Dear Reader,

Once again, we bring you our research into the most important current tax issues in summarized form. In this issue we concentrate mainly on the topic of Value Added Tax, with the emphasis as follows:

The European Commission has now received 1,700 responses to its “Green Paper on the Future of VAT”. In its latest report on the subject, the Commission sets out how the VAT system in the European Union is to be further developed in the coming years. Read our article and find out which three measures are the most important in the short term.

If your company’s not in the EU, did it pay VAT in Europe in 2011? The second article in this newsletter explains how, and under what conditions, you can claim it back.

We also examine the Double Taxation Agreement between the Federal Republic of Germany and the Swiss Confederation, and the state treaty solution to the problem of tax evasion involving undeclared assets.

The changes to the German VAT regulations will affect all companies selling goods internationally from Germany. Read more on pages 11–12.
We also consider the Swiss Federal Rail Reform 2 Act ("Bahnreform 2") and its consequences for public transport companies.

The second part of our contributions from the cantons discusses current tax topics in Central Switzerland.

I hope you find this issue an interesting and informative read.

Sincerely

Dominik Bürgy
Partner, Tax Leader Switzerland
dominik.buergy@ch.ey.com
On 5 December 2011, the EU Commission published the results of the public consultation on its Green Paper on the future of VAT, launched in 2010. The Commission reported that it received more than 1,700 responses to the Green Paper from businesses, academics, citizens, tax authorities and professional service providers, including Ernst & Young; the size of the response indicates just how profoundly today’s economy is affected by VAT issues.

Following this consultation, the Commission has now presented its conclusions on how the EU VAT system should evolve in the coming years and outlined its planned next steps. The short-term proposals include a move to taxing transactions using the “destination principle” in the country of consumption, a simplification of the rules and a broadening of the tax base to boost revenues. These proposals will have an impact on all businesses that are established in, or trade with, the EU.

The Green Paper on the future of VAT VAT in the EU dates back to the late 1960s, and the time for a deeper reflection on its functioning seems to be justified not only by the complexity of the current system but also by the rapid changes that have taken place in the economic environment, the advent of new technologies and the growth of complex financial instruments. Few commentators would deny that the European VAT system has come of age and needs profound reforms, improvement and simplification to meet the challenges of today’s global economy.

However, when it comes to suggesting concrete changes, opinions differ and it is no surprise that when the Commission presented its Green Paper on the future of VAT in December 2010, the authors chose a broad approach, raising over 30 questions addressing various VAT issues. In response, the Commission received more than 1,700 comments from businesses, academics, professional advisers and tax authorities, representing a wide range of interests and views.

With so many issues and so many diverging interests on the table, how the Commission would deal with the results of the consultation and what changes would be announced were anticipated with interest. But, in the event, there are no big surprises. In its communication dated 5 December 2011, the Commission clearly sets out its understanding of a future EU VAT system and identifies 26 priority areas for further action. Among these are several action points that are surprisingly detailed and capable of being implemented in the very near future.

Future-proofing EU VAT According to the Commission’s report, a future-proofed European VAT system will be based on the “destination principle.” This implies that all supplies are taxed for VAT according to the rules of the country where the supply to the final consumer occurs. As a consequence, the “origin principle,” which is the underlying principle of the current EU VAT Directive, would be completely abandoned.

It is anticipated that the reshaped VAT system will result in a single set of clear and simple VAT rules – the EU VAT code – and taxpayers will only have to deal with the tax authorities of a single Member State. The national tax authorities will set up an intensified, automated and rapid exchange of information and ultimately collectively act as a European VAT authority.

Finally, in order to generate more revenue at less cost, the future system will have a broader tax base and follow the principle of taxation at the standard rate.

