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Introduction to Swiss Tax Law

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Fiscal Sovereignty in Switzerland: 3 Levels of Taxation

- Confederation

  Authority in all areas in which it is empowered by the Federal Constitution → the Confederation must only levy taxes to which it is authorised by the Federal Constitution

- Cantons (26 Cantons)

  Authority in all areas that are not reserved to the Confederation → the cantons are authorised to levy any type of tax as long as they do not infringe upon the exclusive authority of the Confederation or upon the Federal Constitution and Federal Law

- Municipalities (approx. 2'255 Municipalities)

  Authority in all areas that are entrusted to them by the Canton → the municipalities must only levy taxes within the bounds of the authority delegated to them by the respective cantonal law

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Principal Taxes on the Federal Level

Taxes on income

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

Taxes on goods and services

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

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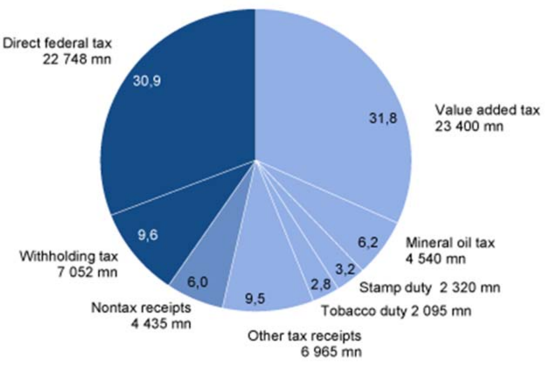
Federal Revenue: 2019 Ordinary Receipts (Budget)



Source: https://www.efv.admin.ch/efv/en/home/finanzberichterstattung/bundeshaushalt_ueb/einnahmen.html

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Principal Taxes on the Cantonal or/and Municipal Level

Taxes on income and on net wealth

All cantons

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

Not all cantons

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

Taxes on goods and services

Not all cantons

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

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Principal International Agreements

- **Double Taxation Treaties**

  Wide net of double taxation treaties concluded by Switzerland (approx. 90 treaties on income taxes, some of them including net wealth taxes, 8 treaties on inheritance taxes)

- **Bilateral Agreements with the European Union, from a tax perspective in particular of relevance**
  - ➢ Agreement on free movement of persons
  - ➢ Agreement on Automatic Exchange of Information, in force since 1 January 2018 (replaced former agreement on taxation of savings income)
- **Multilateral Convention on Mutual Administrative Assistance in Tax Matters (in force as of January 1, 2018)**
- **Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS** (signed on 7 June 2017, not yet in force, approval by the Parliament and ratification expected end of 2018 / beginning of 2019; see: https://www.admin.ch/gov/de/start/dokumentation/medienmitteilungen.msg-id-71891.html)

Most relevant Federal Tax Acts

- Federal Act on the Federal Direct Tax (FDTA) of December 14, 1990 (Bundesgesetz über die direkte Bundessteuer [DBG], SR 642.11)
  - ➢ Individual income tax
  - ➢ Corporate net-profit tax
- Federal Act on the Harmonisation of Direct Taxes of Cantons and Municipalities (FTHA) of December 14, 1990 (Bundesgesetz über die Harmonisierung der direkten Steuern der Kantone und Gemeinden [StHG], SR 642.14)
  - ➢ Federal guidelines on the cantonal taxes on income and net-wealth, net-profit and capital as well as on real estate capital gains
- Federal Withholding [Anticipatory] Tax Act (WHAT) of October 13, 1965 (Bundesgesetz über die Verrechnungssteuer [VStG], SR 642.21)
- Federal Value Added Tax Act (VATA) of June 12, 2009 (Bundesgesetz über die Mehrwertsteuer [MWStG], SR 641.20)

Constitutional Principles of Taxation (I)

Art. 127 Federal Constitution

1 The general principles of taxation, particularly the circle of taxpayers, and the object of the tax and its calculation, shall be established by statute

2 To the extent that the nature of the tax allows it, the principles of universality and equality of tax treatment and of taxation according to economic capacity shall be followed

3 Inter-cantonal double taxation is prohibited. The Confederation shall take the necessary measures

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Constitutional Principles of Taxation (II)

- Principle of universality
  - Prohibition of a privileged treatment of certain taxpayers or group of taxpayers
  - Prohibition of discrimination and of more burdensome taxation of certain taxpayers or group of taxpayers
- Principle of equality and ability-to-pay principle
  - Each taxpayer must contribute to the fiscal revenue of the state according to his/her economic and personal resources
  - Horizontal equality: taxpayers who are in the same economic and personal situations and derive the same amount of taxable income must be taxed identically
  - Vertical equality: taxpayers who are in different economic and personal situations and derive a different amount of taxable income must be taxed differently

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Constitutional Principles of Taxation (III)

- Ability-to-pay principle: Examples of ongoing discussions in Switzerland (I)
  - Equal treatment of married couples and cohabiting couples
    - Married couples are taxed together (family taxation; article 9 and 36 FDTA); cohabiting partners are taxed separately (single taxation), because of the progressive income tax rate married couples who live in the same economic and personal situation than cohabiting couples may pay more income taxes (calculations show that approx. 350’000 married couples are actually concerned)
    - Equal treatment is not yet solved with regard to the federal income tax
    - Different solutions are discussed in Swiss parliament to solve that inequality

