CORPORATE TAX - SWITZERLAND

New step-up on migration instrument introduced

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Introduction

As of 1 January 2020, foreign companies can take advantage of a tax-neutral step-up of built-in gains (including self-created goodwill) to fair market value for Swiss direct tax purposes when relocating their legal seat, effective place of management or assets, business units and functions to Switzerland from overseas. The disclosed built-in gains may be depreciated tax-effectively over a specified time period, allowing the Swiss company or branch to reduce its tax burden significantly during the respective timeframe.

The new step-up on migration is an attractive instrument alongside various other tax measures (eg, the patent box or the R&D super deduction) introduced with the implementation of the Swiss corporate tax reform on 1 January 2020 and contributes substantially to preserve and enhance Switzerland's international attractiveness as a business location.

Key features of step-up on migration

New step-up on migration instrument

In general
The new step-up on migration allows for a tax-neutral disclosure of built-in gains (including self-created goodwill) for Swiss direct federal, cantonal and communal tax purposes on a foreign corporation's:

- transfer of its assets, business units or functions to a Swiss legal entity or a Swiss branch office; or
- transfer of its statutory seat or place of effective management to Switzerland.

The step-up on migration instrument applies regardless of whether exit taxation is triggered in the foreign jurisdiction following a company's relocation or transfer of its assets to Switzerland. Further, the disclosure of built-in gains is generally limited to tax accounts and is not necessarily presented in the statutory financial statements, if permissible at all under commercial law.

Specific cases

Transfer pricing adjustments
Given its broad scope, the step-up on migration instrument is available irrespective of the legal form of the transfer of assets to Switzerland (eg, sale or contribution) and, as a consequence, may apply even in the event that transfer pricing adjustments are made. For instance, if a Swiss entity acquires goods from a foreign group entity below the arm's-length price (acquisition price) and resells the respective goods at market price to a third party (reselling price) within the same business year, it will be given the option of disclosing the difference between the acquisition price and the arm's-length price in a tax-neutral manner. As a result, only the difference between the reselling price and the arm's-length price will be subject to taxation in Switzerland. As some details remain unanswered, it is expected that the tax authorities will evolve their practice and further define the scope and modalities of a step-up in the context of such transfer pricing adjustments.

Qualifying participations

While built-in gains on investments and participations below 10% may be disclosed under the new step-up regime, such a disclosure is not possible with regard to participations in Swiss or foreign companies of at least 10%, since capital gains derived from the sale of such participations are already virtually tax-exempt due to the Swiss participation relief.

Valuation method

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Swiss law stipulates no specific valuation method for determining the amount of built-in gains and self-created goodwill on relocation to Switzerland. Rather, any recognised valuation method may be chosen. In practice, it is advisable to agree a recognised valuation method with the competent tax authority prior to the relocation to Switzerland in order to have legal certainty in this regard.

Further, it must be noted that the method chosen for determining the fair market value on relocation to Switzerland also applies for establishing the exit tax in case the given company decides to leave Switzerland or transfer a part of its activities and functions overseas.

Tax-effective depreciation of step-up
Following relocation, the disclosed built-in gains may be depreciated tax-effectively throughout the amortisation period pertaining to the individual assets or over a 10-year period in the event of self-generated goodwill, respectively.

In the event that the depreciations exceed the taxable income in a given year and a tax loss results, such a tax loss may be carried forward and offset against any taxable income generated in the next seven years.

As a result, only built-in gains and goodwill created under Swiss tax sovereignty are subject to Swiss corporate income tax on realisation at an effective ordinary tax rate ranging between 12% and 22%, depending on where the company or branch is located.

Tax optimisation of cross-border payments

Effective and constructive dividend distributions made by a Swiss resident entity to its shareholders are subject to Swiss withholding tax at a rate of 35%. While the Swiss withholding tax will be refundable or creditable in full to a Swiss tax resident corporate and individual shareholder if certain requirements are met, it is generally intended as a final tax burden for beneficiaries who are not Swiss resident for tax purposes. However, a full or partial refund will be available if the country in which such a beneficiary is resident for tax purposes has entered into a double tax treaty with Switzerland. By contrast, distributions paid out of capital contributions are not subject to Swiss withholding tax.

Since there is no step-up of the tax base for withholding tax purposes, it may be favourable to create such capital contribution reserves in the framework of pre-immigration planning – in particular, in cases where the Swiss withholding tax is not fully refundable under a double tax treaty. This option is particularly paramount in the event of cross-border group reorganisations. For instance, capital contribution reserves may be created by contributing the participation in the foreign entity to be migrated to Switzerland to a newly established Swiss company at fair market value prior to the relocation. Hence, the newly established Swiss company may repay capital contribution reserves in the amount corresponding to the fair market value of the respective participation to its foreign shareholders in the subsequent fiscal years without triggering any Swiss withholding taxes.

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