First-step measures To move the current VAT to the future system, the Commission wants to implement the following short-term measures as a first step:

- Setting up an EU VAT web portal that provides information in several languages on basic issues such as registration, invoicing, VAT returns, VAT rates, special obligations and limitations to the right of deduction
- In 2012, publishing the Guidelines agreed by the VAT Committee on EU legislation and explanatory notes on the new legislation before its entry into force, in order to inform businesses
- Setting up a tripartite EU VAT forum (involving the Commission, Member states, and stakeholders) in the course of 2012
- Proposing a standardized VAT declaration (VAT Return) to be available in all languages and optional for businesses across the EU by 2013
Ensuring the smooth introduction of the mini one-stop shop scheme (registration in a single EU Member State) in 2015 and envisaging a managed broadening of the concept from 2015 onward

**Other measures**

In addition, the Commission announced that it will work towards proposals for the following issues:

- Proposing a quick reaction mechanism in 2012 to deal with massive, organized and sudden VAT fraud
- Establishing a more neutral and simpler VAT framework for passenger transport activities
- Restricting the use of reduced VAT rates in order to increase the efficiency of the VAT system by 2013
- Proposing legislation to lay down the definitive regime of taxation of intra-EU trade by 2014

Furthermore, the Commission intends to explore the possibility of setting up an EU cross-border audit team to facilitate and improve multilateral controls and strengthened cooperation with third countries (i.e., non-EU countries) with a view to exchanging information in the field of indirect taxation. The Commission will also further analyze new ways for VAT to be collected. Not surprisingly, the suggested “split payment model”\(^1\) prompted negative reactions from business and tax practitioners; they feel it is likely to have a negative impact on cash flow and compliance costs. Nevertheless, the Commission does not want to discard this model, as some Member States expressed an interest in exploring it further.

Other aspects of EU VAT such as the small business scheme and the VAT grouping provisions or the complex and divergent rules on the right of deduction and double taxation issues, will be addressed only in the medium-term.

**Issues that are not addressed in the report**

Interestingly, some other issues that were part of the Green Paper are no longer mentioned by the Commission in its report. This is the case for the still unclear VAT treatment of holding companies’ transactions notably those related to management of shares or treasury functions, for the handling of a large number of exemptions and for the question of how the EU VAT system could be further harmonized, e.g., by using Council regulations or by allowing the Commission to adopt implementing decisions.

**Ernst & Young’s response**

Ernst & Young’s response to the Green Paper — which was based on feedback from our clients and our professional experience — recommended that the Commission should concentrate in the short- to medium-term on making proposals to improve and modernize the administrative and technical framework within which businesses are required to collect and account for VAT. In particular, we recommended:

- Further efforts to simplify and harmonize invoicing requirements
- Harmonizing the frequency and content of VAT returns and listings using modern computerized technology
- Extended use of the one-stop shop mechanism for registering and fulfilling VAT obligations with a view, in particular, to incorporating the possibility of deducting input tax

In addition, we recommended that, in the longer term, priority should be given to harmonizing the rules regarding restrictions on the right to deduct input tax, and to disassociating formal requirements in this area from the actual right to deduct input tax, to increase the neutrality of the VAT system.

It is good to see that the Commission also considers most of these recommendations to be priorities. There is hope that the reform and modernization of the European VAT system has now finally taken off and will gather speed. It should, however, be kept in mind that it could be a long time before even the short-term proposals are implemented. Surprising twists are still possible along the way! We believe that stakeholders should follow further developments attentively and not hesitate to contribute their opinions as the discussions progress.

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\(^1\) In this model, the purchaser pays the VAT on the purchase price to a blocked VAT bank account, which can only be used by the supplier for paying VAT to his suppliers’ blocked VAT bank accounts.
EU VAT refunds
Are you preparing your 2011 EU VAT refund application?

Has your non-EU business incurred VAT in Europe in 2011? If so, you may be able to recover the cost by applying to the relevant EU country(ies) for a refund — provided you comply with the rules. In general, claims by non-EU businesses must be submitted within six months after the end of the calendar year. Although the deadline for applications for 2011 for most EU countries is June 2012, you should be collecting the right information now to support a successful claim.

Most multinational enterprises (MNEs) incur VAT in countries where they are not established. A business may, for example, incur foreign VAT on trade fairs and conferences, meals and accommodation, travel, transportation and fuel costs, business entertainment, marketing and advertising costs, professional services, telecommunications, printing materials and stationery and training. Even for large business expenses, recovering foreign VAT may be an issue.

