

Swiss special purpose vehicles

Adriano Marantelli offers an overview of using Swiss special purpose vehicles as a gateway to Europe for India investors

By Dr. Adriano Marantelli, Partner, meyerlustenberger

Introduction

For a variety of reasons, Switzerland has always been an ideal location for foreign investors, a real gateway to Europe. One important reason for this is the country's favourable tax regime.

Typically, Swiss entities (legal entities, branches, partnerships etc.) are used for special purposes and activities such as:

- >holding company functions
(incl. joint venture functions)
- >centralised purchasing or distribution
(sales companies)
- >group financing
- >headquarter functions
- >factoring/leasing

We would like to discuss below some of the special tax features and tax incentives available.

General remarks on the Swiss tax regime

The Swiss income tax system is based on three layers: namely federal, cantonal and communal; the total tax is assessed by the cantonal authorities. In general, income tax for business activities is levied at a flat rate of approx. 7.8% on income before taxes at the federal level (federal tax) and at flat or sometimes graduated rates at the cantonal/communal level. However, in many instances it is possible for foreign investors to negotiate tailor-made tax rulings for a variety of activities (see list above) based on the merits of the particular case. A tax ruling basically substantially reduces the cantonal tax or even exempts income from taxation as in the case of dividend income or a tax holiday situation (see below).

For central purchasing or distribution activities an overall tax rate of approx. 9% can be obtained in a number of Swiss cantons. Depending on the sales company's or branch's risks and functions, a transfer pricing study may decrease the overall tax rate even further as a result. Certain financing functions performed within an international group are even taxed as low as 2% if certain conditions can be met.

We would like to discuss certain special purpose vehicles in more detail below:

Holding companies

Dividends as well as capital gains on the sale of qualifying Swiss and foreign participations of a Swiss holding company are in principle tax-exempt. Furthermore a Swiss holding company is fully exempt from cantonal/communal income tax, which means that any income other than dividends (e.g. interest or royalty income, management fees etc.) are subject only to the federal income tax at the flat rate of 7.8%. Moreover, according to the more than eighty Swiss double taxation treaties, profits generated in Switzerland can typically be repatriated with a zero or 5% withholding tax. A 0% withholding tax rate also applies based on the EU-Swiss agreement on the taxation of savings, which became effective on July 1, 2005 between Switzerland and the EU. Such agreement basically grants Swiss companies the same advantages on dividends, interest and royalties as the EU parent-subsidiary directive and interest-royalty directive grant to companies in EU countries.

Unlike the holding regimes of other countries, the Swiss holding regime applies even if the foreign subsidiary is located in a low- or zero-taxed jurisdiction because Switzerland does not apply either any CFC rules (Controlled-Foreign-Corporations rules) or any subject-to-tax clauses. In addition, unlike EU holdings, Swiss holdings can benefit from VAT input tax deduction related to their holding activities (new regime as of 1 January 2010).

Service companies

There is an attractive regime for service companies. Such companies that perform services like marketing, administration etc. for other group companies can often be assessed on a deemed profit that is determined on the basis of overhead costs plus 5%. Additionally, if the place of performance of the services is outside Switzerland, the service company can benefit from an effective overall low tax rate (approx. 9%).

Finance branches

In the case of finance branches dealing with group internal financial activities (borrowing, treasury, factoring and so on) on a large scale, tax rulings may even be obtained that result in an overall tax burden as low as 2%.

Sales, distribution or principal companies/branches

International sales companies or branches are set up in Switzerland for the specific aim of trading outside Switzerland. Such companies usually qualify for a tax rate of approx. 9% or even lower as long as their commercial activity for which the ruling is requested is generated outside Switzerland for the most part (as a rule non-Swiss sales of 80%).

A sales activity can also take the form of a more sophisticated operation within a group, meaning that the Swiss company takes over the function of a so-called principal company. Instead of an international group selling goods to the local distribution subsidiary and the subsidiary then taking the responsibility for selling to local customers, the essence of the commission arrangement is that the company in the international group that would otherwise sell the goods to the distribution subsidiary retains title to the goods until their sale to the final customer and the local distribution subsidiary acts as a limited risk distributor or a commissioner by selling the goods in its own name but on behalf of the foreign supplying company.

If a Swiss distribution company is established by the foreign parent manufacturing company, the use of a commission arrangement can offer a number of interesting advantages for an international group, such as (i) lower profit margin for the local subsidiary and very low taxation of commission income in Switzerland and (ii) centralisation of the commercial risk at the parent level etc.

Production, assembly, R&D etc.

Switzerland has an attractive answer in terms of tax advantages for a large variety of international activities such as research and development, production, assembly etc. For these kinds of activities, Switzerland even grants tax holidays for up to ten years. Here again, the tax holidays granted may depend on the canton or region where an operation is established.

Tax benefits are available not only for any investment on a stand-alone basis, but also for investment projects where the investor is entering into cooperation with a Swiss partner, or in the case of an acquisition.

The tax concessions are obtained on the merits of each individual case, taking into account the possibility of new jobs being created or existing jobs being maintained. Tax holidays are not limited to companies that are newly established. Companies undergoing necessary reorganisations or Swiss

companies which have been acquired by a foreign investor also qualify.

Last but not least: individual tax issues

Swiss resident employees (such as for instance foreign executives) are subject to Swiss income tax. Tax rates are progressive and depend on worldwide income, family situation, and place of residency. There are a number of tax planning techniques available to increase the net compensation earned by Swiss resident employees. In addition, important tax concessions are granted to expatriates, which may result in tax-free income amounting to a substantial percentage of gross compensation. Some of these tax planning opportunities are detailed below:

Cost of living allowance

This is a tax deductible allowance available for expatriates seconded temporarily to Switzerland. In certain cantons, an important part of the total compensation may be characterised as a cost of living allowance and be deductible for Swiss federal and cantonal/communal income tax purposes for a certain period of time.

