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Second Series of Swiss VAT Simplification Measures

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The Swiss Federal Council recently published a report on ten years of experience with Value Added Tax (VAT) in Switzerland proposing various simplifications. A first series of simplification measures came into effect on 1 January 2005. The Swiss Federal Tax Administration (FTA) lately released a second series of extra-statutory concessions, applicable as from 1 July 2005. The gist is summarized below.

Apportionment of Input Tax on Dual-use Inputs

If goods and services are not acquired solely for the purposes of taxable supplies of goods and services or qualifying supplies, the VAT incurred on such dual-use inputs must be apportioned between deductible and non-deductible amounts. Alternatively, the new statements of practice provide that a taxable person may fully deduct the VAT incurred on dual-use inputs if he or she voluntarily pays VAT on all outputs at the standard rate. In view of the fact that this simplification requires voluntary payment of output tax on all supplies without the right to openly pass on the VAT to the customer, it is hardly conceivable that many taxable persons will benefit from this extra-statutory concession. In this context, it is particularly odd that the simplified procedure explicitly requires taxable persons also to pay VAT on zero-rated services supplied to foreign customers, but with respect to the partly taxable and partly exempt short-term leasing of immovable property, the concession facilitates VAT compliance.

Mixed Supplies of Goods and Services

Mixed supplies are separate supplies of goods and services which are charged at a single inclusive price. If mixed supplies contain components subject to VAT at different rates (e.g. chocolate + toy, magazine + CD, etc.), the basic rule requires a taxable person to work out the total VAT liability in proportion to the value of each component. However, if 90% or more of the total consideration is attributable to one main component, then a taxable person is allowed to calculate the total VAT liability based on the rate applicable to this main component. As from 1 July 2005, this simplified method is extended to mixed supplies if the consideration attributable to the main component amounts to 70% or more of the total consideration. This extension is certainly welcome. However, it should be noted that the simplified method may not be applied if tax privileged accommodation or exempt supplies are packaged with standard-rated supplies.

Input Tax Adjustments Due to Partial Change of Use

In principle, the proportion of deductible input tax must be calculated by using a method which accurately reflects the extent to which inputs are used for the purposes of deductible or non-deductible supplies. Taking into account that the strict application of this basic rule could require a new calculation for every taxable period, the current VAT statements of practice provide that an approximate calculation may be used. According to this simplified method, a partial change in use requires (or allows) input tax adjustments only if the deduction entitlement changes by more than 10% compared to the deductible proportion in the previous year. The new VAT statements of practice have increased the threshold requiring (or allowing) input tax adjustments due to changes in use resulting in decreases or increases of the deductible proportion by more than 20% which is intended to extend the scope of the approximate calculation of the deductible proportion. Taxable persons who wish to benefit from this new simplification measure are required to contact the FTA by 31 December 2005.

Deduction Entitlement of Holding Companies

The mere acquisition, holding and sale of shares in a company does not confer the status as a taxable person for VAT purposes. Therefore, pure financial holding companies are not entitled to deduct input

tax at all. Mixed holding companies which provide taxable supplies of services to its subsidiaries or third parties, however, are entitled to deduct VAT incurred on inputs attributable to these economic activities. With regard to non-attributable input tax, the calculation of the deductible proportion based on the ratio of turnover from taxable activities to the total turnover of the holding company (standard turnover method) normally does not lead to an appropriate result. In most cases the standard turnover method does not properly reflect the different level of inputs required for transactions exempt from or outside the scope of VAT and taxable transactions, regardless of the revenues generated there from. In Switzerland, this mismatch is particularly aggravated by the fact that – contrary to EC VAT law and recent decisions handed down by the European Court of Justice – dividends are included in the denominator of the fraction used to calculate the deductible proportion. The new VAT statements of practice stipulate that the calculation of the deductible proportion may be performed by reducing the deduction of VAT on dual-use inputs by 0.02% of the turnover generated from exempt or outside the scope transactions, provided the simplification does not result in an obvious tax advantage or disadvantage. As from 1 July 2005 this simplified calculation of the deductible proportion also may be used in general if a taxable person effects incidental financial transactions exempt from VAT, and applies irrespective as to whether the turnover generated from these exempt transactions amounts to more than 10% of the total annual turnover.

Required Mark-up on Inter-company Transactions
The taxable amount for the supply of goods and services between related parties (e.g. companies belonging to the same group of companies) is the open market value which a customer would have to pay to a supplier at arm's length in order to obtain the goods or services in question. In this context, the FTA often issued additional VAT assessments if goods or services were deemed to be provided below the open market value. In general, the FTA applied the cost-plus 5% method (i.e. a mark-up percentage on costs). According to the new VAT statements of practice a mark-up on costs below 5% will be accepted if the taxable person is able to justify the calculation with reference to appropriate transfer-pricing documentation. Maintaining good transfer-pricing defence files appears to be vital.

Status as Disclosed Agents for VAT Purposes
If an agent concludes agreements explicitly in the name and for the account of another person (i.e. the principal), and the tax invoice for the supply of goods or services clearly shows that the supply is directly from the principal to the customer (and not to, or by, the agent), the agent only has to account for VAT on the value of the services provided to the principal. The VAT statements of practice, however, had previously indicated that a specific mandate from the principal was required for each individual item sold by the agent in the name, and for the account of, the principal. According to the new statements of practice, a general mandate including a generic description of the goods to be sold by the agent suffices.

What's next?
From a taxpayer's point of view, the extent and nature of the new VAT simplification measures may seem nowhere near enough the improvements sought. It is hoped, however, that more substantial amendments to the Swiss VAT Act will complement the rather tentative steps the FTA has made in the direction of reforming the Swiss VAT system for the better.

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