burckhardt

Attorneys • Civil Law Notaries • Certified Tax Experts

Introduction to the Swiss tax system

burckhardt

Attorneys Civil L

Certified Tax

focused

pragmatic

personal service

Law Notaries
ax Experts

Better known for its fine cheeses and Swiss watches, Switzerland is also one of the best places to choose to establish your growing business. Whether an operating, trading, finance, or holding company, your business can benefit from one of the most generous tax jurisdictions in the world that is competitive to offshore rates, but located in the heart of Europe. Switzerland is one of most politically and economically stable countries and, in addition to tax incentives, offers businesses a stable and educated professional work force, an unobtrusive legal environment, and world-class banking services.

We provide our clients and their businesses with comprehensive, tailored advice on national and international tax planning issues. We support our clients with professional expertise and broad international experience on structuring, restructurings, mergers, and joint ventures, and advise on inbound and outbound investments (in particular Switzerland/USA). We also advise professional practices and service firms about their global structure.

Contact information tax and corporate
Rolf Wüthrich
Mühlenberg 7 • PO Box 258 • CH-4010 Basel • Switzerland
Phone +41 61 204 01 00 • Fax +41 61 204 01 09
wuethrich@burckhardtlaw.com

www.burckhardtlaw.com

Introduction

Switzerland offers many competitive benefits for production companies, holding companies, and group and captive companies, including:

- Tax holidays
- Lower the average group tax rate
- Comprehensive Swiss tax treaty network
- Friendly atmosphere between tax administration and tax payers
- Reliable tax ruling practice
- Excellent infrastructure and services offered
- Geographical location of Switzerland in the middle of Europe and its transport possibilities (airports, trains, highways, Rhine ships)
- Political and monetary stability
- Bilateral agreements with the European Union
- Liberal labor law and social freedom
- Well educated labor

Swiss tax system

- Two levels of taxation in Switzerland:
  - Federal corporate income tax (8.5%), and
  - Cantonal corporate income taxes (about 25%)
- Average total corporate income tax rate of ordinary taxed company: 25% (after deduction of taxes due from taxable income)
- Classical system of double taxation (taxation of profits on corporate level as well as on shareholder level)
- Withholding tax of 35% on dividend distributions, unless withholding tax rate is reduced under a tax treaty
- No withholding tax on intercompany interest payments and royalty payments
- No withholding tax on repayment of contributed capital
- No withholding tax on profits remitted by a branch to its foreign head office
- For effective tax burden the choice of the residence canton is decisive

Corporate entities

- Stock company (AG; not eligible to „check the box" for US tax purposes)
- Limited liability company (GmbH; eligible to „check the box" for US tax purposes)

Participation exemption for dividend income

- Dividend income is (nearly) tax exempt from corporate income tax under the participation exemption if:
  - the shareholder owns at least 10% of the capital in the dividend distributing subsidiary; or
  - the value of the shares in the dividend distributing subsidiary exceeds CHF 1 million.
- Capital gains realized on the sale of shares also qualify for the participation exemption

International aspects

- About 110 tax treaties concluded by Switzerland
- Savings agreement between Switzerland and the European Union, which provides for zero withholding tax rate on intercompany dividend, interest and royalty payments
- Method to avoid/mitigate double taxation under tax treaties:
  - Dividends, interest and royalties: Switzerland grants a foreign tax credit
  - All other income: Switzerland exempts such other income from Swiss taxation
- Treaty Switzerland / USA reduces 35% withholding tax to 5% for dividend distributions to qualifying corporations

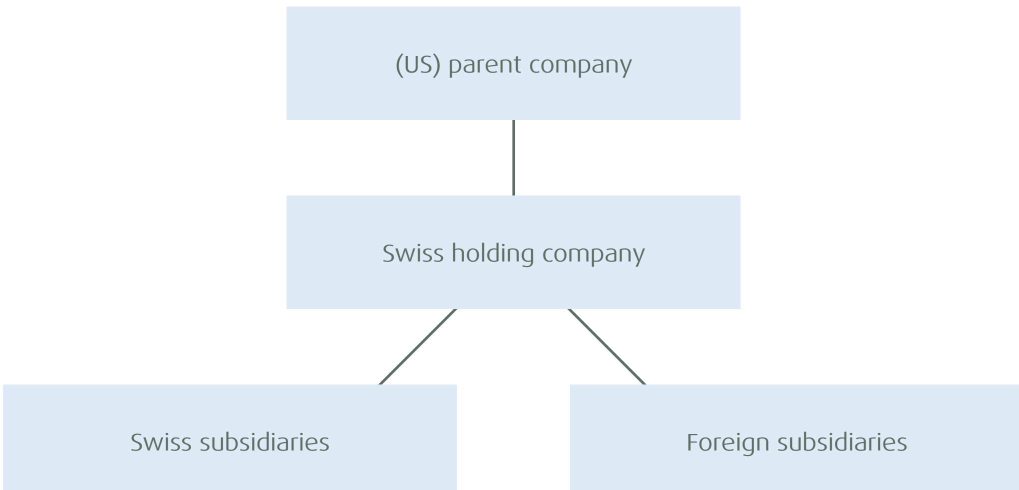
Swiss anti-abuse measures

- No Controlled Foreign Corporation (CFC) legislation
- Swiss anti-abuse measures
  - Measures against illegal and improper use of tax treaties
  - Legal basis: Federal decree on measures against the improper use of tax treaties concluded by the Swiss Confederation of December 14, 1962
  - Federal circular of explanation of December 31, 1962
  - Federal circular of explanation of December 17, 1998, including the modifications of December 2001
  - Decree as Swiss domestic law applies to every Swiss taxpayer taking advantage of a tax treaty
  - If no tax treaty is applied no anti-abuse measures do apply
  - Examples of treaty abuse in the decree:
    1 Abusive transfer of income to non-qualifying persons conduit companies
    2 Inappropriate profit distributions 25% distribution rule
    3 Fiduciary relationships
    4 Foreign-controlled family foundations or partnerships
  - Consequence of anti abuse measures: treaty application is refused

