

TAX ON INBOUND INVESTMENT

Switzerland



Tax on Inbound Investment

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Quick reference guide enabling side-by-side comparison of local insights into acquisitions (from the buyer's perspective), post-acquisition restructuring, and disposals (from the seller's perspective), including stock versus asset/liability transactions; domicile of acquisition company; company mergers and share exchanges; tax benefits of issuing stock as consideration; transaction taxes; treatment of deferred tax assets; interest relief; protections for acquisitions; spin-offs; migration of residence; interest and dividend payments; tax-efficient extraction of profits; methods of disposal including for tax mitigation and deferral purposes; and recent trends.

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ACQUISITIONS (FROM THE BUYER'S PERSPECTIVE)

Tax treatment of different acquisitions

What are the differences in tax treatment between an acquisition of stock in a company and the acquisition of business assets and liabilities?

Both the seller and the acquirer face different tax implications depending on whether an acquisition is carried out by way of acquisition of stock (share deal) or acquisition of business assets and liabilities (asset deal).

The main differences concern the tax treatment of capital gains, respectively realised income on the transfer of assets, transfer of historic tax liabilities, step-up in basis of the target's underlying assets, transfer of the tax loss carry-forward and transaction taxes.

In an asset deal, the seller will generally be taxed on the realised income (namely, realised hidden reserves) at the applicable corporate income tax rate. An acquirer often prefers an asset deal, as in this case, the tax risks transferred with the acquired business are very limited. Generally, only liabilities in respect of social security and real estate taxes (if applicable) and potentially value added tax (VAT) and customs are inherited. Further, a step-up in basis and tax-deductible depreciation are, in principle, possible and interest for acquisition debt may be more easily set off against taxable income of the acquired business. Income tax loss carry-forwards of the business remain with the seller. The asset transfer is generally subject to VAT, currently at 7.7 per cent, on the transfer of taxable goods and goodwill. Alternatively, a VAT notification procedure, in some cases, can respectively be used. This means that no Swiss VAT is charged on the transaction, but the transaction is notified using a specific form. Finally, should real estate be transferred, special cantonal or communal real estate gains taxation for the seller and real estate transfer taxes may need to be considered.

Sellers typically prefer share deals because of the privileged tax treatment of capital gains in Switzerland. The acquirer of shares in a Swiss company assumes potential historical tax risks and the tax book values of the target company, since both remain unchanged in the target company. The goodwill reflected in the share price generally cannot be written off against taxable profits. The acquirer's interest expenses on acquisition debt cannot be directly set off against taxable income of the target, but require additional structuring. The acquisition of a partnership interest is, from an income tax perspective, generally treated like an asset deal and results in a step-up for the acquirer.

In the case of a share deal, the target company generally keeps its tax loss carry-forward, if any, and can set it off against taxable profit during the ordinary tax loss carry-forward period of seven years. The acquisition of shares in a Swiss company is not subject to Swiss VAT. Further, in the case of a share deal, the acquirer may inherit the latent dividends withholding tax liability in respect of the retained profits accumulated pre-sale (old reserves of the target company per the date of the share acquisition). This issue is particularly relevant in the case of foreign resident sellers, who were not entitled to a full refund of the Swiss dividends withholding tax under the relevant double tax treaty.

The Federal Tax Authority's (FTA) interpretation of anti-abuse limitations has also become more restrictive in cross-border constellations in recent years. Owing to an 'international transposition', the refund of Swiss withholding tax will be denied based on the practice of the FTA if a person not entitled to a full refund transfers the shares in a Swiss company to a Swiss company controlled by the same person by way of sale against a share capital increase of the receiving entity with respect to a contribution into the capital contribution reserves of the receiving entity. This practice has recently been extended and is also applied to certain acquisitions by Swiss acquisition companies, which are financed via shareholder loans or capital contribution reserves (an extended international transposition). The tightened-up practice is especially relevant for investments by private equity funds.

Law stated - 08 August 2022

Step-up in basis

In what circumstances does a purchaser get a step-up in basis in the business assets of the target company? Can goodwill and other intangibles be depreciated for tax purposes in the event of the purchase of those assets, and the purchase of stock in a company owning those assets?

In cases where the purchase price in an asset deal exceeds the fair market value of the net assets of an acquired business, an acquirer may capitalise such difference as goodwill, which is typically depreciated according to Swiss tax and accounting rules at 40 per cent per annum (declining balance method; the remaining amount depreciated in the last year) or at 20 per cent per annum (straight-line method) over five years. Such depreciation expense is generally deductible from taxable income. A depreciation of 20 per cent per annum generally also applies to the part of the purchase price allocated to intellectual property (IP). Certain cantonal tax authorities have, however, in recent months started to take a stricter standpoint and only allow an impairment (instead of a straight-line depreciation over the years) on IP (not, however, on goodwill) in cases of an evidenced loss in value.

In the case of a share deal, the purchase price is entirely allocated to the shares acquired and the taxable basis of the target company remains unchanged (namely, no goodwill is recognised). A depreciation on the acquired shares is typically only possible for a Swiss acquirer if there is a decrease in the fair market value of the shares. Such adjustment of the share value is tax-deductible for a Swiss corporate acquirer. However, if the value of a participation of at least 10 per cent recovers in subsequent years, the Swiss tax authorities may demand the reversal of the adjustment or depreciation up to the original acquisition cost basis, which is taxable.

Law stated - 08 August 2022

Domicile of acquisition company

Is it preferable for an acquisition to be executed by an acquisition company established in or out of your jurisdiction?