Although there are mechanisms for VAT recovery, it may be difficult for foreign businesses to fulfill the requirements in practice. According to an Organization for Economic Cooperation and Development (OECD) survey from 2010, over 80% of businesses incur more than US$10,000 of VAT on foreign business expenditure every year. Yet, half of such businesses recover 50% or less of this foreign VAT — even when they are entitled to recover it all.

Not every country allows non-residents to recover VAT or to recover VAT on all items of expenditure. In addition, tax authorities apply strict criteria before they will authorize a repayment. Barriers to recovering foreign VAT include a lack of understanding of the VAT rules in different jurisdictions, difficult administrative procedures, language barriers, insufficient or incorrect documentation to support the application and missing important deadlines. So, planning ahead, understanding the detailed rules and applying them thoroughly can improve your organization’s chances of success in reclaiming European VAT on your business expenses.

EU 13th VAT Directive — who can use it?
The EU 13th VAT Directive grants the right for a business established outside the EU to recover VAT incurred in one of the 27 Member States. Similar refund rules also apply for expenditure incurred in Norway and Switzerland. You can use the 13th Directive to reclaim VAT paid in the EU if you are registered for business purposes in a non-EU country, provided that all of the following hold:

- You are not registered, liable or eligible to be registered for VAT in the EU
- You have no place of business in the EU
- You do not make any supplies in the EU (other than transport services related to the international carriage of goods, or services where VAT is payable by the person in the
- EU to whom the supply is made).

In addition, the expenses must be incurred by a business person or entity that would be considered to be engaged in a VATable activity if its activity were carried out in the EU. For example, financial services are generally VAT-exempt in the EU; therefore, a bank established, for example, in India may not be entitled to file a VAT refund application, as it may not be considered a VATable person under EU VAT legislation. However, this is not always a simple issue to decide, as it depends very much on the actual activities that the claimant undertakes.

Eligible expenses
Only VAT paid on business-related expenses can be reclaimed. Therefore, any private expenditure is not allowable under this refund procedure. In addition, some business expenditure may not be eligible for a VAT refund.

Each EU Member State has specific rules concerning which expenses can be subject to a claim in that country, and the rules can vary considerably from country to country. Some Member States, for example, do not allow recovery on hotel accommodation or fuel costs. In general, to be eligible for reclaim, the goods/services you include must be expenses that would be deductible if your business was carried on locally. For example, if local businesses are not entitled to take a VAT deduction for business entertainment, your non-EU business cannot lodge a VAT refund application for business entertainment incurred in that country.

Non-EU reciprocity
Some EU Member States also require that your country allows similar refunds to EU be able to claim VAT incurred in some EU countries. But it is worth remembering traders in respect of any turnover taxes that not all EU Member States apply this levied in your country. This is called the rule in the same way. “reciprocity” principle. So, if your country does not levy a VAT or if it does not refund a local VAT to non-residents, you may not be able to claim VAT incurred in some EU countries. But it is worth remembering that not all EU Member States apply this rule in the same way.

EU 13th Directive claim forms
EU VAT can be claimed quarterly or annually. The EU VAT refund process for non-EU businesses is still largely a paper-based system. A separate claim must be lodged with each country where you want to reclaim VAT. Although the claim form can generally be printed off from the relevant tax authority’s website, it must then be filled in and filed together with the original paper invoices. Difficulties can arise if the form needs to be completed in the local language. Assistance from the country of claim may sometimes be necessary to comply with this requirement.

1 VAT/GST Relief For Foreign Businesses: The State Of Play, OECD, February 2010
2 Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Rumania, Sweden, Slovakia, Spain, United Kingdom
Deadlines
The deadline for annual claims is generally 30 June of the year following the calendar year when the expenses were incurred. This means that for 2011 (invoices dated 1 January to 31 December 2011) the deadline for submission is 30 June 2012. There are, however, certain exceptions to the period covered by claims and the deadline. In the UK, VAT refund claims for non-EU businesses are based on a “prescribed year” running from 1 July to 30 June. The deadline for submission of annual claims in the UK is six months after the end of the prescribed year, i.e., 31 December. The deadline set by the EU Member States is a firm date and late claims are not accepted. This is an area where foreign businesses often struggle to meet the requirements. Although six months after the year-end seems a generous time limit, it can prove difficult to meet without forward planning. Claimants should have all the necessary paperwork, including certificates of taxable status and supporting documentation, ready well in advance to make sure the claim is submitted within the time limit.

