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Tax Controversy

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in Geneva, Zürich and Lausanne. Tax practice areas include M&A; restructurings and buyouts; financing; financial products and derivatives; estate and tax planning for executives, including employee share and stock option plans; investment funds; private equity funds; property (acquisition and development); value-added tax; internal investigations; and tax litigation.

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1. Tax Controversies

1.1 Tax Controversies in this Jurisdiction

As a preliminary remark, it should be emphasised that taxes in Switzerland are levied at three different levels: federal, cantonal and municipal. Due to the fact that cantons still have a high level of independence regarding tax matters, this can result in significant differences in the handling of tax controversies between the various cantonal and federal tax authorities.

Tax controversies usually arise by way of a formal complaint filed by the taxpayer against a tax assessment decision rendered by a tax authority. In the fields of withholding tax, stamp tax and VAT, where the principle of spontaneous taxation applies (meaning that the taxpayer determines himself the amount of tax due, declares it and pays said amount to tax authorities), controversies usually start as a result of a tax audit conducted by the Swiss Federal Tax Administration (SFTA).

1.2 Causes of Tax Controversies

All tax matters may give rise to tax controversies, regardless of the type of tax or of the values involved.

1.3 Avoidance of Tax Controversies

Broadly speaking, Swiss tax authorities are quite open to discussion with the taxpayers, which serves to mitigate the possibility of tax controversies further down the line. In particular, tax rulings (see **6.4 Avoiding Disputes by Means of Binding Advance Information and Ruling Requests**) provide a powerful tool to ensure certainty and avoid ulterior disputes.

1.4 Efforts to Combat Tax Avoidance

As an effort to comply with the base erosion and profit shifting (BEPS) recommendations of the Organisation for Economic Co-operation and Development (OECD) as well as with the EU's various measures to combat tax avoidance, Swiss tax authorities have taken, over the years, a stricter approach in many tax matters. This has led to a growing number of tax controversies in Switzerland, with, for instance, offshore structures being increasingly challenged.

1.5 Additional Tax Assessments

When faced with an additional tax assessment, the taxpayer is not obliged to pay or guarantee the tax assessed in order to be able to lodge a formal complaint, and subsequently an appeal, against it.

Alongside the additional tax assessment, Swiss tax authorities will typically open criminal proceedings against the taxpayer; for instance, due to the misdemeanour of not having declared a taxable event to the tax authorities.

2. Tax Audits

2.1 Main Rules Determining Tax Audits

Swiss tax authorities do not share the criteria on which they base their decisions to perform a tax audit. The different tax authorities have a certain flexibility in that matter. Some tax authorities set year-to-year variation thresholds regarding the taxable amounts reported, which can trigger a verification process.

2.2 Initiation and Duration of a Tax Audit

Tax authorities may initiate tax audits as soon as they have information relevant to taxation previously unknown to them.

The statutory limitation to initiate a procedure for the collection of back taxes is ten years after the end of the tax period for which the tax has not been levied, preventing any such procedure afterwards.

Once the procedure has been initiated, the statutory limitation to determine a supplementary tax is 15 years after the end of the tax period to which the procedure relates, preventing any levy of tax afterwards, even if a back-taxes procedure has been opened.

2.3 Location and Procedure of Tax Audits

As a rule, tax authorities in Switzerland, whether cantonal or federal, have an audit department with an internal and an external unit. The latter can visit the taxpayer's premises.

2.4 Areas of Special Attention in Tax Audits

Tax auditors may be interested in all aspects of taxation. Regarding companies, compliance of the accounts with accounting and tax rules is the most important aspect for legal entities examined by tax auditors. As for natural persons, justification of the deductions claimed and the existence of unlimited liability are frequently examined.

2.5 Impact of Rules Concerning Cross-border Exchanges of Information and Mutual Assistance Between Tax Authorities on Tax Audits

The exchange of information and the evolution of international tax rules has certainly led to an increase in tax audits in Switzerland.

Assisting clients targeted by requests for information from foreign countries in the context of a foreign tax audit is a frequent activity of this firm.

2.6 Strategic Points for Consideration During Tax Audits

One unique feature of the Swiss tax authorities is their willingness to discuss tax matters with taxpayers openly. In the context of a tax audit, the best strategy is often to demonstrate transparency regarding the facts and technical accuracy regarding the legal analysis.

3. Administrative Litigation

3.1 Administrative Claim Phase

If a taxpayer disagrees with an assessment decision made by a tax authority, they may submit a formal complaint to the same tax authority that has issued the assessment decision, within 30 days as from notification. The formal complaint procedure is an official appeal procedure that forces the tax authority to issue a new decision subsequently.