In the case of an asset deal, a Swiss acquisition company is highly preferable from a tax and legal perspective. Otherwise, the acquired business will likely constitute a permanent establishment of a foreign acquirer, creating the need to prevent international double taxation through the allocation of profits between the acquirer's foreign head office and its Swiss permanent establishment.

Even though Switzerland has no tax-consolidation rules (except for VAT), a Swiss acquisition company may be a good choice for a share deal.

First, Switzerland has a generally attractive tax regime. The applicable corporate income tax rates are internationally competitive. The effective corporate income tax rate (on the profit before tax) amount to between approximately 11.9 per cent (Zug) or 12.3 per cent (Lucerne) to a maximum of 21 per cent (Berne). Further, Switzerland has various additional tax benefits, such as a patent box, notional interest deduction (only in the canton of Zurich) and a reduction of cantonal capital tax on qualifying participations.

Switzerland has no controlled foreign corporation (CFC) regime and is not currently planning to introduce such rules.

Any dividend income from qualifying participations of at least 10 per cent (or with a fair market value of at least 1 million Swiss francs) and capital gains on the sale of qualifying participations of at least 10 per cent held for at least one year benefit from the participation deduction scheme, under which such income is virtually tax-exempt. Swiss holding companies are also generally entitled to a refund of the input VAT.

Further, a Swiss acquisition company may benefit from a tax-neutral reorganisation in the sense of the Mergers Act (eg,

a merger with the Swiss target company if required by the financing banks).

Finally, a Swiss holding company may be beneficial in terms of the Swiss dividends withholding tax in the case of a Swiss target. Dividends distributed to a Swiss acquisition company are either not subject to the withholding tax (if the acquisition company holds at least a 20 per cent stake (10 per cent from 1 January 2023) in the Swiss target and the notification procedure is complied with) or the withholding tax is fully refundable (except where old reserves exist or an anti-abuse setup is seen. A foreign acquisition company can request the relief from the 35 per cent dividends withholding tax only if it complies with the requirements under the relevant double tax treaty; generally, residency, beneficial ownership and no abuse (treaty or rule shopping).

The equity capitalisation of a Swiss acquisition company by its direct shareholder is subject to 1 per cent stamp duty (the first 1 million Swiss francs of contributed capital is exempt), whereas an indirect capital contribution (namely, equity funding not by the direct, but the indirect shareholder) would generally not be subject to stamp duty. In the case of a debt-financed acquisition, a Swiss acquisition company with mainly only dividend income may not benefit from tax-deductible interest expenses owing to its lack of taxable income. However, there are certain debt pushdown strategies available, by which interest expenses can be allocated to a Swiss target company and set off against its taxable income. Swiss thin capitalisation rules principally need to be considered if the acquisition company is funded by shareholder or related party debt (including third-party debt that is secured by shareholders or related parties). Interest on such debt is only tax-deductible if certain debt-to-equity ratios are complied with and the interest does not exceed arm's-length terms. Generally, the debt-financing of investments (shares) is limited to 70 per cent of the fair market value of such investment.

As Switzerland has a broad treaty network, no CFC rules, an attractive income tax regime and usually offers possibilities to structure around potential tax inefficiencies, a Swiss acquisition company is often preferable.

Law stated - 08 August 2022

Company mergers and share exchanges

Are company mergers or share exchanges common forms of acquisition?

An immigration merger (inbound into the Swiss target) is generally possible to the extent that the foreign legislation permits such a merger. An immigration merger could generally be performed in a tax-neutral manner (including for Swiss stamp duty, with an exception in the case of abuse of law). A (tax-neutral) step-up of the income tax values is generally possible in the context of the immigration and in respect of assets that become subject to tax in Switzerland, with the exception of qualifying participations. The stepped-up values subsequently need to be depreciated over time (the applicable timeline depending on the assets, eg, a maximum of 10 years for goodwill) and are subject to capital tax.

Swiss withholding tax may be triggered if the nominal share capital in a Swiss merged entity increases or if reserves subject to Swiss withholding tax are reduced, such as if the merger is done with a company in a loss situation. Considerations for exiting Swiss shareholders are generally taxed like ordinary capital gains except if such considerations are paid by the merged company (taxed like dividends). Swiss individual shareholders holding the shares as private assets are deemed to receive taxable income if they benefit from a higher share capital in the merged company.

A potential alternative to an immigration merger is a quasi-merger as a share-for-share exchange between the acquisition and target companies, whereby the shareholders of the target company are compensated with (new) shares of the acquisition company. A tax-neutral quasi-merger requires that the acquisition company obtains at least 50 per cent of the voting rights of the target and the shareholders obtain at least 50 per cent of the value of the target in new shares of the acquirer (namely, the cash component may not exceed 50 per cent of the value of the target). In the case of a quasi-merger, the target remains a separate entity (as opposed to a statutory merger resulting in just one

entity). In inbound cases, a foreign acquirer would typically set up a Swiss acquisition company, which would then acquire a Swiss target via share-for-share exchange based on the conditions outlined above. In this case, the Swiss acquisition company typically issues new shares to the tendering shareholders of the Swiss target company with a modest nominal share value and a large share issuance premium, which together reflect the market value of the acquired shares. The share premium may be booked and reported for Swiss withholding tax purposes as capital contribution reserves of the Swiss acquisition company, which could later be distributed free of Swiss dividends withholding tax. Such a quasi-merger is exempt from the 1 per cent Swiss stamp duty. Qualifying quasi-mergers with Swiss target companies are in general tax-neutral for the acquisition and target entities. Swiss-resident individual shareholders holding the shares of the target company as private, non-business assets are considered to realise a tax-exempt capital gain (or loss) upon the exchange (share and other consideration, if any). Swiss-resident corporations or individuals holding the shares of the target company as business assets may be able to roll over their tax basis in the target company shares into the shares of the acquisition company, provided the book values are carried on. A merger between the Swiss acquirer and Swiss target within five years would result in a re-qualification of the quasi-merger into a real merger with different tax consequences.

