

## **SWISS COMPANIES... WHY NOT?**

There are many different ways of structuring your business operations in Switzerland which can help optimize your company's tax situation.

In addition, the specific location may entitle your company to significant tax reduction incentives.

On a cantonal and municipal level, as well as for direct federal tax, legal entities, as a rule, having either their registered office or their effective administration in Switzerland, are subject to tax on an unlimited basis. Profit tax is levied at all three levels: federal, cantonal and municipal, while only cantons and municipalities levy a tax on paid-in capital (registered capital or share capital) and reserves. The tax rate imposed on companies in Switzerland depends on the type of legal entity and the company's purpose and activity. There is much more variation in the tax treatment of Swiss companies, which are most often either corporations or limited liability companies. Furthermore, the main activity (core business) of the company is the most important factor which the taxation depends on. The Swiss tax system outlines various types of entities for tax purposes. The main fiscal regimes are:



- the ordinary company, the holding company, the mixed holding company,
- the auxiliary (base) company,
- the principal company,
- the service company (cost-plus company),
- The finance branch.

Branches may also be entitled to some of the tax treatments mentioned above.

### **ORDINARY REGIME**

An operating company performs commercial or other business activities in Switzerland, and is taxable on its profits and capital.

The federal direct tax on profits after tax is of 8.5%. As the tax is deductible, the effective federal direct tax rate is of 7.83%. This rate may even be reduced if other taxes are deductible simultaneously.

The tax rates can be quite different between the various municipalities and generally consist in a base rate, as well as additional communal and cantonal multipliers, which can be adapted every year by the Municipal Council.

### **HOLDING COMPANY**

This special tax regime strictly applies to companies whose main statutory purpose is the management of substantial investments (qualified participations) in the capital of other corporations on the long term. These companies cannot carry out commercial activities in Switzerland.

Furthermore, two-thirds of the assets or income of a Holding Company must derive from long term and essential participations (based on book value, or upon request, on the fair market value of all balance sheet's items). Long term loans to subsidiaries may qualify as participation as well, subject to certain conditions.

At the cantonal level, holding companies are exempt from profit tax and benefit from a reduced capital tax rate on their equity. An investment is considered substantial (qualified participation) when its owner may exercise, at least, a notable influence on the management of the company's activities. This regime is granted only at the cantonal level. At the federal level, the participation reduction system applies (see below "Industrial or commercial holding company (Mixed Holding)"), meaning that income which does not derive from participations is fully taxable (7.83 %) while the income deriving from participations is widely exempt.

**INDUSTRIAL OR COMMERCIAL HOLDING COMPANY (MIXED HOLDING)**

Certain form of companies handling at the same time commercial and/or industrial operating activities and holding participations benefit from the participation reduction regime at the cantonal and federal levels. According to this regime, dividend income and capital gain (both of them less the financing and administrative costs) derived from qualifying participations are tax exempt and the profit of the company is consequently taxed at a reduced rate according to the proportion between the exempt participations net income and the total net profit.

Qualifying participations are defined as follows:

**For dividend income exemption purposes:** participation of at least 10 % (20 % until December 31, 2010 for federal profit tax purposes) in the capital of another company or with a fair market value of at least CHF 1 million (CHF 2 millions until December 31, 2010 for federal profit tax purposes). A share of 10% at least in the profit and reserves of a company does also qualify (only as from January 1, 2011 at federal level).

**For capital gains exemption:** participation of at least 10 % (20 % until December 31, 2010 for federal profit tax purposes) in the capital of another company or it entitles a share of 10 % at least in the profit and reserves of a company (only as from January 1, 2011 at federal level) and that the ownership has lasted at least one year. Finally, the income generated by the sale should exceed the investment cost computed based on specific criteria.

**AUXILIARY COMPANY / BASE COMPANY (OR MIXED COMPANY)**

International administration companies whose revenues and related expenses are generated at least at 85% from abroad qualify for this privileged tax regime. It is underlined that both counterparts should be located outside Switzerland. These companies do predominantly depend on markets and activities located, respectively carried out outside Switzerland.

Under this regime and provided that the

shareholder is not residing in Switzerland, 80 % to 90 % of the foreign income from the following activities may be tax exempt at cantonal level:

- international commercial activities (purchase and sale of any products that do not pass through Switzerland),
- financial management (financing, cash management, currency) with foreign counterparts,
- licenses, trademarks and patents developed outside Switzerland, operations of European or international headquarters (principal structure),
- Centralized purchases, etc.

Swiss source income is taxed according to the ordinary regime. If the company is owned by Swiss residents, the tax rates here below are increased based on specific criteria.

**PRINCIPAL COMPANY**

This special tax regime applies at the federal level to Swiss companies (general and regional headquarters) which manufacture and sell goods generally abroad through contract manufacturers and local agents (commissionaires or stripped buy-sell arrangements).



