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Update

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Corporate Tax Reform III

On June 17, 2016 the Swiss parliament adopted the Corporate Tax Reform III (CTR III) which will abolish cantonal corporate tax privileges, likely as per January 1, 2019. At the same time, a series of new tax measures are intended to replace the abolished tax treatment along with expected substantial general tax rate cuts at the cantonal level.

The CTR III adopted by the Swiss parliament may be subject to a public referendum if requested by at least 50'000 citizens. It is widely expected that such public vote will in fact take place, likely in February 2017.

The CTR III includes the following measures:

Abolishment of cantonal tax privileges

The CTR III abolishes the existing cantonal holding, domiciliary and mixed company regimes. Likewise, the so called principal company regime and the finance branch regime, applicable according to Swiss tax administration practice, will no longer be available. All corporations will hence be subject to ordinary corporate income and capital tax, which should make the Swiss corporate income tax (CIT) system OECD and EU compatible. Still, for holding companies participation reduction usually resulting in full or almost full exemption from CIT on dividend income and capital gains from substantial shareholdings and unilateral PE exemptions continue to apply.

Step-up

Companies benefitting from the above mentioned regimes may in most cantons have the option to voluntarily give up the privileged tax treatment ahead of the CTR III and thereby benefit from a tax-free step-up in the value of their assets for cantonal tax purposes, including for goodwill up to fair market value, which will be available for later depreciation. Alternatively, unrealized gains including goodwill will be determined by the tax administration upon entry into force of the new legislation. Within the determined amount of unrealized gains, corporations may benefit from a reduced CIT rate on profits for five years.

A step-up of hidden reserves, including goodwill, also applies to companies relocating their corporate seat or assets to Switzerland, with the possibility of later depreciation.

Reduced Cantonal corporate income tax

Many Cantons announced significant corporate income tax rate reductions, currently varying between 11.3% and 24.4%. Such reduced rates will be partly financed by a larger share of the Federal CIT proceeds allocated to the Cantons.

Patent box regime

The CTR III introduces at the cantonal level a "patent box" regime allowing for up to 90% reduced taxation of qualifying income from patents and similar rights. Following the OECD-principles, the so called "modified nexus approach" applies, which means that only income resulting from own research and development activities plus an uplift of 30% qualifies for the reduced taxation.

The determination of the qualifying income follows the residual method whereby overall profit is reduced by non-patent related income such as income from trademarks, routine functions, financing, production, etc.

R&D super deduction

Cantons are entitled to introduce an R&D super deduction up to 150% of effectively incurred R&D expenses.

Notional interest deduction

The CTR III introduces at the Federal level a notional interest deduction (NID) that allows for a notional interest deduction on non-core equity. Non-core equity is determined by reference to the Swiss thin-capitalization rules.

Cantons are allowed to introduce a NID as well, provided they also introduce a minimum dividend-income taxation for individuals.

The applicable NID interest rate is determined based on Swiss government bonds. It can be increased to the extent a company grants intragroup financing.

Reduced capital tax

Cantons are allowed to reduce annual corporate capital tax levied on the equity to the extent the company holds significant shareholdings, qualifying patents and intragroup loans.

Conclusion

Most of the CTR III replacement measures are applying at cantonal level only. The cantons have thus an important level of discretion for the determination of the reduced rate applying to the patent box income or to the profits corresponding to the step-up. Likewise, they can freely determine whether to introduce a notional interest deduction. In addition, many cantons have already taken steps towards an important reduction of the ordinary CIT rate.

Please do not hesitate to contact us in case of any questions.

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