Law stated - 08 August 2022

Tax benefits in issuing stock

Is there a tax benefit to the acquirer in issuing stock as consideration rather than cash?

For a Swiss acquisition company, the issuance of stock as consideration may be beneficial if the requirements for a tax-neutral quasi-merger are met. In particular, at least 50 per cent of the fair market value of the Swiss target are compensated with (newly issued) shares of the acquisition company. Such a quasi-merger is preferential for the Swiss acquirer, as the contribution of the target shares will generally not trigger stamp duty, the acquisition of remaining target shares will benefit from a Swiss securities transfer tax exemption and the Swiss acquisition company can create capital contribution reserves that may be later distributed without Swiss dividends withholding tax and without Swiss income tax for Swiss-resident individuals holding the shares as private assets. For Swiss sellers holding the shares in the target as business assets, the stock consideration may result in a deferral of the capital gain or rollover of the tax basis in the target shares.

Law stated - 08 August 2022

Transaction taxes

Are documentary taxes payable on the acquisition of stock or business assets and, if so, what are the rates and who is accountable? Are any other transaction taxes payable?

The acquisition of stock is generally subject to securities transfer tax of up to 0.15 per cent on Swiss securities and up to 0.3 per cent on foreign securities, provided a qualifying Swiss securities dealer is involved in the transaction either as a party or as an intermediary. The term 'Swiss securities dealer' includes not only professional securities traders, banks, brokers, asset managers and the like, but also all Swiss-resident corporate entities whose assets consist, as per the last annual balance sheet, of taxable securities in excess of 10 million Swiss francs. The tax liability is divided between the parties to the transaction, including the intermediary, as follows:

- if a registered security dealer is involved as an intermediary, the security dealer must pay half of the burden for each party to the transaction that is not itself a registered securities dealer or exempt party (eg, a foreign listed company); or
- if a registered security dealer is a party to the transaction, the security dealer must pay half of the burden for itself

and half of the burden for its counterparty that is not a registered securities dealer or exempt party. The parties can also agree a different commercial allocation in the share purchase agreement.

In a decision of 23 November 2021 (A-5038/2020), the Swiss Federal Administrative Court ruled that the M&A adviser, whose role is to provide guidance to shareholders intending to sell their shares along the entire deal and who is processing the transaction, qualifies as an intermediary subject to securities transfer tax. For its assessment of a qualified intermediary, the court considered, among others, the following:

- searching for suitable buyers for the clients' companies;
- preparation of sales documentation;
- contacting prospective buyers;
- organisation of meetings with potential buyers; and
- assistance in the negotiation of the sales contracts.

The court deemed these circumstantial aspects sufficient for an active role as an 'investment adviser' to influence potential buyers to enter into a purchase contract. The M&A adviser has a causal influence on the conclusion of the contract and thus shall qualify as a securities dealer, which brings such adviser into the scope of securities transfer tax. The ruling has led to some uncertainty among potentially affected M&A advisory companies, since the securities transfer tax adds costs of the transaction and results in additional reporting obligations for the securities dealer.

Certain restructuring exemptions may apply in the case of transfers of taxable securities, but rarely in the case of a transaction between unrelated parties. Swiss or foreign securities, such as bonds, shares or other securities that are sold in an asset deal, may also be subject to securities transfer tax if a Swiss securities dealer is a party or an intermediary in the transaction.

Further, most cantons or communes impose a real estate transfer tax upon a transfer of real estate in an asset deal. An acquisition of a majority of shares in a real estate company would also be subject to a (cantonal or communal) real estate transfer tax in the majority of cantons. The liability (acquirer or seller) differs per canton; no tax is levied in the case of a tax-neutral reorganisation or merger. In addition, the transfer of real estate may be subject to real estate register and notary fees.

In the case of an asset deal, the transfer of such assets is generally subject to a 7.7 per cent (standard rate) or 2.5 per cent (reduced rate for certain assets) VAT, except for assets that are not within the scope of VAT (eg, assets located abroad) or exempt from VAT (eg, receivables or real estate). VAT is generally payable by the transferor, unless the notification procedure applies or the transfer is made to a foreign acquirer (exemption for export of goods; export of services such as IP, which are taxable at the place of the acquirer). The transfer of real estate can be subject to VAT unless the real estate is used only for private purposes.

The VAT liability can in certain cases be fulfilled by applying the notification procedure. This procedure is mandatory if:

- the assets transferred qualify as a taxable supply and both parties are (or become) Swiss VAT taxpayers;
- the VAT amount exceeds 10,000 Swiss francs and the transfer qualifies as a tax-neutral reorganisation or constitutes a transfer of a totality of assets or a part thereof; or
- the VAT amount does not exceed 10,000 Swiss francs, but the assets are transferred intergroup and the transfer qualifies as a tax-neutral reorganisation or constitutes a transfer of a totality of assets or a part thereof.

On a voluntary basis, the procedure may be applied if real estate is transferred or significant interest is proven. As a consequence of the notification procedure, the acquirer steps into the position of the seller in respect of the assets'

VAT-able basis and use for VAT purposes. That is, if the acquirer changes the use of the transferred assets within the respective VAT depreciation period (five years or 20 years for real estate), the acquirer could benefit from an additional input VAT refund or may need to repay the input VAT previously refunded to the seller.