Swiss tax structures

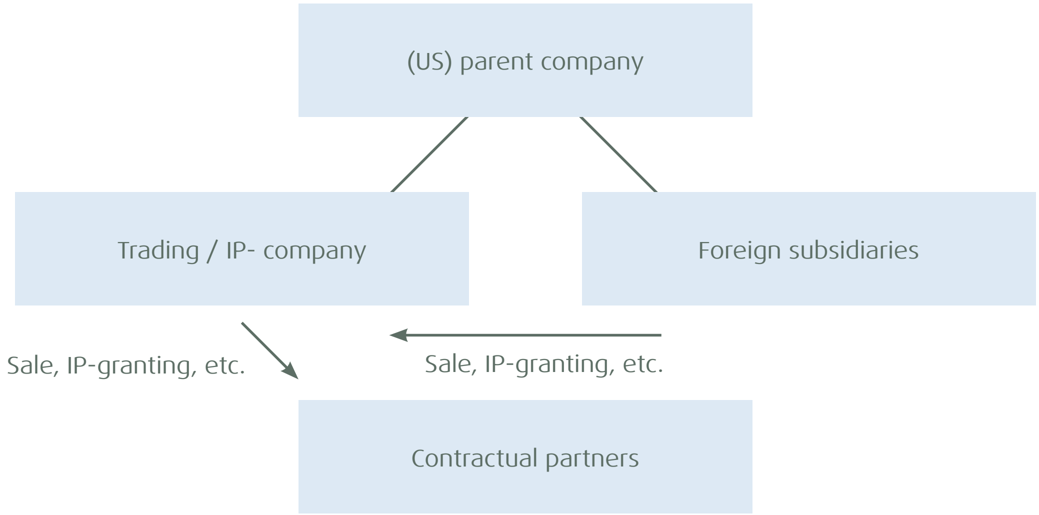
Holding companies

- Tax treatment:
  - exempt from corporate income tax on cantonal level;
  - reduced cantonal capital tax
  - subject to federal corporate income tax, but dividend income is exempt under the participation exemption
  - average tax burden: 0.01% to 1%
- Use of Swiss holding company:
  - as foreign holding company for investments in Europe



Trading and service companies

- Tax treatment:
  - Federal tax: ordinary corporate income tax of 8.5%;
  - Cantonal tax:
    1. Dividend income is exempt
    2. Income from Swiss sources is taxed at ordinary rates (rate about 25%)
    3. Income from foreign sources is partially exempt (between 85% and 100% of the foreign sourced income is exempt from cantonal taxes); remaining income is taxed at ordinary rate
  - Reduced cantonal capital tax
  - Average total tax burden: 8% to 12%
- Requirement: at least 80% of the income (and expenses) must steam from non-Swiss sources
- Used as:
  - Trading company
  - Invoicing company
  - Service company
  - Group captive company
  - Intangible property company
  - Financing company



Principal structure

- Tax treatment:
  - Federal tax: Corporate income tax rate of about 4.25% (trading principle) or 6% (production principle)
  - Principal companies normally qualify also for the cantonal trading company status or a principal status for cantonal tax purposes
  - Reduced cantonal capital tax
  - Average total tax burden: 5% to 7%
- Use of Swiss principal company:
  - As centralized trading company

Swiss tax holidays

- Available in all cantons for cantonal tax purposes:
  - Up to 10 years
  - Tax holidays are granted up to 100% at the beginning and gradually decrease
- Available for federal tax purposes in certain areas of Switzerland only
- Granted to enterprises that are in the economic interests of an area:
  - Creation of new jobs
  - Technological development
  - Opening of new markets
  - Production of new goods or production of goods that are complementary to existing products

Swiss finance branch

- Swiss permanent establishment with bank-like activity
- Tax effect:
  - Foreign head office in exemption country: excludes foreign branch income from taxation
  - Based on domestic legislation Swiss finance branch is allowed to make a deemed interest deduction for its bank-like activity
    Result: Non-taxation of deemed interest amount
- Requirements:
  1. The branch's assets amount to at least CHF 100 millions
  2. Branch activity: primarily a financing activity
     - 3/4 of its gross profit must be derived from financing activities and
     - 3/4 of its assets must be invested in financing activities
       Financing activities = any activities generating interest or any activities aimed at reducing exchange risks or bad debts
     - granting of loans
     - cash management as well as the management of debtors and creditors for the subsidiaries
     - factoring, leasing, netting and re-invoicing
     - centralization of the foreign currency rate management within a group

     Gross profit from non-financing activities (e.g. dividends, selling or manufacturing) cannot exceed 1/4 of the total gross profit of the branch and the assets allocated to these operations cannot exceed 1/4 of the total branch assets
  3. Loans or advances granted by Swiss branch to Swiss subsidiaries may not exceed 10% of the branch's assets
- Deemed interest deduction in % of commercial profit:
  - 82.644628%
  - If average balance sheet total exceeds CHF 1 bio.: 86.580086%
  - Interest effectively paid by branch reduces deemed interest deduction accordingly

burckhardt Ltd

Mühlenberg 7
PO Box 258
CH-4010 Basel
Switzerland

Tel. +41 61 204 01 01
Fax +41 61 204 01 09

info@burckhardtlaw.com
www.burckhardtlaw.com