Business expense allowance

Business expenses reported by the employee on his or her periodic expense account can be reimbursed without any tax implications for the individual. In addition, the Swiss-based HQ may provide a flat rate business expense reimbursement designed to compensate the employee for sundry business expenses such as the entertaining of customers and other items that the employee might not want to specify on an expense account. This amount, commonly referred to as a representation allowance, is deductible from the employee's taxable income and, to a certain extent, from income subject to social security.

A competitive location

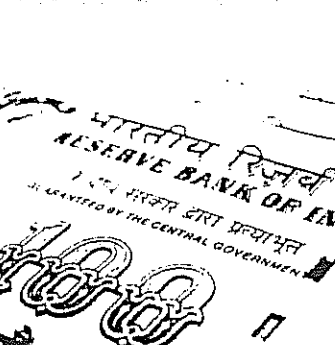
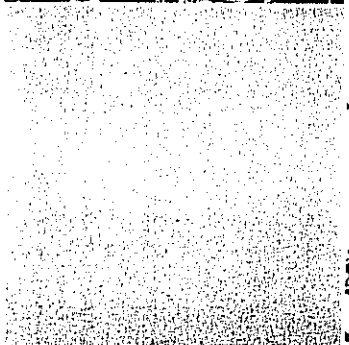
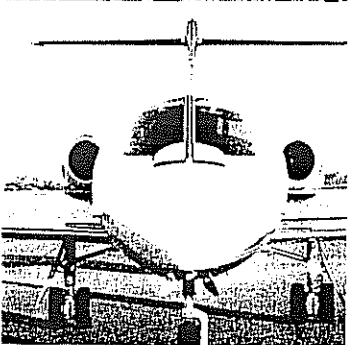
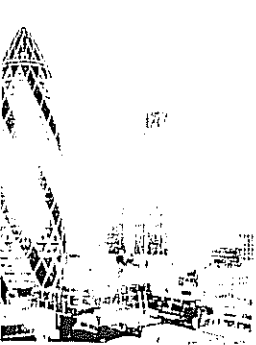
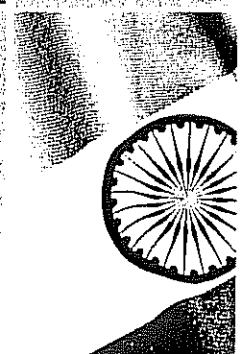
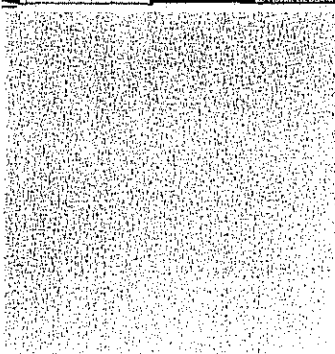
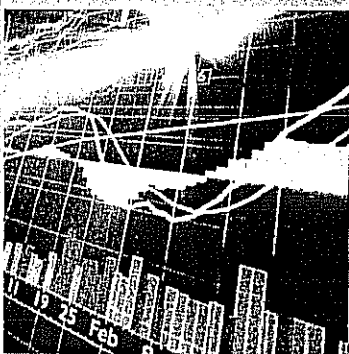
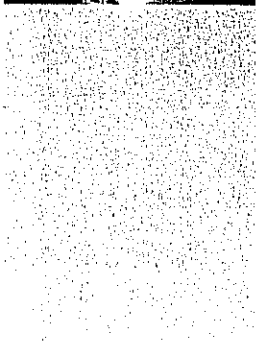
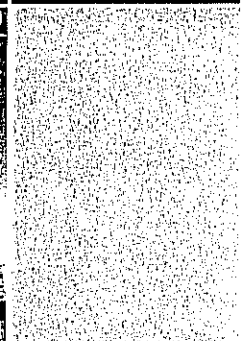
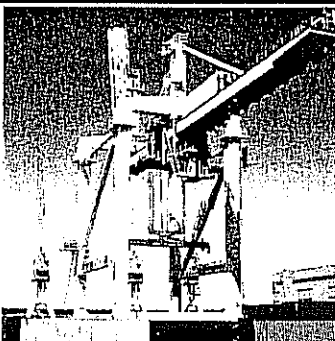
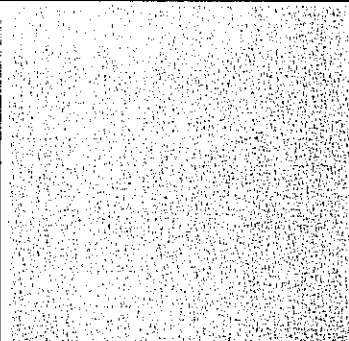
An excellent and flexible Swiss tax regime can be combined with other hard and soft investment factors such as central location within Europe, political stability, excellent infrastructure and highly qualified personnel. As a result, Switzerland is indeed a very competitive and real alternative to any other European location.



Name: Dr. Adriano Marantelli
 Title: Partner
 Firm: meyerlustenberger
 Email: a.marantelli@meyerlustenberger.ch
 Phone: +41 44 396 9191
 Web: www.meyerlustenberger.ch

2010-
2011

A Guide to International Financial Centres What Indian investors need to know



Bahrain
Barbados
British Virgin Islands
Cayman
Cyprus
Dubai

Hong Kong
Isle of Man
Jersey
London
Luxembourg
Mauritius

Saudi Arabia
Seychelles
Singapore
South Africa
Switzerland

LONGTAIL