A share deal is exempt from VAT.

Law stated - 08 August 2022

Net operating losses, other tax attributes and insolvency proceedings

Are net operating losses, tax credits or other types of deferred tax asset subject to any limitations after a change of control of the target or in any other circumstances? If not, are there techniques for preserving them? Are acquisitions or reorganisations of bankrupt or insolvent companies subject to any special rules or tax regimes?

Principally, a change in ownership of a Swiss entity in a share deal has no influence on the carry-forward of tax losses; that is, losses from the past seven tax years can be carried forward and set off against the taxable profits of the current period. There are exceptions; for example, if the acquired company has already been brought into liquid form and has no commercial activity anymore. In the case of a financial restructuring or recapitalisation, the tax loss carry-forward is unlimited time-wise. Other tax attributes are principally also not affected by a change of control.

In the case of an asset deal, any tax loss carry-forwards remain with the selling company and may be set off with a gain resulting from the sale. There are principally no special tax rules for acquisitions of bankrupt or insolvent companies. A change of ownership has generally no impact if a Swiss target company qualifies for a special tax regime or is entitled to a partial tax relief (tax holiday).

Law stated - 08 August 2022

Interest relief

Does an acquisition company get interest relief for borrowings to acquire the target? Are there restrictions on deductibility generally or where the lender is foreign, a related party, or both? In particular, are there capitalisation rules that prevent the pushdown of excessive debt?

Interest payments in general are tax-deductible and not subject to Swiss withholding tax at the level of a Swiss acquisition company. However, since there is no tax consolidation or group taxation for income tax purposes, the interest deduction is only tax-efficient to the extent that the acquisition company has its own taxable income. Otherwise, debt pushdown structures or the creation of taxable income at the acquisition company level should be considered.

Interest deduction limitations may apply to related-party debt; that is, debt financing provided by shareholders, related parties or third parties where the debt is secured by related parties. Thin capitalisation rules set a limit for maximum loan amounts by shareholders or related parties that are accepted by Swiss tax authorities. The maximum amount of accepted debt is determined by applying the safe-haven rates (namely, a percentage amount of allowed debt per asset category, such as 100 per cent debt-financing for cash or 70 per cent for participations or IP), which are set out in a circular of the FTA. The maximum permitted debt is measured in percentages of the fair market value of the corporation's assets (which is assumed to be equal to the (tax) book value, unless proven otherwise). Related-party debt exceeding that maximum permitted debt is treated as hidden equity for tax purposes. Such hidden equity is subject to annual capital tax; it is, however, not subject to a 1 per cent stamp duty on equity contributions. Further, interest payments on the hidden equity are treated as constructive dividends; they are subject to 35 per cent Swiss

dividends withholding tax and are not tax-deductible.

To avoid adverse withholding tax consequences, loans to a Swiss acquisition company may be granted interest-free, if this is possible from a lender's perspective. Such an interest-free loan would not – other than a subsequent waiver of interest – trigger stamp duty of 1 per cent on equity contributions. Where the direct shareholder provides debt in excess of the thin capitalisation limitations but benefits from a full dividends withholding tax relief (eg, based on a double tax treaty or as a Swiss-resident corporation holding at least 20 per cent in the Swiss target), the withholding tax cash-out could be avoided by a proactive, timely notification of the hidden dividend distribution.

In addition, interest on related-party debt must comply with arm's-length terms. Circulars published annually by the FTA set out the maximum safe-haven interest rates that may be paid by a Swiss company on shareholder or related-party loans, generally with higher rates if the loans are denominated in foreign (non-Swiss francs) currency. If the debt does not qualify as hidden equity and the safe-haven interest rates are complied with, the interest is generally tax-deductible. Higher interest rates may be accepted if the arm's-length character or a third-party test can be evidenced. This question can be addressed in a tax ruling to obtain certainty.

With respect to interest withholding tax, the Swiss 10/20/100 non-bank rules need to be considered if a bond is issued by a Swiss acquisition company or a collective fundraising scheme is used. In this case, withholding tax of 35 per cent is levied on interest due that may be refundable based on Swiss domestic law for a Swiss lender or depending on the applicable double tax treaty for a foreign lender. A loan facility qualifies as a collective fundraising where the aggregate number of non-bank lenders (including sub-participations) to a Swiss company under a facility agreement exceeds 10 (if granted under equal conditions) or 20 (if granted under different conditions; eg, various tranches or facilities), and the total amount of such debt exceeds 500,000 Swiss francs. Cash pooling does not amount to collective fundraising unless the aggregate number of non-bank lenders exceeds 100 and the total amount of such debt exceeds 5 million Swiss francs. The Swiss withholding tax exposure under the 10/20/100 non-bank rules may be mitigated under certain conditions if acquisition debt is granted to a foreign entity and lent on to a Swiss subsidiary (acquirer). The borrowing via a foreign subsidiary of a Swiss parent could, however, trigger Swiss interest withholding tax if the collective fundraising criteria are met by the foreign borrowing subsidiary, the Swiss parent guarantees the debt and the borrowed funds are lent on to a Swiss group company (generally, there is an exemption if a subsidiary does not lend to a Swiss group company an amount exceeding the foreign group company's total equity). It may be possible that the Swiss withholding tax (WHT) system will be reformed in the near future and in principle, no WHT will be levied on domestic interest anymore.

