

# Tax Relief in Switzerland

*Switzerland is in many respects an ideal location for taking up residence and doing business. An environment of high legal and political stability and best economic infrastructure combined with low tax rates and a well developed DTT network make up the frame for safe and efficient activities. Switzerland is a confederation of 26 cantons and about 2'800 communities. Taxes are levied at Swiss federal, cantonal and communal levels. Although the tax harmonization law brought conformity under the 26 cantons, there are still many substantial differences to take into consideration when selecting the best place for tax reasons.*

## 1. Individuals

### 1.1 Lump-sum taxation

Lump-sum taxation is a special tax system where Swiss income tax is levied on the basis of expenses (i.e. standard of living).

Foreign nationals who take up Swiss residency for the first time, or after an absence of more than ten years, and who do not undertake a lucrative activity in Switzerland, may qualify for lump-sum taxation. Swiss nationals returning to Switzerland as taxpayers for the first time in 10 years and who do not take up a lucrative activity in Switzerland may also qualify for this regime, but only during the year of arrival and the following year. The amount that serves as basis of taxation is generally negotiated with the competent authorities. The amount of the payable tax must exceed the income tax which would be due on certain Swiss source income and income for which exemption of foreign taxes is requested by virtue of a DTT.

### 1.2 Capital gains

Capital gains are defined as the income generated from the sale, exchange or re-evaluation of assets. They are taxed differently depending on whether they are generated on the realization of personal or business assets.

Capital gains realized on the sale of personal movable assets are always tax exempt. With regard to immovable assets, all cantons levy a tax on capital gains. For Swiss federal tax purposes, also capital gains on immovable property are tax exempt.

Capital gains realized on business assets, movable and immovable, are always subject to income tax. The transfer of business assets into private assets or to affiliates or a foreign permanent establishment is a deemed realization.

For capital gain purposes, independent business activities must also be clearly distinguished from the management of personal wealth. The former are subject to income tax on capital gains. Transactions performed in a professional manner are always deemed to be an independent business activity.

## 2. Corporations

### 2.1 Qualifying dividend income and capital gains

Switzerland has a classical corporate tax system that results in economic double taxation. The shareholders are charged a second time on the dividends and do not get a credit for the tax paid by the corporation. Nevertheless, Switzerland has low tax rates and even the accrued tax burden is normally much less than in other countries.

To avoid triple taxation, intermediate companies receiving dividends or capital gains derived from qualifying holdings may file for tax relief. This relief is available to Swiss corporations, cooperatives and foreign companies of a similar nature if they have a permanent establishment in Switzerland and the dividends or capital gains are linked to the Swiss operations. The relief is available regardless of the nature of the activities and the country of residence of the shareholders.

To qualify for relief on dividend income, the participation must represent at least 20% of the registered capital of the paying company or the market value of the participation must exceed CHF 2 million. To qualify for relief on capital gains, the participation must represent at least 20% of the registered capital of the company and must have been held for at least one year.

### 2.2 Holding companies

Holding companies obtain relief on qualifying dividend income for Swiss federal tax purposes (see above). A pure holding company is therefore more or less exempt from Swiss federal taxes. However, relief does not apply to interest on loans to affiliates or other types of income.

For cantonal tax purposes, companies who qualify for holding company status are widely tax exempt, if the main purpose as per bylaws and as a matter of fact is the management of long-term financial investments in affiliated companies. At least 2/3 of the assets (or income) must be derived from long-term participations. Furthermore a holding company may not be engaged in commercial activity in Switzerland.

According to the tax situation in the Canton of Zug, any stock holdings are considered to be participations. At least one participation must have a substantiation of at least 20% of the registered capital of the concerned company or alternatively have a market value of at least CHF 2 million. Certain Swiss source income is taxable at ordinary rates (real estate located in Switzerland and DTT favored income).

### 2.3 Domiciliary companies

Domiciliary companies have as a basic principle only administrative activities in Switzerland and the commercial activities are exclusively or at least predominantly (80% and more) performed abroad.

The Swiss federal tax law does not provide for any particular relief for domiciliary companies, but there are special rules for cantonal and communal income tax purposes.

Under the definition of 'administration companies' the tax law of the Canton of Zug differs between (pure) domiciliary companies and mixed companies. While (pure) domiciliary companies are forbidden to have any business activity in Switzerland (i.e. no staff and no localities), the mixed companies may have that in a marginal nature.

In case of a (pure) domiciliary company, any income derived from foreign sources and any net income from substantial participations (see holding companies) is tax exempt. All other income is taxable at ordinary rates. Offsetting of net losses from participations with other income is prohibited. Administration expenses and taxes generally are deducted in a lump sum (ordinarily 25%).

The taxation of 'mixed companies' is basically equal to those of (pure) domiciliary companies with the following exception: Income derived from foreign sources is taxed on a reduced basis in accordance with the number of fulltime employees engaged in Switzerland.

### 2.4 International sales companies

International sales companies are set up in Switzerland for the aim of doing trade outside Switzerland in the interest of an alien person.

The Swiss company which is managed from abroad and which has no commercial or technical organization in Switzerland may distribute 50% of its gross income without any form of substantiation. This amount may be paid to related or unrelated parties or offshore accounts with no further explanation. This is the so-called '50% ruling or 50/50 practice'. From the remaining income, certain administrative expenses and direct taxes may be deducted. The difference is taxable at ordinary tax rates.

For cantonal and communal tax purposes, the 50% ruling may be combined with the rules applicable to domiciliary companies. In the Canton of Zug, this implies that the net taxable foreign source income may be absolutely tax exempt.

The Swiss federal tax administration requires that any remaining income must be distributed in the form of a dividend, what is subject to withholding tax of 35%.

### 2.5 Service companies

Service companies generally provide activities to other companies within the same multinational group. Services to third parties do not qualify.

Profit assessable in Switzerland is generally deemed to be at least 5%

of total expenses incurred on the twelfth (8.33%) of total local payroll costs. For cantonal and communal tax purposes it may be combined with the rules applicable to domiciliary companies. Depending on the facts in a given case, the Cantonal Tax Authorities are often open for rulings simplifying the methods of calculating the corporate income tax.

### 2.6 New businesses

Relief is often also granted to newly established businesses and vital reorganizations to attract investments. Nearly all cantons encourage certain establishments within their territories by granting tax privileges for periods of up to ten years. The establishment or restructuring of a business must be in the interests of the regional economy in order to qualify for relief. This depends on the appreciation of the competent authorities. Reorganizations such as mergers, demergers etc. do not automatically qualify.

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