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Constitutional Principles of Taxation (IV)

- Ability-to-pay principle: Examples of ongoing discussions in Switzerland (II)
  - Exemption of capital gains on private assets from the taxable income tax base: article 16 (3) FDTA
  - Lump-sum taxation of non Swiss citizen who do not work in Switzerland: article 14 FDTA
  - Reduction of the double tax burden on dividend distributions; partial dividend taxation: article 18b and 20 (1bis) FDTA

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Prohibition of Intercantonal Double Taxation (I)

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

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Prohibition of Intercantonal Double Taxation (II)

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

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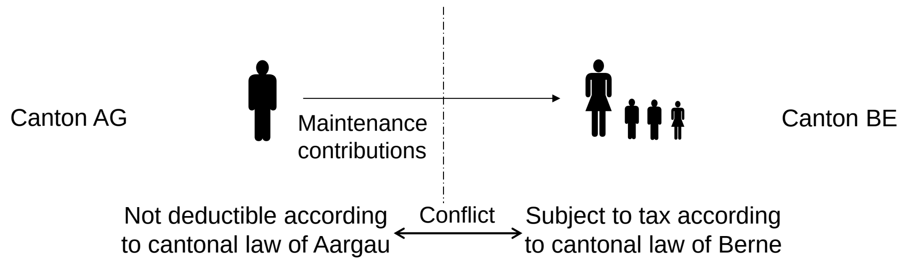
Prohibition of Inter-cantonal Double Taxation - Example: Federal Supreme Court of 4 Dec. 1992, ATF 118a I 277

Divorced couple, payment of maintenance contributions from one canton to another



The Federal Supreme Court ruled that the Canton Aargau must deduct the maintenance contributions and the Canton Bern is allowed to tax them

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Harmonisation of Direct Taxes (I)

Art. 129 Federal Constitution

1 The Confederation shall establish principles on the harmonisation of direct taxes of the Confederation, the Cantons and the Municipalities; it shall take into account the efforts of the Cantons to harmonise their taxes.

2 The harmonisation shall concern tax liability, tax object, taxation period, and procedural and criminal law on taxation. Harmonisation shall not cover tax scales, tax rates, and tax-exempt amounts

3 The Confederation may issue regulations against arrangements granting unjustified tax advantages

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Harmonisation of Direct Taxes (II)

1 January 2001:
Federal Tax Harmonisation Act (FTHA) took effect

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

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

Coordination based on the FTHA

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

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Harmonisation of Direct Taxes (III)

No harmonisation of tax allowances and tax rates → the tax rates of the cantons and municipalities differ considerably

Example 1: Assumption: single person, taxable income CHF 100'000 (Option 1) or CHF 300'000 (Option 2); tax year 2018

Taxable income	CHF 100'000	CHF 300'000
Federal income tax: (maximum tax rate: 11.5 %)	2.87 %	8.92 %
Cantonal income tax (incl. municipal income tax)		
• Wollerau (Canton Schwyz)	8.14 %	10.26 %
• Hergiswil (Canton Nidwalden)	10.34 %	11.37 %
• Zurich (City of Zurich)	13.81 %	21.49 %
• Berne (City of Berne)	20.89 %	25.64 %

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Harmonisation of Direct Taxes (IV)

Example 2: Assumption: Company with a taxable profit of CHF 1'000'000; statutory tax rates 2018

Federal corporate tax	8.5 %
Cantonal corporate tax (incl. municipal and parish tax)	
• Lucerne	5.5 %
• Zug	8.2 %
• Zurich	18.3 %
• Berne	18.8 %

It should be noted that the effective tax rates are lower than the statutory tax rates since Swiss corporate tax law allows the deduction of paid taxes (effective tax rate federal corporate tax minus approx. 1 %, effective tax rates cantonal corporate tax minus approx. 2 - 4% depending on the individual situation)

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Federal Income Tax

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

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

Federal Individual Income Tax (I)

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

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

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Federal Individual Income Tax (II)

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

- Taxpayers with **economic** attachment → non-residents
→ **limited** tax liability («source principle») (art. 4 and 5 FDTA)
  - real estate in Switzerland
  - permanent establishment in Switzerland
  - gainful activity without temporary abode
  - board members or directors of Swiss corporations
  - pensions and similar remunerations paid by Swiss institutions/insurance
- Taxation of the Swiss source income
- Ordinary tax assessment or source tax, e.g. salary source tax for any dependent work in Switzerland or for sportspersons and artists

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Federal Individual Income Tax (III)

Taxable income

Principle of taxation of the overall income (no baskets, no schedules), including:

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

Exceptions

- capital gains on movable and immovable assets if not realised on business assets, e.g. realised on private assets (art. 16 (3) FDTA)
- Inheritance and gifts (= subject of cantonal gift and inheritance tax); some kind of insurances payments; financial aids for low-income people (art. 24 FDTA)

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Federal Individual Income Tax (IV)

Deductible Expenses and Allowances

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

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Federal Individual Income Tax (V)

Deductible Expenses: Example work-related expenses (Art. 26 FDTA)

Peter lives in Berne and works in Zurich. He commutes by train from Berne to Zurich. He is a young attorney-at-law and decides to attend evening courses in English in order to improve his chances to work for an international law firm.