Further, federal and cantonal Swiss withholding taxes on interest may arise if a loan is directly or indirectly secured by Swiss real estate; the tax rate depends on the location of the real estate. Many Swiss double tax treaties reduce such withholding taxes to zero.

The tax-efficient pushdown of the acquisition debt on the target level is not easy to achieve, as Switzerland has no consolidation for income tax purposes. A debt pushdown of acquisition debt by merging the acquisition company with the target company is generally viewed as abusive from a tax perspective by the Swiss tax authorities if the acquisition company itself had no taxable income to set off the interest expenses. Debt pushdown can, typically in current practice, be better achieved by strategic acquirers (Swiss operating acquisition companies with their own taxable income) or by careful structuring. The distribution of debt-financed dividends (leveraged dividends), whereby the target company resolves a dividend that is not directly settled in cash but left outstanding as an interest-bearing downstream loan by the shareholder or settled by the assumption of external acquisition debt and the allocation of interest expenses to the target company, may be possible, always within the limitations of the thin capitalisation rules. In addition, debt-financed intergroup acquisitions, such as the acquisition of shares or assets from group companies by the Swiss target against an interest-bearing loan may be possible.

Law stated - 08 August 2022

Protections for acquisitions

What forms of protection are generally sought for stock and business asset acquisitions? How are they documented? How are any payments made following a claim under a warranty or indemnity treated from a tax perspective? Are they subject to withholding taxes or taxable in the hands of the recipient? Is tax indemnity insurance common in your jurisdiction?

Tax risks are usually addressed in the asset purchase agreement (APA) or share purchase agreement (SPA) in representations and warranties and a tax indemnity clause.

Historic tax risks remain with the target company in the case of a share deal. A tax due diligence and sufficient SPA protection for identified risks are thus highly recommended to an acquirer.

Typically, an acquirer asks for tax representations and warranties to be granted by the seller in the SPA for pre-closing periods to obtain general protection relating to tax compliance status, tax registrations, tax filings and tax payments, as well as certain tax attributes and the absence of blocking periods, old reserves for withholding tax purposes, foreign permanent establishments, or reversals of past depreciation of participations or loans. Tax indemnities are either granted for the pre-closing period or until a locked-box date (depending on the purchase price mechanism) and either broadly for all taxes payable that are not already reflected in the purchase price (as debt) or only for specific risks identified. The goal of those clauses is to shift the liability for tax obligations originating from pre-closing periods back to the seller. Claims under a warranty or indemnity should principally be considered as a purchase price reduction between the acquirer and seller and would be income tax-neutral and as such not subject to withholding tax. Direct claims by the target against the seller could result in taxable income. Even if the payment were structured as an income tax-neutral contribution via the purchaser, 1 per cent stamp duty on the contribution into the Swiss target could be triggered. Thus, both should be avoided and the indemnification should be made between the acquirer and seller.

An acquirer in an asset deal can be liable for certain taxes, such as VAT, customs and social security contributions and potentially payroll taxes, and should seek protection in the APA. Claims of the acquirer against the seller would usually be considered a purchase price reduction and may reduce the capital gain for the seller and step-up (depreciation basis) for the acquirer. No withholding taxes should arise on such payments, but transfer taxes and VAT may need to be adjusted accordingly.

It is becoming increasingly popular in Switzerland to use warranty and indemnity insurance to cover tax risks in transactions.

Law stated - 08 August 2022

POST-ACQUISITION PLANNING

Restructuring

What post-acquisition restructuring, if any, is typically carried out and why?

A post-acquisition merger of the (Swiss) acquisition vehicle and the acquired company is often contemplated and can generally be done on a tax-neutral basis. The benefit is the integration of the acquired business by combination with the existing business of the acquirer in Switzerland, the reduction of legal entities and the faster access to operating cashflow in the target entity irrespective of distributable reserves. The latter is often requested from financing banks, as the bank debt is then on the level of the target company and directly secured by the target's assets.

From a tax perspective, such a merger can have the benefit of offsetting the taxable profits of the operative target business with interest expenses from the acquisition financing. However, if the acquisition company does not have its

own taxable income, such offsetting is usually not permitted by the Swiss tax authorities but is seen as abusive after a merger (debt pushdown). Even if this tax benefit is not achieved, the merger can be done for the abovementioned reasons.

If the Swiss target entity has been acquired from Swiss-resident individuals and the indirect partial liquidation rules apply, a merger with the acquisition company within five years after the transaction would trigger income taxation for the sellers as if the target entity had distributed its pre-sale reserves to the sellers. Depending on the amount of taxes triggered and whether the acquirer was liable according to the SPA for such taxes towards the sellers, no merger with the acquisition company should be performed during five years after the transaction; side-stream mergers or mergers within the target group, in contrast, should generally not trigger the indirect partial liquidation taxation.

A merger of the Swiss acquirer with a Swiss target that had been held by non-Swiss shareholders or shareholders not being entitled to a full withholding tax reduction on dividends from the Swiss target should be carefully analysed, as it could trigger non-refundable Swiss withholding taxes on the amount of the purchase price less share capital and potential capital contribution reserves (liquidation by proxy).

Additionally, intragroup transactions in the acquired target group may be used in certain cases to generate distributable reserves (eg, an intragroup transfer of a participation to another group company at fair market value with the potential capital gain being subject to the participation deduction if the required conditions are fulfilled), which may then be used to upstream cash to the acquisition company and further.

Law stated - 08 August 2022

Spin-offs

Can tax-neutral spin-offs of businesses be executed and, if so, can the net operating losses of the spun-off business be preserved? Is it possible to achieve a spin-off without triggering transfer taxes?

