Switzerland publishes recommendations for new corporate tax proposal 17

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In brief

After rejection by popular vote of the Swiss corporate tax reform III (CTR III) package in February 2017, a Swiss governmental working group comprised of federal and cantonal members (the steering body) has been working on a revised package (tax proposal 17).

The steering body on June 1, 2017, published its recommended contents for tax proposal 17. The Federal Council now will consider the draft proposal and is expected to publish a final proposal for consultation by end of June 2017. Thereafter, parlamentary discussions are expected to start in spring 2018 and entry into force is expected to take effect January 1, 2020.

In detail

Over the past few months, following the February 'no-vote' on CTR III, the steering body held multiple meetings and workshops with various stakeholders on tax proposal 17. The draft proposal incorporates the essence of these discussions and is designed as a recommendation to the Swiss Federal Council, which will craft the final proposal. One of the key objectives is to maintain Switzerland as an attractive tax and business location.

Tax proposal 17 is comparable to CTR III. However, the provisions of tax proposal 17 are generally narrower than the ones included in CTR III. Also, some additional elements have been added to allow a political compromise.

The steering body recommends the following core elements:

- Eliminating current special tax regimes (holding, mixed, principal, and current finance branch notional interest deduction (NID) regimes)
- Creating the following new cantonal regimes:
  - Patent box: introduction of a mandatory patent box in accordance with the Organization for Co-operation and Development (OECD) standard that follows the modified nexus approach
  - Research and development (R&D) deductions: additional deduction for R&D costs at the cantonal level up to 50% of actual costs (focused primarily on salaries)
  - Maximum benefit: combined cantonal tax relief arising from the new patent box and R&D deductions may not exceed 70% of taxable profit
- Implementing step-up measures included in CTR III, which mainly are designed to ensure a smooth transition following elimination of the current tax regimes.
- Introducing additional measures that generally would not be of major importance to multinational entities, such as individual tax measures and provisions regarding the inter-Swiss financing mechanism of the tax proposal.

The above recommendations for the new package reflect the political discussions with various stakeholders; several of the left-wing party's requests have been taken into account. The general goal is for all parties to agree during the upcoming formal consultation process and parliamentary discussions to avoid a request for another public vote.

Let's talk

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

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Important additional aspects

Notional interest deduction

While the new proposal would eliminate the NID, there are ongoing political discussions on this topic and it is unclear what the final result will be. There also are ongoing discussions regarding the potential introduction of a grandfathering clause for existing NID structures, such as a transition period of up to five years that takes into consideration international developments at the European Union (EU) and OECD level.

Another pending discussion regarding whether an NID concept may be considered or introduced subsequently as a separate stand-alone bill. Consequently, even if the NID is eliminated under the final version of tax proposal 17 following the recommendation of the steering committee, there still may be interim or long-term solutions or a separate bill.

Cantonal tax rate reductions and implementation

The goal is for the cantons to disclose their plans for cantonal implementation in parallel to the federal discussion mentioned above. This disclosure would increase transparency of the proposal and acceptance of the overall tax reform to be effective January 1, 2020. Several cantons have confirmed they plan to reduce the cantonal tax rate.

In essence, a combined federal and cantonal tax rate of 12% to 14% would apply in many cantons — e.g., Lucerne, Zug, Schaffhausen, Basel, Geneva, and Vaud, with a higher effective tax rate (ETR) of 16% to 18.5% in the higher tax cantons, such as Zurich and Berne. The Canton of Zug on June 1, 2017, released a press statement reconfirming its plan to have an ETR of roughly 12%.

The takeaway

The Federal Council will decide on the previously mentioned draft proposals later this month and publish its final proposal by the end of June 2017. The Federal Department of Finance then will prepare a consultation draft for parliamentary discussion, with targets of final parliamentary vote in spring 2018 and an effective date of January 1, 2020. Simultaneously, the cantons will continue with cantonal implementation so that both federal and cantonal tax reforms would be effective January 1, 2020.

Overall, Switzerland will remain very competitive with a standard tax rate of 12% to 14% total ETR in most cantons and retain a highly attractive business location with business advantages such as qualified talents and labor, geographic location, flexible labor law, service orientation of tax and general administration, and quality of life.

Considering non-Swiss developments such as the EU anti-tax-avoidance directives and hybrid mismatch legislation, interest and royalty limitations, EU developments regarding harmful tax practices, and EU black list discussions, the use of special low-rate regimes will become even more restricted in the future. Thus, Switzerland is well positioned by offering low headline tax rates combined with other location advantages.