
IFA London

Service Permanent Establishments / Switzerland

Martin Busenhart

walderwyss attorneys at law

Service Permanent Establishment Swiss Domestic Law (1/2)

Service PE in Switzerland:

In general, the Service permanent establishments (PE) has not led to discussions in Switzerland (Possible reasons: low CIT burden, tax-rulings, establishments of branches and subsidiaries with regard to activities of a certain importance also for practical reasons)

The Term “Permanent Establishment” under Swiss Domestic Law:

- Under Swiss domestic law, PE are defined as being **fixed places of business** which are wholly or partially engaged in the business activities of an enterprise or an independent profession.
- A physical presence or installation is required.
- PE of Swiss companies, which are located abroad are exempt from Swiss taxes, effective foreign substance i.e. allocation of risks and functions (manpower, offices etc.) is required.
- PE of foreign companies located in Switzerland are subject to tax on the income attributable to the PE at ordinary income tax rates.

Service Permanent Establishment Swiss Domestic Law (2/2)

The Term “Services” under Swiss Domestic Law:

- Switzerland has not enacted specific domestic income tax provisions regarding services (income from services is taxed in the same manner as other income);
- The term “service” does not appear in the Swiss Act on the Federal Direct Tax;
- In the Value Added Tax Act “service” is defined as every supply that is not a delivery;
- There is no Swiss withholding tax on services fees or royalty payments.

Service Permanent Establishment Swiss Tax Treaties

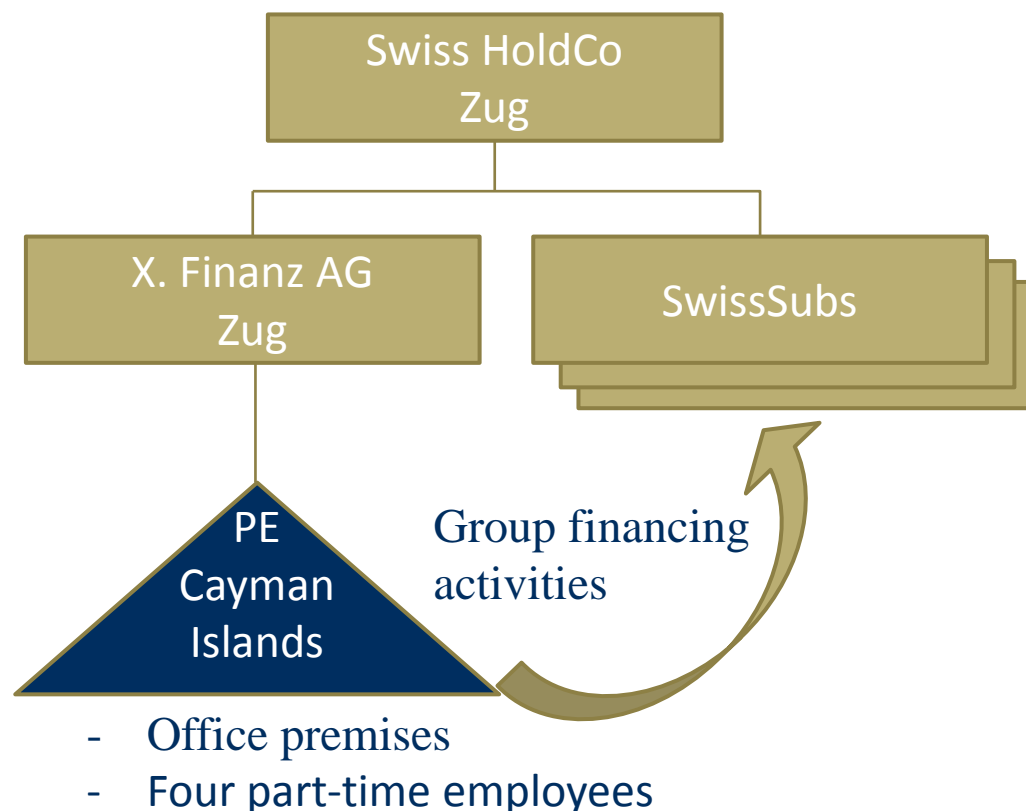
Service PE in Switzerland under Swiss Double Tax Treaties:

- The definition of PE in **Swiss tax treaties** which relate to the provision of services largely follows the rules of **art. 5 of the OECD model treaty**.
- In its tax treaties, Switzerland has not agreed to include the alternative services provision of the commentary on art. 5 OECD model treaty that secures additional source taxation rights, in certain circumstances, with respect to services performed within the territory of the source State.
- As an **exception**, around 10 Swiss tax treaties include a provision along the lines of art. 5 (3) b of the UN model convention, which states:
*“The term **“permanent establishment”** also encompasses: The furnishing of services, including consultancy services, by an enterprise through employees or other personnel engaged by the enterprise for such purpose, but only if activities of that nature continue (for the same or a connected project) within a contracting State for a period or periods aggregating **more than six months within any twelve-month period.**”*

Recent Developments in Switzerland: SwissCo with Offshore PE

Swiss Federal Supreme Court Decision of 1 February 2013

Swiss Federal Tax Administration versus X. Finanz AG, Zug:



Swiss Federal Supreme Court:

- Domestic definition of PE is applicable to foreign companies with activities in CH and to Swiss companies with activities abroad; **but**
- Unilateral rules, with which double taxation is to be avoided, are to be interpreted in favour of Switzerland's right of taxation. To the extent a DTT applies, the DTT acts correctively.
- Office premises and four branch managers working 20% each (with a total amount of salaries of USD 50'000) is not enough substance: Group financing does not constitute a business activity, which fulfils the requirement for a PE
- Is this the end for offshore branches?

Recent Developments in Switzerland: Swiss Finance Branch



Low-taxed branches of foreign companies are under attack by OECD (see OECD-report “Addressing Base Erosion and Profit Shifting”).

Swiss Finance Branch („SFB“) Principles;

- For Swiss federal, cantonal and communal tax purposes, it is possible to make deemed interest deduction on a notional basis;
- On cantonal and communal level mixed company status can be applied for;
- Low overall effective Swiss income tax burden
- No deemed interest income on the head office level
- Interest deductions and financial expenses at the level of high-taxed operating companies;
- Tax treaties of the head-office country apply.

Recent Developments in Switzerland: Swiss Finance Branch

Possible points of attack;

- On the level of the head office: deemed interest income, application of credit method;
- *On the level of the borrower: LOB clauses in treaties (e.g. triangular clauses)*

Alternatives

- Low ordinary CIT rate

Recent Developments in Switzerland: Principal Structures



National tax regimes are increasingly targeting principal company structures

Principal Structures:

- The principal company regime (PCR) applies at the federal level to Swiss companies (e.g. regional headquarters) which develop, manufacture and sell goods generally abroad through contract developers, contract manufacturers and local agents abroad.
- Low CIT base leading to low effective tax burden

Possible points of attack;

- (Agency) permanent establishment;
- Transfer pricing

Alternatives

- “Embedded” IP box
- Low ordinary CIT rate



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