increase in value that did occur outside the

Swiss taxing jurisdiction, either because the company was abroad or because the income was partly or fully exempt under a former privileged Swiss tax regime. The step-up essentially would grandfather the existing tax rates available under privileged tax regimes so they would continue to apply for a period of up to 10 years after the reform becomes effective.

Reduction of corporate tax rates: Many cantons would reduce their headline corporate tax rates that currently range from approximately 12% to 24% (combined federal/cantonal/communal rate). While the cantons of Lucerne and Schwyz (certain areas) already are at approximately 12%, Zug, for instance, has announced plans to reduce its rate to approximately 12%, Geneva to approximately 13% and Vaud to approximately 14%, to just to name a few of the planned reductions.

Comments

The draft legislation will be subject to an extensive consultation process where interested parties, such as political parties and the business community, can comment on the legislation and suggest changes. The consultation period will last through 31 January 2015; the government is expected to submit formal legislation to the parliament in June 2015, so that the parliament still would be able to pass the legislation during 2015. There also may be a referendum and a national vote on the legislation.

Cantonal tax laws subsequently would have to be amended to reflect the changes, so the most likely date for the law to become effective would be 1 January 2019.