A tax-neutral demerger of a Swiss company may be carried out in the form of split-up or spin-off and is principally tax-neutral (namely, no taxable realisation of transferred hidden reserves) under the following cumulative conditions:

- the companies continue to be subject to tax liability in Switzerland;
- one or more business or business units are transferred;
- the transfer is done at (tax) book value, against sufficient equity; and
- both Swiss entities continue their businesses after the demerger.

Under these conditions, a demerger also does not trigger any transfer taxes, such as securities transfer tax or real estate transfer tax. The payment of value added tax is substituted by a notification procedure. Registration fees or notary fees upon the transfer of real estate may still apply. Because the demerger is not subject to any blocking period, it is often used by sellers as a pre-deal restructuring or carve-out to transfer a business unit to a new entity and sell it through a share deal. The demerger can be structured in different ways; for example, as a direct demerger (split of a legal entity) under the Merger Act or as a contribution of the business unit into a new subsidiary and distribution of the shares in the new subsidiary to the shareholders. To be neutral for stamp duty purposes, certain restrictions regarding the maximum amount of newly created share capital at the level of the new entity need to be considered.

Other ways to achieve, under certain conditions, a tax-neutral spin-off include the transfer of (partial) business or operating fixed assets to a Swiss subsidiary, Swiss parent or sister company. However, this is always subject to a five-year blocking period. The transfer of stock of a minimum of 10 per cent to a Swiss or foreign subsidiary can generally be done tax neutrally and is not subject to a blocking period.

Usually, a tax loss carry-forward can be transferred with the tax-neutral transfer of a (partial) business unit if and insofar as the loss is related to the business activity of the transferred unit. Otherwise, the tax loss carry-forward remains with the transferor. Thus, it is recommended to confirm the allocation of the tax loss carry-forwards in a tax ruling with the competent tax authorities.

Law stated - 08 August 2022

Migration of residence

Is it possible to migrate the residence of the acquisition company or target company from your jurisdiction without tax consequences?

In general, a migration of a company from Switzerland is considered a deemed liquidation, triggering the same tax consequences as a statutory liquidation process. In particular, hidden reserves (fair market value less tax book values of the business of the company) would be subject to income tax at the applicable tax rate of the Swiss company. Further, the liquidation surplus (net assets at fair market value, minus nominal share capital and recognised capital contribution reserves) would be subject to a 35 per cent dividend withholding tax: depending on the domicile of the shareholders of the Swiss entity and the applicable double tax treaties, the withholding tax may be notified instead of paid or partially or fully refunded. No income tax will generally be due if the business activity of the Swiss entity is continued upon the migration through a permanent establishment in Switzerland and the book values are carried on and remain subject to Swiss taxation based on the international allocation between the foreign headquarters and the Swiss permanent establishment.

Law stated - 08 August 2022

Interest and dividend payments

Are interest and dividend payments made out of your jurisdiction subject to withholding taxes and, if so, at what rates? Are there domestic exemptions from these withholdings or are they treaty-dependent?

Dividends paid by a Swiss company are generally subject to a withholding tax at a rate of 35 per cent.

However, this withholding tax may be fully reclaimed by a Swiss tax-resident shareholder; for a Swiss corporate shareholder holding at least 20 per cent in the Swiss company, the payment may be substituted with a notification to the FTA (to avoid a temporary cash-out). This participation rate will be lowered to 10 per cent as from 1 January 2023.

Whereas dividends withholding tax is meant to be a final burden to non-Swiss-resident beneficiaries, full or partial relief may be available for them under an applicable Swiss double taxation treaty. Further, in a cross-border context, the notification procedure for dividends paid to a qualifying corporate shareholder (owning at least 10 per cent of the equity of the distributing Swiss entity or the percentage required under the applicable tax treaty and meeting all further conditions for treaty benefits) may be applicable. It requires an advance filing of a specific application form with the FTA and the demonstration that the foreign beneficiary fulfils all conditions for the requested tax-treaty benefits.

Relief in respect of the dividends withholding tax may be denied to Swiss or foreign shareholders entitled to a full or partial treaty relief under the liquidation by proxy or old reserves practices if the sellers in a share deal were not themselves entitled to at least the same relief in respect of the dividends withholding tax at the time of the sale (namely, as Swiss residents or pursuant to a double tax treaty). The liquidation by proxy practice applies if the target is legally liquidated, merged or fully or partially factually liquidated by the acquirer. In that case, relief from the withholding tax may be denied to the new shareholders in the same amount as would have been denied to the former shareholders in the amount of the difference between the target's fair market value (namely, purchase price paid) and the target's

capital contribution reserves and share capital. The old reserves practice is a milder version of the liquidation by proxy practice and also applies to situations where the previous shareholders were not entitled to a full refund or relief from the withholding tax. Relief from the 35 per cent withholding tax is denied to the new shareholder on any dividend distribution up to the amount of old reserves. The amount of old reserves is the lower of the target's legally distributable reserves and the non-operating assets of the target on a consolidated basis (namely, the target and all consolidated companies) at the time of the sale.

The repayment of qualifying capital contribution reserves or share capital is generally not subject to dividends withholding tax. The Swiss tax reform introduced a new restriction regarding the distribution of qualifying capital contribution reserves by Swiss listed companies. Since 1 January 2020, a Swiss listed company wishing to distribute a dividend out of capital contribution reserves is required to distribute at a minimum an equal amount of dividend out of other reserves (retained earnings), subject to the availability of such other reserves. This rule should restrict the possibility to distribute only capital contribution reserves, which are not subject to Swiss withholding tax and not subject to income tax at the level of Swiss individual shareholders. Exemptions apply for foreign capital contribution reserves of Swiss listed companies that are created; for example, upon an inversion or quasi merger.