Minimum claim amount
All countries have a minimum threshold for the amount of VAT that can be reclaimed. The threshold applies to the claim as a whole, not to every single expense. For example, in Germany the minimum value for a quarterly claim is €500 and the minimum value for annual claims (or the remaining period of the year) is €250. If the VAT incurred for a quarter is less than the minimum claim amount, the VAT can be included in the next claim (subject to the existing time and value limits).

Tax representatives and signatures
Some countries require the appointment of a locally accredited tax representative before a claim for refund can be filed. In addition, countries have strict requirements on who has the right to sign the application form (e.g., president of the board of directors). Again, it is advisable to check these requirements well in advance and certainly before filing the claim. It can take time to appoint a representative, for example, especially if the mandate needs to be translated and notarized.

Documentation is key to successful claims
Documentation is key to successful claims. You can increase your chances of making a successful claim by planning ahead and by complying meticulously with the detailed rules in each country with respect to the invoices you submit.

Original invoices
The first requirement is that the claim must be supported by an original VAT invoice for each expense. Generally, PDF copies or other copies are not acceptable. If you wish to reclaim VAT, the first step is to ensure that you receive an original invoice from your suppliers.

VAT invoice requirements
The VAT invoice requirements differ between EU Member States. However, in general, a valid VAT invoice should include all of the following information:

- Date of issue
- Invoice number
- Full name, address and VAT registration number of the supplier
- Quantity and nature of goods or services received
- Unit price or the consideration for the service supplied
- The date of the supply
- VAT rate applied
- VAT amount payable

The invoice requirements are subject to change from time to time, so it is advisable to check that the invoice received complies with the latest requirements. As many foreign VAT claims relate to expenses incurred on business trips, it is vital that all employees understand the documentation required to support EU claims.

Electronic invoices
Most EU Member States permit electronic invoices. But not every electronic invoice is considered to be valid for VAT purposes. Most countries require that an electronic invoice contains an advanced electronic signature. In the past, some companies have lost considerable VAT reclaim opportunities because the electronic invoices they submitted did not comply with the rules in that country – as they differ between member states.

What to do now
If your business incurred VAT on business expenditure in the EU, Switzerland or Norway in 2011, you should begin identifying this VAT, the supporting invoices and other documentation you will need to make a claim. This process is likely to be time-consuming. For most countries, the strict filing deadline is 30 June 2012 for 2011 applications – so there is no time to lose!

In gathering the necessary information and documentation, you may want to consider the following approach:

- Ensure your business does not have an EU establishment and that the other requirements for a refund are met
- Identify the VAT costs
- Analyze the VAT costs incurred in each country
- Gather supporting valid VAT invoices and ensure that the invoice requirements in relation to each invoice are met
- Determine if it was correct for the supplier to charge VAT
- Determine if the VAT suffered is refundable in the country concerned
- Obtain a certificate of taxable status (tax certificate) from the tax authorities where your business is resident
- Appoint a tax representative where necessary
- File the application for a VAT refund before the deadline

How we can help?
As a non-EU business you may be entitled to reclaim VAT incurred in Europe. Sometimes these amounts can be substantial, even in connection with travel expenses. However, you must comply with the detailed rules for each country, which can prove difficult. It is crucial to be aware of the rules and to adopt robust processes to identify recoverable VAT, obtain the correct documentation to...
support your claims and submit the forms within the time limits allowed.

Using our extensive network of indirect tax professionals, at Ernst & Young we can assist your business in identifying opportunities for European VAT claims and help you to develop or improve related business processes to reduce the time and administrative costs associated with making claims and increase your chances of success. We can help you, for example:

- Develop efficient procedures to capture European VAT incurred
- Identify VAT incurred in Europe and its eligibility for refund
- Determine if you have sufficient documentation to support a VAT reclaim
- Ascertain whether your business is entitled to a VAT refund in the relevant EU Member State
- Apply for a tax certificate from the domestic tax authorities
- Review your activities to identify any European VAT compliance issues
- File the VAT refund application in the local language, where necessary
- Communicate with the relevant European tax authorities locally
- If you would like more information about reclaiming VAT in Europe, please contact your usual Ernst & Young indirect tax adviser.
Agreement between the Swiss Confederation and the Federal Republic of Germany

