Switzerland Rejects Corporate Tax Reform III in Public Vote February 13, 2017

With a majority of 59.1%, Swiss voters rejected the Corporate Tax Reform III (CTR III) in a public vote held on February 12, 2017. CTR III, which was the result of a long and complex political process, would have abolished current existing tax regimes, such as the rules for holding or mixed companies. At the same time, the reform would have introduced new internationally accepted measures such as the patent box, research and development (R&D) incentives, notional interest deduction, and basis step-up.

The negative vote raises a number of questions on the future tax landscape for companies in Switzerland and abroad, especially concerning the immediate impact on Swiss taxpayers. At a minimum, the 'no' vote means that the current tax legislation and tax rules remain in place and that Swiss taxpayers will not face any immediate, unanticipated changes.

Nevertheless, considering the worldwide debate and recent developments on taxation, pressure will remain on Switzerland to abolish its current tax regimes, so the need for reform remains undisputed by all parties and the Federal Council will have to work out a new reform proposal as quickly as possible. However, it is clear that the reform will not be ready to take effect in 2019 as originally planned. Instead, there will likely be a delay of two to three years.

Nevertheless Switzerland remains a business friendly location, offering a highly skilled workforce, excellent infrastructure, political stability and last but not least a competitive and attractive tax system. We at PwC Switzerland will continue to observe the future reform developments and our engagement to help create a well-balanced reform that reaches its political goals and further promotes the business location Switzerland.

In detail

CTR III, which was triggered by the EU challenging certain Swiss tax regimes, was intended to bring about substantial changes in the Swiss tax landscape in response to international pressure, tax developments, and evolving policy standards.

The process really began when the Swiss Federal Council and the EU on October 14, 2014, reached an agreement to modify the current corporate tax system in Switzerland. They agreed that Switzerland would work towards abolition of certain tax regimes – the rules regarding the cantonal taxation of holding, domicile, and mixed companies and, with regard to direct federal tax, would eliminate the principal company allocation and the tax rules for so-called finance branches.

The need for reform is undisputed, even among CTR III opponents. The real debate and actual reason for the 'no' vote was not the fact of a reform itself, but rather disagreements on the type and scope of the new measures envisaged. In light of the above agreement with the EU, it is widely expected that a new proposal will be developed as quickly as possible. However, the development of such a proposal is a complex and time consuming matter, and many stakeholders must be involved in the process. The possible timing for a new reform proposal is unclear at this time; even if the development is pushed forward with the highest priority, it could take an additional two to three years.

Rejection of CTR III concerns 'only' legislation at the federal level, i.e. the laws regarding direct federal tax and the harmonization of cantonal taxes, governing which measures the cantons are allowed to offer. The cantons, however, remain free to make

Let's talk

For a deeper discussion of how this might affect your business, please contact:

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unilateral changes to their tax laws within the frame set by the tax harmonization law. Cantons have full discretion to decide their corporate income tax rates; therefore, it is still very possible that the "no" vote may accelerate the cantons' decisions. Some of the cantons may take unilateral measures and reduce their corporate tax rates, even with the CTR III rejection, to boost their international competitiveness.

For example, on May 20, 2016, the Canton of Vaud voted for a significant reduction of the tax rate from 22.1% to 13.8%, effective January 1, 2019. This vote was in conjunction with abolition of the cantonal taxation regimes for holding, domicile, and mixed companies. The unchanged provisions in the Federal Harmonisation Law concerning the cantonal taxation regimes are self-executing and apply directly also to the absence of respective cantonal norms. Thus, the Vaud tax law changes on abolishment of tax regimes is overruled by the existing Federal Harmonisation Law. The Vaud cantonal bill voted for on March 20, 2016 foresees that in the event of a rejection of CTR III at national level, the Vaud government must come up with a proposition to rebalance the reform at cantonal level within 6 months. It may be the case that the approved 13.8% Vaud tax rate could eventually be increased again. In any case, several cantons are already offering very attractive ordinary tax rates, including Lucerne (12.3%), Nidwalden and Obwalden (12.7%), and Appenzell Ausserrhoden (13.0%). The tax rate in other cantons, such as Zug (14.6%) and Schaffhausen (16.04%), is not much higher.

Observations: Acknowledging the fact that many Swiss taxpayers are uncertain as a result of the 'no' vote, we expect the Federal Council and political stakeholders to quickly develop a new proposal that also can be implemented as quickly as possible. In terms of content, we expect the new package to bear many similarities to the rejected CTR III, but will also support and help maintain Switzerland's attractiveness as a business location that is compliant with internationally accepted standards.

Even through this period of a new reform package development, Switzerland maintains its advantages and benefits as one of the most attractive and competitive business and tax locations, particularly in those cantons where the corporate income tax is already at a very competitive level.

Combined with the international developments calling for minimum tax rates and imposing subject-to-tax tests in certain situations, the introduction of new anti-abuse rules in many jurisdictions, and the trend towards increasing transparency, the current Swiss tax environment already offers very attractive opportunities, even if the current "tax regimes" that remain applicable might in fact no longer be applied by some taxpayers due to the international pressure.

The current practice regarding tax-free disclosure of hidden reserves, which were not previously liable for taxation (so-called step-up practice) also could help companies currently taxed under a '"preferential regime' in certain high-tax cantons obtain temporary relief to bridge the period until a new reform may be enacted. This practice would be relevant for companies that, due to international pressure, find themselves forced to relinquish their previous tax advantages prematurely on a voluntary basis.

The takeaway

Even with the rejection of the CTR III, Switzerland remains a business friendly location, offering a highly skilled workforce, excellent infrastructure, political stability, and a competitive and attractive tax system. PwC Switzerland will continue to monitor future reform developments and will work to help create a well-balanced reform that reaches its political goals and further promotes Switzerland as a business location.

In light of this new situation, taxpayers doing business in Switzerland should carry out an in-depth analysis of new, alternative strategies for action, such as voluntary exit from tax regimes with a cantonal step-up, the transfer of functions and operations to another canton, or other international options. This will allow such taxpayers to be prepared for future changes, be aware of the strategic alternatives and their advantages and disadvantages, and make well informed, timely decisions. We at PwC will be happy to continue working with you through this process, so that you and your organisation are well prepared to tackle the challenges lying ahead in the world of taxes.