On interest payments, there is generally no withholding tax levied in Switzerland, with the exception of interest payments on qualifying bonds or collective fundraisings (which may, however, be abolished in the future) and on interest paid on bank deposits (with the Swiss entity qualifying as a bank under the Swiss withholding tax provisions) exceeding a defined minimum amount. Further, withholding tax may apply if the loan is secured by Swiss real estate. Dividends withholding tax may apply on intercompany interest if the interest qualifies as hidden dividend distribution (if the Swiss entity is thinly capitalised or the interest exceeds the arm's-length amount).

Law stated - 08 August 2022

Tax-efficient extraction of profits

What other tax-efficient means are adopted for extracting profits from your jurisdiction?

In addition to dividends and interest, other intercompany payments could be considered to extract profit from the Swiss entity. Such payments need to comply with arm's-length terms to be accepted from a tax perspective. Switzerland usually follows the Organisation for Economic Co-operation and Development transfer pricing guidelines in this respect.

There is no Swiss withholding tax on royalties or management fees. Accordingly, it would be possible to extract profits by such payments provided they are at arm's length.

Law stated - 08 August 2022

DISPOSALS (FROM THE SELLER'S PERSPECTIVE)

Disposal methods

How are disposals most commonly carried out – a disposal of the business assets, the stock in the local company or stock in the foreign holding company?

Usually, the seller has an interest to carry out the disposal by selling the directly held stock of the company or of the foreign top company. For corporate sellers, provided the one-year minimum holding period requirement is fulfilled and the stock of a minimum of 10 per cent is sold, capital gains are virtually tax-exempt (participation deduction).

Individual businesses benefit from a partial tax exemption under the same conditions (generally, subject to cantonal differences). For private individual sellers, capital gains are generally tax-exempt, with a few exceptions. The most common exception is indirect partial liquidation: in the case of Swiss resident private individuals selling (alone or

together) a stock of a minimum of 20 per cent to a corporate or individual business acquirer, under certain circumstances, the sale can qualify as indirect partial liquidation. The tax-free capital gains of the sellers will then retroactively requalify as taxable investment income. This requalification may take place if, at the time of the sale, the target company has distributable reserves covered by non-operationally required assets and, within a five-year period following the acquisition, distributes such reserves to the new (corporate or business) shareholder (to the extent that certain additional conditions are met). The sellers would typically insist on an indemnity clause in the share purchase agreement to shelter themselves against this potential risk, which is post-sale in the control of the acquirer.

In contrast, the sale on a lower level or an asset deal would require the repatriation of proceeds, which is subject to dividend taxation for Swiss resident individuals (fully taxable income or privileged taxation in the case of a shareholding of a minimum of 10 per cent).

To the extent that the foreign holding company is in a jurisdiction with a favourable double tax treaty with Switzerland, the sale of shares by the foreign holding company followed by a dividend distribution to Swiss corporate shareholders can also be a tax-efficient structure. Provided the dividends are not subject to foreign withholding tax, the Swiss corporate shareholder can benefit from the participation deduction on dividends if its shareholding in the foreign holding is either at least 10 per cent or has a fair market value of at least 1 million Swiss francs (no minimum holding period applies to dividends).

An asset deal is generally less beneficial for a seller as it triggers a taxable gain. It may be considered if the seller has a tax loss carry-forward that would otherwise be forfeited, the seller can make use of a deferral (re-investment relief for certain operating assets) or the seller benefits from low or privileged taxation and receives a higher purchase price from the acquirer owing to the acquirer's step-up and depreciation.

Law stated - 08 August 2022

Disposals of stock

Where the disposal is of stock in the local company by a non-resident company, will gains on disposal be exempt from tax? Might a disposal of stock in a foreign holding company trigger taxes in the local company in your jurisdiction? Are there special rules dealing with the disposal of stock in real-property, energy and natural-resource companies?

Based on Swiss unilateral law, irrespective of a double tax treaty, Switzerland does not impose tax on the gains of the disposal of stock in a local company by a non-resident seller (namely, a foreign seller without permanent establishment and without place of management in Switzerland).

One important exception applies at the cantonal or communal level for the direct or indirect sale of a majority of stock in a real estate company (namely, a company that predominantly owns Swiss real estate for investment purposes). The exact qualification criteria for a real estate company vary between the cantons. Such transactions are put on an equal footing with the sale of real estate assets. In a number of double tax treaties, the taxation right of Switzerland in respect of such transactions may be restricted; for example, currently, under the double tax treaties with Denmark, Germany and Luxembourg. However, the majority of Swiss tax treaties reserve the right of the contracting state in which the real property is located to tax indirect gains upon the sale of company shares if more than 50 per cent of the company's assets comprise local real property. Also, certain tax authorities have recently started to interpret the provisions of the aforementioned double tax treaties (in the case at hand with Luxembourg) in a more restrictive way and tend to nevertheless levy real estate gains tax despite provisions in the double tax treaties supposedly limiting the taxation rights of Switzerland (expected court cases in future will bring clarity on this).

With regard to energy and natural-resource companies, there are no special tax rules in Switzerland.

Law stated - 08 August 2022

Mitigating and deferring tax

If a gain is taxable on the disposal either of the shares in the local company or of the business assets by the local company, are there any methods for deferring or mitigating the tax?