Thomas Linkerhängner, Senior Manager Swiss German Tax Group, Basel, thomas.linkerhaegner@de.ey.com

Upon the conclusion of the negotiations pertaining to the amendments to the Double Taxation Agreement between the Federal Republic of Germany and the Swiss Confederation, a treaty solution was announced during the initialing ceremony of the amendment protocol on 26 March 2010 to resolve the tax evasion issue associated with undeclared assets. After protracted negotiations, the text of the Agreement was initialed in Bern on 10 August 2010 by negotiators Michael Ambühl (State Secretary, Swiss Federal Department of Finance) and Hans Bernhard Beus (State Secretary, German Federal Ministry of Finance).

After the text was approved by the German Federal Cabinet, Eveline Widmer-Schlumpf and Wolfgang Schäuble signed the agreement on 21 September 2011 in Berlin. That same day, the text of the Agreement, hitherto kept secret, was published by the German Federal Ministry of Finance and the Swiss Federal Tax Administration.

Principles, terms and definitions

The Agreement is designed to ensure that those persons in Germany to whom it applies satisfy their tax obligation by way of a retroactive tax for the past and a final withholding tax for the future. The persons concerned are those individuals who were resident in Germany on 31 December 2010 (reference date 1) and had/have a client relationship with a Swiss paying agent on or after 1 January 2013. Beneficial ownership alone does not suffice.

In order to benefit from the future anonymous withholding tax, the individual must have a client relationship with a Swiss paying agent on or after 1 January 2013 (this date is definitive if the agreement goes into effect later on) and be the beneficial owner of assets. Beneficial ownership alone does not suffice. By virtue of the “look-through” concept embodied in the agreement, the income from corporations, trusts, establishments, foundations and similar constructs is attributed to the beneficial owner, documented in «form A». That is not, however, the case when companies operate an enterprise managed according to commercial principles or are subject to tax liability in their country of domicile or are not deemed to be intransparent under German law.

In the case of universal succession, e.g. inheritance, the individual is superseded by the successor in title. The agreement applies to all assets held in the current or custody accounts of a Swiss paying agent, e.g. stocks, bonds, options, derivatives, certificates, cash accounts and fiduciary investments, but not the contents of safe deposit boxes such as gold, precious stones and the like. Life insurance policies are included among relevant assets where they serve as “insurance wrappers”.

Switzerland may demand that Germany establish mechanisms for the taxation of persons resident in Switzerland.

The States party to the Agreement are in accord that the effect of the cooperation provided for in it is equivalent to the automatic exchange of information on capital income.

Legalization of the past

Three back-tax options are available:

1. One-off lump-sum tax payment
2. Authorized voluntary reporting of information
3. Voluntary declaration by the taxpayer pursuant to section 371 of the German Tax Code (AO)

The rate applicable to the one-off lump-sum taxation of assets not previously taxed is 34%, albeit a minimum of 19% of the higher asset value on 31 December 2010 or 31 December 2012.

The relevant tax rate is determined on the basis of a complex formula which, in simplified terms, derives the tax liability from the increase in asset value since the custody account was set up and from the notional income for 2011 (3%) and in 2012 (ca. 2.9%).

This formula is based on the experience gained in the course of the voluntary declarations of previous years in which the back-taxes paid were primarily on increases in asset values (inheritance and gift taxes), and to a lesser extent, on income. In cases in which the contractual relationship with a Swiss paying agent can be assumed to be recent, the tax liability will be higher as it is assumed that the funds originate from untaxed sources and no statute of limitation yet applies to levying tax.

The amount of the tax liability is also dependent on the increase in the value of the assets from 31 December 2002 to 31 December 2010.

Asset inflows from Germany between 21 September 2011 and 31 December 2012 do not fall under the one-off settlement payment. Although the inflows will be included in determining the amount of tax payable, the higher tax amount will not result in the associated tax obligation being discharged but rather will be deemed an advance on income tax payable for the 2013 assessment period. This also means that no exemption from criminal prosecution ensues.