According to this regime, the taxable sales profit is reduced by a maximum of 35 % at the level of the federal direct tax. Non-commercial profits such as financial investment income, royalty income and commissions are fully taxed. At cantonal level, the base company regime may be applicable if the relevant conditions are met. If the goods manufacturing takes place in Switzerland, and therefore no



base / auxiliary tax ruling may be granted, the ordinary tax regime is applicable at the cantonal level, subject to the granting of the principal company tax regime at that level as well.

The Swiss principal tax status meets all the most modern supply chain management's requirements.

### **SERVICE COMPANY**

A company which performs functions or services to member companies offering administrative, technical, scientific or marketing assistance is considered captive. Such a company has not for purposes to make profits (it is only organized as a cost center). Its costs are covered by an affiliated company, usually the parent company. The mark ups of service companies must be determined in accordance with the arm's length principle, on the basis of comparable uncontrolled transactions and with appropriate ranges of mark ups for any individual case. This margin is usually taxed at the ordinary rate.

The service company regime does not apply to management and financial services.

### **FINANCE BRANCH**

The finance branch is a structure which usually consists in a foreign company with a Swiss registered branch. The branch uses funds obtained from the head office, related or third parties to finance affiliates within the Group.

There is a minimum funding requirement of CHF 100 million. Financing activities include lending, cash management, foreign exchange hedging, etc.

This tax regime allows a notional interest deduction for tax purposes. The cantonal base company status may be combined with this tax regime.

### **TEMPORARY TAX HOLIDAY**

A temporary tax holiday, either full or partial, on cantonal profit and equity taxes may be granted for a maximum 10-year period. It is reminded that the term "cantonal tax" does also cover the communal tax. The State Council intends in that way to encourage the creation of enterprises as well as

the creation of jobs in Switzerland.

### **BENEFICIARIES**

The temporary tax holiday is granted to newly created enterprises that carry out a long-lasting activity in the canton. It applies also to enterprises that modify in a substantial way their activities and undertake an important economic reorganization.

The temporary tax holiday first concerns enterprises that "serve the economic interests of the canton". This valuation falls within the competence of the government organization and is in keeping with the general pattern of economic development. The State Council has thus defined the following high-priority fields and activities:

- life sciences (pharmaceutics, biotechnology, medical technology), industrial technology,
- information and communication technology (ICT), energy and environmental technology (cleantech), food-processing / nutrition industry,
- luxury goods industry,
- International sport.

### **RATES AND DURATION**

The temporary tax holiday is of **at most 100% for 10 years**.

Very specific criteria apply as regards rate and duration:

- the sector of activity,
- the number of jobs created,
- the nature and the volume of the investments,
- the setting-up area,
- the cooperation with high schools and research Centre within the canton,
- the competitive situation,
- the possibilities to diversify the regional fabric (indirect economic repercussions for the canton and the region),

- The enterprise autonomy from outside in decision-making and operating.

#### FILLING

The tax holiday application must consist in the following documents:

As a general rule, a temporary tax holiday is granted in two five-year periods of time, when it refers to 10 years. The extension to the second period of time depends on the capacity of having achieved the forecasted creation of jobs and investments put forward in the initial application.

Other conditions apply, in particular a claw-back clause (keeping of the activity in the canton for a maximum period of ten years after the end of the tax holiday).

#### PROCEDURE

The tax holiday request is handled by the Finance Department who gives a decision based on the advance notice of the Economic, Housing and Tourism Service (SELT), of the Cantonal Tax administration and of the Municipal Tax administration where the enterprise is located (residence).

The tax holiday decision is taken

by the

State Council by delegation, in certain cases, to the Head of the Department of Finance and External Relations.

Requests submitted to the Economic, Housing & Tourism Service (SELT) or to the Cantonal Tax Administration (ACI) are treated confidentially.



- A business plan or a presentation of the enterprise (general information, chart, products and services, marketing and distribution, competition, financing plan, etc.),
- A detailed overview of the financing situation of the enterprise (balance sheet, profit & loss, share capital, liabilities, risks, etc.),
- a description on the economic impact of the activities of the enterprise (number of new jobs created, volume of investments, partnerships with subcontractors, collaborations with academic or research institutions, added value for the regional economy).

Furthermore, the application must include the following attachments:

- articles of association and trade register record,
- the last two years Financial statements (for existing enterprise), including the auditor report,
- a budget of the current and next two years (estimated profit and loss),
- a signed engagement form to comply with the existing collective workplace agreements
- A formal tax holiday request.

**Please feel free to contact us with any questions or queries.**

**Trust 4 Trust Group**

**Email: [info@trust4trust.com](mailto:info@trust4trust.com)**

**Ph.: +41 91 220 4710**

**Fax: +41 91 220 4711**