Such a formal complaint must be filed in writing. With regard to income tax, the complaint does not need to be substantially motivated. The taxpayer only has to express their unquestionable disagreement with the assessment decision. Formal complaints in the field of other taxes must be sufficiently motivated, meaning that the taxpayer has to demonstrate that the assessment decision is obviously inaccurate.

If the formal requirements are met, the tax authority has to re-examine the tax assessment decision and may modify in whole or in part the first decision or reject the taxpayer's formal complaint.

3.2 Deadline for Administrative Claims

While Swiss tax law does not provide for a particular deadline for the tax authorities to respond to a formal complaint lodged by a taxpayer, they have a constitutional obligation to process the claim within a reasonable time. The meaning of 'reasonable time' is not clearly defined and depends on the specific circumstances of the case at hand. The taxpayer can lodge a judicial claim if a tax authority does not process their formal complaint within a reasonable timeframe.

4. Judicial Litigation: First Instance

4.1 Initiation of Judicial Tax Litigation

If the taxpayer is not satisfied with the decision of the tax authority on their formal complaint, they have the ability to lodge an appeal with a first-instance cantonal court or, in matters falling under the authority of the SFTA, with the Swiss Federal Administrative Court. The deadline to lodge an appeal is 30 days as from notification of the contested decision on formal complaint.

4.2 Procedure of Judicial Tax Litigation

Swiss administrative procedure rules, including tax procedure rules, provide for an essentially written litigation process and imply few or no investigative acts such as hearings, due to the technical nature of tax law and the numerical content of litigations.

Following the taxpayer's appeal, the tax administration files a reply before the court, supporting the position of its tax decision. Usually, an additional exchange of replies is allowed, before the case is kept to be judged by the court until the judgment is rendered.

4.3 Relevance of Evidence in Judicial Tax Litigation

Evidence must be provided at the time of lodging the appeal and is particularly important because of the burden of proof in Swiss tax litigation (see **4.4 Burden of Proof in Judicial Tax Litigation**).

4.4 Burden of Proof in Judicial Tax Litigation

Regarding tax matters in general, as well as within the context of judicial tax litigation, the tax authority must establish the facts upon which the tax liability is based, while the taxpayer has to prove the facts that reduce or eliminate said liability.

If the elements gathered by the tax authority provide enough evidence of the existence of taxable items, it also falls upon the taxpayer to establish the truth of their own claims and to bear the burden of proof regarding elements that justify their exemption.

4.5 Strategic Options in Judicial Tax Litigation

Legal analysis and reassessment of the tax administration's position is the most important aspect of a tax litigation. Settlements with the tax administration are still possible but less likely once the dispute has begun, as tax authorities sometimes have an interest in having their practice confirmed by courts.

With the exception of a back-taxes procedure, which often covers the previous ten years and where statutes of limitation may play a minor role for the earliest years depending on the case at hand, timing is generally not an efficient strategy.

4.6 Relevance of Jurisprudence and Guidelines to Judicial Tax Litigation

Statutes and case law are the most important sources for Swiss tax courts. The ECHR's case law is also taken into account, in particular within criminal tax procedures. International guidelines are also elements of interpretation on which the courts rely. Tax doctrine is also a source of interpretation used by courts, but they are not bound by the doctrine.

5. Judicial Litigation: Appeals

5.1 System for Appealing Judicial Tax Litigation Appeal Before a Second-instance Court

Any tax decision previously challenged before a first-instance court may be appealed. There is no limit based on the value of the dispute.

A decision of a first-instance court can be appealed to a second-instance cantonal court within 30 days of service of the first-instance court's decision. The appeal can be filed by the tax authority or the taxpayer, or both.

The procedural principles are the same as those applying before the first-instance court. Judgments of a second-instance court may be appealed to the Federal Supreme Court.

Appeal Before the Federal Administrative Court

The Federal Administrative Court is the ordinary administrative tribunal of the Swiss Confederation. The main role of the Federal Administrative Court is to examine the legality of decisions in matters falling under the authority of the Federal Administration.

Lower instances are mainly the federal departments and subordinate federal offices. The Federal Administrative Court hears appeals against decisions of federal authorities, in the fields of withholding tax, stamp tax and value added tax (VAT) in particular.

A decision of the Federal Administrative Court can be appealed to a second-instance cantonal court within 30 days of service of the first-instance court's decision. The appeal can also be filed by the tax authority or the taxpayer, or both.

Its judgments may be appealed to the Federal Supreme Court.