Peter may deduct from his taxable income:

- Train costs (effective costs up to an amount of CHF 3’000 per year)
- Costs of taking lunch out of home (lump-sum amount of CHF 15 per day, total per year CHF 3’200): costs for meals are deductible if it is not reasonable for the taxpayer to go home for lunch
- Costs of the language course as costs of further education: educational costs are deductible if they are directly connected to the current profession of the taxpayer

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Federal Corporate Income Tax (I)

Types of legal entities – Two categories

- Corporations: Share Company (AG/SA), Limited Liability Company (GmbH/Sarl), Cooperative Society
- Other legal entities: Association, foundation and other legal entities that are treated as legal entities, e.g. investment trusts with direct real estate ownership
- Not partnerships: in Switzerland, partnerships are not considered legal entities; their income is attributed to the partners (transparent taxation)

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Federal Corporate Income Tax (II)

Subjects to the Federal Corporate Tax – Two Categories of taxpayers

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

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Tax Proposal 17: Planned Tax Law Amendments

- Switzerland has to abolish several criticised tax regimes (e.g. regimes for holding, administrative and mixed companies, finance branches)
- Switzerland will introduce other measures that are in line with EU law and the OECD project on Base Erosion and Profit Shifting (BEPS)
- Tax proposal 17 = new proposal, following the Corporate Tax Reform III that was abolished by the Swiss people in February 2018, most amendments only concern the cantonal corporate taxes:
  - Introduction of a patent box
  - Introduction of tax incentives for research and development expenses
  - Introduction of a notional interest deduction on equity capital (only for certain cantons)
  - Rules regarding the disclosure of built-in gains
  - General reduction of cantonal ordinary corporate income tax rates for all companies to a competitive level
  - Combination of the Tax Proposal 17 with a proposal for additional financing of the social security system

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Cantonal Corporate Tax – Special tax regimes (to be abolished)

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

- **Holding companies:** companies whose purpose is mainly the holding and administration of participations and which refrain from exercising a business activity in Switzerland are (after fulfilment of some additional quantitative requirements) exempted from the cantonal corporate income tax.
- **Domicile companies** (Administrative company or mixed company): companies which exercise only administrative and/or auxiliary activities in Switzerland are taxed on the profits made abroad only at a rate of 0%-25%, depending upon the importance of the activities in Switzerland.

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Withholding (Anticipatory) Tax (I)

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

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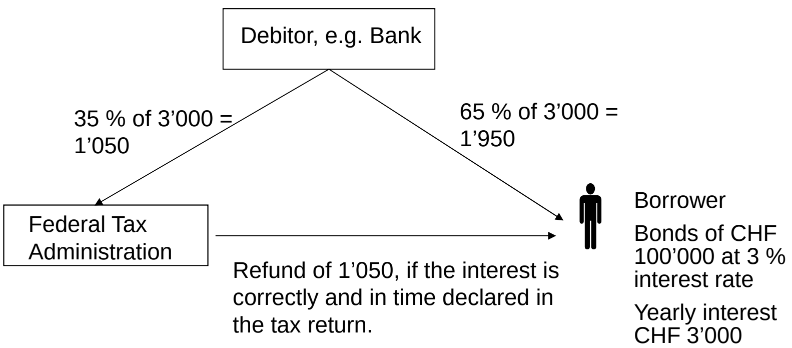
Withholding (Anticipatory) Tax (II)

Concept of the Swiss Withholding Tax on Dividends and Interests



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Stamp Tax

- Legal basis: Stamp Tax Act of June 27, 1973 (Bundesgesetz über die Stempelabgaben [StG], SR 641.10)
- Three kind of stamp taxes
  - ➢ Stamp tax on the issuance of shares in Swiss corporations
  - ➢ Stamp tax on the transfer of domestic and foreign securities
  - ➢ Stamp tax on insurance premiums
- Tax rate on the issuance of shares: 1 %
- Tax rate on the transfer of securities: 0.3%
- Tax exemption in the case of reorganization, e.g. spin-offs, mergers, change of the legal structure, etc.

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Value Added Tax (VAT)

- Legal basis: Value Added Tax Act of June 12, 2009 (Bundesgesetz über die Mehrwertsteuer [MWStG], SR 641.20)
- Consumption tax mainly following the principles of the EU directive on VAT levied on all phases of production and distribution as well as on the import of goods, domestic service industry and the import of services from abroad
- Tax rates 2018
  - ➢ Standard tax rate 7.7%
  - ➢ Reduced tax rate on certain categories of goods, e.g. food, medicine, books 2.5 %
  - ➢ Special reduced tax rate for hotel and lodging industry 3.7 %
  - ➢ On-going parliamentary discussion: simplification of the VAT, e.g. only two tax rates instead of three, abolishment of certain exemptions

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Inheritance and Gift Tax (Cantons)

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