A sale of all shares in the local company would be either tax-exempt (in the case of a Swiss individual holding the shares as private assets and not qualifying as a securities trade; eg, due to debt-financed shareholdings or frequent trading) or virtually exempt, subject to the requirements of the participation deduction, at the level of a Swiss tax-resident company.

Business-required long-term assets can qualify for a deferral or rollover relief to the extent that the proceeds are re-invested within a certain time frame in the acquisition of other long-term assets. The sale proceeds of real estate cannot be rolled over to movable long-term assets.

Law stated - 08 August 2022

UPDATE AND TRENDS

Key developments of the past year

Are there any emerging trends or hot topics relating to tax on inbound investment?

WHT and securities transfer tax reform

On 14 April 2021, the Federal Council published the 'Dispatch on an Amendment to the Federal Act on Withholding Tax (Strengthening the Debt Capital Market)'. In principle, this reform bill aims to largely abolish the 35 per cent withholding tax (WHT) currently levied on interest payments on a domestic bond and, as an accompanying measure, to abolish the turnover tax on Swiss bonds. The reform proposal is to be welcomed due to the undisputed positive incentives for the Swiss debt capital and corporate financing markets.

On 17 December 2021, the Swiss parliament passed an amendment to the Federal Act on Withholding Tax and the Federal Act on Stamp Duties. The decree sets forth that only newly issued bonds shall profit from no WHT on interest. Domestic bonds already issued at the time of the reform's entry into force shall remain subject to WHT. The same applies to interest on customer deposits of Swiss resident individuals. In contrast to the Federal Council's proposal, however, WHT will also be abolished on interest on bonds held indirectly via a Swiss investment fund, provided that the interest income is reported separately. Further, the reform sets forth that the brokerage, as well as the purchase and sale of participations of 10 per cent or more in a Swiss or foreign company's share capital, shall be exempt from securities transfer tax if the participation qualifies as fixed assets as defined in article 960d of the Code of Obligations. On 5 April 2022, a referendum against the reform was submitted. The vote on the reform will take place in autumn 2022. The entry into force of the Swiss federal WHT and securities transfer tax reform, if adopted, is not expected before the beginning of 2023.

Update – reform of corporate law

From 1 January 2023, the revision of the stock corporate law reform will enter into force, which will provide more flexible formation and capital regulations to stock corporations. The bill includes, among other things, new provisions for more flexible incorporation and capital regulations, the introduction of gender guidelines, and stricter transparency rules for companies active in the extraction of raw materials sector. Relevant tax topics related to the reform are, in particular:

- the introduction of a new legal institution, the 'capital band'. The board of directors of a company will be authorised to increase or decrease the capital within a pre-defined range within a maximum period of five years. As for tax aspects, this means that capital contribution reserves that may be repaid tax-free at a later stage may only be created at the end of the capital band, and stamp issuance tax will only apply at that time on the net amount (namely, after five years at the latest);
- the reform explicitly allows interim dividends distributed from profits of the current financial year; and
- the companies will be able to have their share capital and capital contribution reserves in certain foreign currencies (eg, US dollars or euros), a new circular dealing with the resulting currency exchange differences is expected in 2022.

This extensive revision of the stock corporate law finally concludes a process that began more than 10 years ago.

Circular No. 5a regarding restructurings

In Switzerland, the Federal Tax Authority (FTA) publishes the tax authorities' practice in 'circular letters' to harmonise the implementation of federal tax law by the 26 Swiss cantons and the practice of the cantonal tax authorities.








The new edition of Circular No. 5 (now No. 5a) of the FTA concerning restructurings is the most comprehensive and probably the most important practice instruction of the FTA. Its comprehensive revision was overdue due to numerous changes in the law, such as the introduction of the capital contribution principle allowing for tax-free repayment of paid-in capital. Besides the amendments to the law, it was also necessary to consider case law that has been developed by the Federal Supreme Court; for example, the leading decision of the Federal Supreme Court on the demerger of holding companies (DFT 2C_34/2018, dated 11 March 2019), according to which a directly or indirectly controlled operating entity may be considered a business unit. The FTA also clarified certain topics and made changes to its administrative practice on some points; for example, Circular No. 5a now explicitly sets forth that tax-neutral spin-offs (in the meaning of transfer to a subsidiary) and relief on the replacements of participations require a 10 per cent participation quota (instead of 20 per cent). Further, tax consequences arising from partial tax-neutral restructuring, and no levying of the stamp issuance tax of 1 per cent in the case of a violation of a lock-up period, were clarified. The publication of Circular No. 5a was preceded by an extensive consultation procedure where tax experts and industry submitted contributions and suggestions, which the FTA, in numerous cases, implemented in said Circular.

Implication of international tax developments – OECD Pillars 1 and 2

In January 2022, the Federal Council decided to implement the minimum tax agreed by the Organisation for Economic Co-operation and Development (OECD) and the Group of 20 (G20) countries by creating a new constitutional basis to provide legal certainty for affected companies. Until implementation, the Federal Council intends to issue a temporary ordinance that, from 1 January 2024, will implement the minimum tax rate of 15 per cent for multinational companies with turnover of more than €750 million as suggested by the OECD. The ordinance is based on a change of the federal constitution, which is subject to a potential referendum. Subsequently, a legal basis shall be prepared in an ordinary legislative procedure and the ordinance will be replaced. The Federal Council opened a consultation on the implementation of the OECD and G20 minimum tax. Initial rough estimates suggest short-term additional fiscal income of 1 to 2.5 billion Swiss francs due to the minimum tax rate.

Law stated - 08 August 2022

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