Appeal Before the Federal Supreme Court

If the taxpayer considers that the final decision of the second-instance cantonal court or of the Federal Administrative Court violates their rights, they may file an appeal before the Federal Supreme Court. Such an appeal must be filed within 30 days of notification of said contested decision.

The Federal Supreme Court is the highest judicial authority within the federal state. It issues final rulings in tax matters.

5.2 Stages in the Tax Appeal Procedure

For the different stages in tax appeal procedures before all Swiss courts, see **4.2 Procedure of Judicial Tax Litigation** regarding the first-instance cantonal court, given that the procedure is essentially the same.

However, it should be noted that the Federal Court does not re-establish the facts of the case. These facts may only be corrected by the Federal Court if it finds that they have been blatantly incorrectly established by the lower court, or that they have been based on a violation of law. This means that the Federal Court only takes its decisions applying the law on facts already determined.

5.3 Judges and Decisions in Tax Appeals

In the opposition procedure, the tax administration renders a decision. In the canton of Geneva, before the first instance, a judge renders their decision with the help of two associate judges specialised in tax law. The second instance is composed of three professional judges.

The Federal Administrative Court and the Federal Court are, as a rule, composed of three judges but may be composed of five judges in special cases. Before these courts, a single judge may render a judgment for clearly inadmissible or insufficiently motivated cases.

6. Alternative Dispute Resolution (ADR) Mechanisms

6.1 Mechanisms for Tax-related ADR in this Jurisdiction

Swiss tax law does not provide for national mediation or arbitration procedures.

With regard to ADR means, double taxation treaties concluded by Switzerland usually refer to a mutual agreement procedure, which is independent of Swiss domestic law procedures. Thus, the time limits provided for by domestic law have no influence on the mutual agreement procedure and vice versa. In particular, the 30-day deadline to file a claim against a tax assessment decision is not suspended by a request for a mutual agreement procedure. In order to save their rights according to Swiss tax law, the taxpayer should file a complaint against the tax authority, which will be suspended during the mutual agreement procedure.

6.2 Settlement of Tax Disputes by Means of ADR

In international tax matters, a mutual agreement procedure is carried out if the procedure set out between the competent Swiss and foreign authorities is unsuccessful.

The mutual agreement procedure is initiated at the taxpayer's request, before the competent authority in the taxpayer's country of residence. However, the taxpayer itself is not a party since the mutual agreement procedure is a procedure between one state and another.

In Switzerland, the competent authority for mutual agreement procedures is the State Secretariat for International

Financial Matters (SIF). There is no obligation of result between Switzerland and the relevant other state.

6.3 Agreements to Reduce Tax Assessments, Interest or Penalties

Swiss tax law does not have national mediation or arbitration procedures.

6.4 Avoiding Disputes by Means of Binding Advance Information and Ruling Requests

Given the overall complexity of taxation in Switzerland, taxpayers have an interest in discussing the more complex cases with the tax authorities at an early stage; for instance, in the case of international corporations considering moving to Switzerland, so they can obtain confirmation of their future taxation. The same is true for individuals.

In this regard, tax rulings are commonly used in the Swiss tax practice, although Swiss tax law does not expressly refer to rulings. It should be noted that a tax ruling does not provide any preferential taxation over the applicable law. This constitutes a more quick and efficient way to provide for clarity in readiness for taxation.

In order to obtain a ruling, the taxpayer has to disclose all relevant information, usually in the form of a letter. If the competent tax authority agrees with the taxpayer, the ruling request is sent back to the taxpayer with the stamp of the authority, which provides the taxpayer with confirmation from the State on the tax treatment of a transaction or a situation. Tax rulings are not public.

Regarding the binding effect of such rulings, the taxpayer is protected by the constitutional principle of good faith in so far as he relies on the information received by the competent tax authority. Swiss case law also especially emphasises the importance of implementing the facts precisely described in the ruling.

There is no legal entitlement for a taxpayer to obtain a binding ruling, even though tax authorities are mostly willing to deal with ruling requests. This means that taxpayers cannot contest a refusal of a ruling request.

6.5 Further Particulars Concerning Tax ADR Mechanisms

As mentioned in 6.2 Settlement of Tax Disputes by Means of ADR, the mutual agreement procedure, in the case of double taxation with a country with which Switzerland has signed a double taxation agreement, requires that all relevant steps between the relevant Swiss and foreign entities be respected.

There is no limit value of the claim. According to the OECD Model Tax Convention on Income and on Capital of 2017, the taxpayer has to request the initiation of a mutual agree-

ment procedure within three years from the first notification of the action resulting in double taxation.

