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Briefing February 2017

Tax News: Corporate Tax Reform III – rejected by referendum

On 12 February 2017, the Corporate Tax Reform III ("CTR III") was submitted to a referendum and rejected with 59.1%. It is fair to assume that a new bill including the CTR III's main points will be elaborated and published shortly. The new reform bill will confirm the abolition of the cantonal tax privileges as requested by the OECD and the EU. In addition, and similar to the rejected reform proposal, the new bill will have to introduce some measures designed to maintain and reinforce the fiscal attractiveness of Switzerland. However, these new measures can be expected to be less far-reaching than those provided under the rejected proposal. At present, no detailed information on a potential new bill and its implementation timeline is available.

Background and Objective of the Corporate Tax Reform III

In recent years, Switzerland has come under increasing pressure from both the EU and the OECD to abolish its preferential tax regimes. In fact, the existing cantonal tax privileges for holding, domiciliary and auxiliary/mixed companies as well as certain federal tax practices pertaining to finance branches and principal companies were at the core of international criticism.

On 5 June 2015, the Federal Council published its draft legislative proposal for the Corporate Tax Reform III, along with its detailed explanatory report. After long debate, the Federal Parliament approved the final reform bill on 17 June 2016 (cf. B&K Briefing June 2016). A referendum on the reform package was held on 12 February 2017.

The key objective of the CTR III was to abolish the special corporate tax regimes, whilst safeguarding Switzerland's attractiveness to business and foreign direct investments in Switzerland by introducing several new measures.

Opponents of the rejected reform proposal were primarily concerned with the potential losses in cantonal tax revenues, and their criticism was broadly aimed at limiting the fiscal effects of the new measures. Even so, the need to abolish the cantonal tax privileges remains uncontentious.

Summary of the rejected reform package

The CTR III as agreed by the States Council and the National Council included the following elements (for further information see B&K Briefing June 2016):

– **Abolition of preferential cantonal tax regimes and certain federal tax practices**

- **Basis for reduction of cantonal corporate income tax rates:** Before the referendum, 19 of 26 cantons indicated their willingness to decrease the corporate tax rates. It remains open whether and, if so, to what extent the rates will now be reduced.

- **Introduction of a Patent Box at cantonal level**

- **Introduction of a super-deduction for R&D expenses at cantonal level (optional):** This aspect was not included in the initial reform package of 2015. It is unclear whether the super-deduction will continue to be part of the new bill.

- **Introduction of a notional interest deduction (NID) at federal and cantonal level (optional):** This element was introduced only at the end of the legislative process and was one of the opponent's main point of criticism.

- **Dividend taxation (at least 60%) at the level of an individual shareholder as requirement for cantonal NID:** This point was included in conjunction with the implementation of the NID. It remains to be seen whether the new legislative proposal will stipulate a higher taxable quota.

- **Taxation of built-in gains arising under a cantonal tax privilege:** Determining the special tax rates is at the discretion of each canton.

- **Limitation of total benefit at cantonal level:** Patent Box, super-deduction of R&D expenses and NID together were not allowed to reduce the taxable profit by more than 80% at cantonal level, which would have provided planning certainty for the cantons.

- **Introduction of possible reduction of cantonal net equity tax**

- **Improvement for withholding tax refund of Swiss branches**

Next Steps

The opponents of the CTR III strive for a more balanced bill and, in their opinion, it should still be possible to implement a new bill by the beginning of 2019. However, the Federal Council takes the contrasting view that the implementation – despite reasonable efforts – will not come into force before 2022, for reforming the corporate tax remains a complex undertaking.

To avoid unilateral tax repercussions from the EU, the OECD or any other individual countries, it can be assumed that Switzerland will be inclined to implement a new corporate tax reform as soon as possible. The new proposal will endeavor to find a balance between the measures designed to maintain and reinforce the fiscal attractiveness of Switzerland, the tax collection and the compliance with international standards.

We will continue to keep you informed on current developments and remain at your disposal for any further questions you may have.

Your Key Contacts

Susanne Schreiber
Partner
T: +41 58 261 52 12
susanne.schreiber@baerkarrer.ch

Daniel Bader
Partner
T: +41 58 261 54 32
daniel.bader@baerkarrer.ch

Peter Reinarz
Partner
T: +41 58 261 53 30
peter.reinarz@baerkarrer.ch

Further Contributors to this Briefing:

Paolo Bottini
Partner
T: +41 58 261 58 30
paolo.bottini@baerkarrer.ch

Dr. Daniel Lehmann
Partner
T: +41 58 261 54 30
daniel.lehmann@baerkarrer.ch

Bär & Karrer Ltd.
Brandschenkestrasse 90
CH-8027 Zurich

Telephone: +41 58 261 50 00
Fax: +41 58 261 50 01
zurich@baerkarrer.ch

baerkarrer.ch
Zurich, Geneva, Lugano, Zug