There is no appeal possible against the outcome of the mutual agreement procedure.

6.6 Use of ADR in Transfer Pricing and Cases of Indirect Determination of Tax

ADR is mostly used in transfer-pricing cases. Relating to the mutual agreement procedure and according to the 2017 statistical report of the competent authority, out of 264 cases filed, 150 related to transfer-pricing issues.

7. Administrative and Criminal Tax Offences

7.1 Interaction of Tax Assessments with Tax Infringements

As a preliminary remark, it should be underlined that regarding direct taxes, the fact that the taxpayer seeks to save taxes is not punishable. Furthermore, in Switzerland, anti-avoidance rules are not contained in a specific act. They actually take different forms.

Swiss tax law includes a purely administrative procedure, the back-taxes procedure, which aims to recover amounts not dutifully declared by the taxpayer.

Swiss criminal tax law deals with misdemeanours (or 'contraventions'), which lead to a fine, and tax offences, which may imply imprisonment.

Breach of procedural obligations, tax evasion and attempted tax evasion are the main misdemeanours.

Breach of procedural obligations refers to situations, for example, where the taxpayer fails to file a tax return or does not comply with a duty to provide information. Regarding the sanction, for income and equity taxes, the penalty is limited to CHF10,000. For other types of taxes, the limit differs.

Tax evasion is given where the taxpayer with intent or negligently omits certain items in their tax return, or causes a final assessment to be incomplete. The fine may vary from one third to three times the amount of tax evaded. The statute of limitations is ten years.

Regarding attempted tax evasion, the fine amounts to two thirds of the amount determined for complete evasion. The statute of limitations is six years.

A back taxes procedure, which aims to recover amounts not dutifully declared by the taxpayer, generally triggers a tax evasion procedure.

Forgery and withholding tax at source diversion are the main tax offences.

Forgery is the use of fraudulent documents (eg, false financial statements or salary certificates) and is a qualified tax offence with a maximal penalty of imprisonment up to three years and a fine of a minimum of CHF10,000.

Tax at source diversion is where a person required to collect tax at source misappropriates the amounts collected for their own benefit or for that of a third party. The maximum penalty is an imprisonment of up to three years.

In tax offences, the payment of back taxes is always due.

7.2 Relationship Between Administrative and Criminal Processes

For tax misdemeanours, the competent authority for the processing of the back-taxes and tax-evasion procedures is the same authority, namely the tax administration and then the courts. As a rule, the two cases are therefore treated in parallel and the procedure is set in tax law.

For tax offences, the Public Prosecutor is competent. In such cases, the tax or criminal authority, depending on the case, may decide to suspend one procedure during the settlement of the other. The procedure is set in criminal law. The criminal procedure is generally more elaborate than the tax procedure and leaves more room for investigative acts.

The Public Prosecutor is only competent regarding the criminal part of the tax offence. The calculation of the amount of tax due is still the responsibility of the tax authorities.

7.3 Initiation of Administrative Processes and Criminal Cases

Tax authorities initiate such proceedings when they suspect that a tax return is incomplete. As mentioned (see **7.1 Interaction of Tax Assessments with Tax Infringements**), a back taxes procedure generally implies a tax evasion procedure, which is of a criminal nature.

Depending on the case at hand, the case may evolve into a more serious offence, but most of the cases tend to evolve into a two-way procedure of back taxes and tax evasion.

7.4 Stages of Administrative Processes and Criminal Cases

For tax misdemeanours, since the authority establishing the back taxes also establishes the criminal tax penalty, the process is treated by the relevant authority, whether it is the tax authority or the relevant court.

For tax offences, while the back taxes procedure will still be treated by the tax authority, respectively the relevant admin-

istrative tax court, the Public Prosecutor is competent on the criminal aspect.

7.5 Possibility of Fine Reductions

In cases of tax evasion, the good co-operation of the taxpayer makes it possible to reduce the amount of the fine within the framework of the law. However, the amount of tax due, which relates to the back taxes procedure, cannot be changed.

7.6 Possibility of Agreements to Prevent Trial

For tax misdemeanours, if the taxpayer does not challenge the decision of the tax administration, the procedure is not pursued before the administrative courts, but the payment of the fine will still be due. Before the administrative courts, full payment of the tax and fine, and the withdrawal of the appeal, are also possible. However, this does not change the criminal tax qualification of the procedure.

For tax offences, the issue is a matter for the criminal courts and the mere payment of the tax due is not enough to stop the procedure, since the issue of tax payments is not addressed by the Public Prosecutor.

Where the taxpayer acknowledges the material facts, a simplified procedure may be possible before the Public Prosecutor under certain conditions. The Public Prosecutor prepares an indictment that the taxpayer may accept or refuse.

7.7 Appeals Against Criminal Tax Decisions

For misdemeanours, appeal possibilities are the same as exposed above in **7.4 Stages of Administrative Processes and Criminal Cases** and **7.5 Possibility of Fine Reductions**.

For criminal offences, an appeal to the second instance and then to the criminal chamber of the Federal Court is possible.

7.8 Rules Challenging Transactions and Operations in this Jurisdiction

As a rule, transactions and operations challenged under transfer-pricing rules or general anti-avoidance rules have resulted in two-way procedure cases of back taxes and tax evasion.

8. Cross-border Tax Disputes

8.1 Mechanisms to Deal with Double Taxation

In the vast majority of double taxation cases, domestic legal remedies are first used to correct the situation. However, the mutual agreement procedure available under double tax treaties is increasingly used by taxpayers in parallel with domestic remedies. As to arbitration, it is quite rare in practice, as arbitration clauses are still relatively new in treaties signed by Switzerland.

8.2 Application of GAAR/SAAR to Cross-border Situations

As mentioned, in Switzerland, anti-avoidance rules are not contained in a specific act. However, the Swiss Federal Supreme Court has developed a general principle of tax avoidance and abuse of rights, applicable to all Swiss taxes. This general reservation on abuse of rights also applies to all Swiss double tax treaties.

8.3 Challenges to International Transfer Pricing Adjustments

International transfer-pricing adjustments are usually challenged first and foremost under domestic tax courts. Although Switzerland does not have an explicit transfer-pricing legislation, such courts apply in practice the OECD Transfer Pricing Guidelines.

The majority of tax treaties signed by Switzerland do not contain the corresponding adjustment provisions of Article 9, Paragraph 2 of the OECD Model Tax Convention.

8.4 Unilateral/Bilateral Advance Pricing Agreements

Advance pricing agreements may be used in the context of rulings (see **6.4 Avoiding Disputes by Means of Binding Information and Ruling Requests**).

8.5 Litigation Relating to Cross-border Situations

Among the various cross-border situations, withholding tax is probably the matter that gives rise to the most litigation. This is due to the high withholding tax rate (35%), as well as the fact that Switzerland is a large importer of foreign capital.

In general, a ruling is the most effective way to prevent litigation under Swiss tax law and to prevent the risk proactively.

9. Costs/Fees

9.1 Costs/Fees Relating to Administrative Litigation

A formal complaint with the tax authority is free of charge.

9.2 Judicial Court Fees

The amount of the fees varies according to the canton. In Geneva, before the first-instance court, the fees for the case are fixed according to the complexity of the case, but cannot exceed CHF10,000. An indemnity for legal costs may be charged to the unsuccessful party. The same rules apply before the second-instance court.

Before the Federal Administrative Court and the Federal Court, fees are calculated based on the amount in dispute, the scale and difficulty of the case, the parties' procedures and their financial situation. As a rule, legal costs are borne by the unsuccessful party.

Fees are paid once the judgment is rendered, but an advance payment is required by the courts. There is no interest payment on it.

9.3 Indemnities

There is no possible compensation based on a taxation considered void and null under Swiss tax law. However, any amount already paid by the taxpayer will be reimbursed.

9.4 Costs of Alternative Dispute Resolution

The mutual agreement procedure is free of charge. However, the taxpayer bears the costs incurred by their request (in particular, the fees of their possible agent).

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10. Statistics

10.1 Pending Tax Court Cases

Statistics of the Geneva authorities are not publicly available.

The latest report available from the Federal Court in 2017 indicates that 389 cases were filed in tax matters. Additional statistics on their value are not available.

10.2 Cases Relating to Different Taxes

In 2017, 320 cases were initiated for direct taxes, no cases were initiated for stamp duty tax, eight for indirect taxes, 17 for withholding taxes, one for military tax, one for double taxation, 42 for other taxes and nine for tax exemption. Additional statistics on their value are not available.

10.3 Parties Succeeding in Litigation

According to a private study carried out on the basis of Federal Court data from the last ten years, an appeal filed by a taxpayer with the Federal Court in tax matters succeeds only 14% of the time.

11. Strategies

11.1 Strategic Guidelines in Tax Controversies

The best way to manage a tax dispute is to avoid it by planning, essentially through an early tax analysis of the situation and, if necessary, by a ruling.

In a pending procedure, the legal analysis of the administration's position is an essential step. The use of a specialist is also essential.