On the basis of the calculations illustrated, the minimum tax rate of 19% will be applicable in many cases, in any event whenever the increase in asset value from 31 December 2002 to 31 December 2010 is less than 50%.

3 The agreement is expected to enter into force on 1 January 2013.
After the one-off payment has been credited to the settlement account created for this purpose with the Swiss paying agent, all tax liabilities associated with the assets held in the account will be deemed to be discharged. This also applies to liabilities that arose prior to 31 December 2002 (e.g. non-time-barred gifts). Income, wealth, inheritance and gift tax, VAT and trade tax obligations will be deemed to be discharged. The situation with regard to church tax and the solidarity surcharge is not explicitly covered. Any corporation tax claims will be deemed to not be discharged.

The one-off payments will be forwarded from the Swiss paying agent to the competent German authority and then to the competent authority in Germany.

Under the terms of the agreement, the individual will receive a certificate on the payment of the lump-sum tax settlement; this certificate must contain the individual’s identity, place of residence and client number, the name and address of the Swiss paying agent, the amount of the one-off payment, and the method of computation. This certificate is proof of payment of back-taxes on the assets. The individual concerned can lodge an appeal within thirty days. If no appeal is lodged, the one-off payment is forwarded to the Swiss agency.

Since the tax liabilities are discharged, no criminal prosecution ensues. If, however, the assets are the proceeds of crime or the competent German authority had reasonable suspicion of tax evasion by the taxpayer before 21 September 2011 and the taxpayer was aware of this or should have reckoned with it, no discharge effect or immunity from prosecution arises.

If the assets in the person’s custody account are insufficient for the one-off payment and the account still does not have sufficient funds after the eight-week period granted by the paying agent, the person’s personal data and assets will be communicated to the German tax authority as in the case of voluntary reporting, albeit without the person’s authorization.

Where the one-off payments are legally unfounded, the person affected has the right to reclaim these amounts from the competent German authority.

The Swiss paying agents have undertaken to effect an up-front payment of CHF 2 billion within twenty-five days of the agreement entering into force. The Swiss banks came to an agreement as early as December 2011 concerning the distribution of this advance payment on account.

A one-off payment is dispensed with where the person authorizes his or her Swiss paying agent in writing by 31 May 2013 to notify the German authorities of his or her data and assets (voluntary reporting of information). Apart from the person’s identity, place of residence and client number, the name and address of the Swiss paying agent, the annual account balances on 31 December are (providing the business relationship existed) to be reported for the period from 31 December 2002 to 31 December 2012. The Swiss paying agent will issue the person a certificate on the information reported, this also being deemed as proof of legalization.

What is important in this context is that taxpayers who have always complied with their tax obligations in Germany should also choose voluntary reporting by the Swiss paying agent otherwise the one-off tax payment will be applied quasi-automatically, and thus multiple taxation would ensue.

This means that all those who, for whatever reason, neglect to instruct the paying agent to report their information voluntarily by the deadline (31 May 2013) run the risk of double or multiple taxation.

Here, too, at any rate in keeping with the underlying purpose and spirit of the treaty, there should be a right to claim reimbursement of the tax paid twice over. However, the agreement as worded does not explicitly provide for this.

The voluntary reporting of such information not previously disclosed to the German tax authorities is to constitute constructive voluntary declaration, i.e. from the time of written authorization to the Swiss paying agent to report the information.

There is presently discussion in this context as to what extent voluntary declaration suffices since the text of the agreement refers to “reported bank and custody accounts”. There is a need to clarify this issue particularly in view of the more aggressive rulings handed down by the German Federal Court of Justice, Germany’s supreme court, and the enactment of the German Law Combating Unreported Income.

It is no less unclear how the German tax authorities assess the reported information, e.g. to arrive at a back-tax assessment.

Apart from the options of the one-off flat tax payment and the voluntary authorization of reporting by the Swiss paying agent, voluntary declaration pursuant to section 371 of the German Tax Code (AO) is another option for satisfying one’s back-tax liability with regard to previously untaxed assets.

The legal foundations and procedures are familiar to all concerned and are not changed by the agreement. However, the ruling handed down in May 2010 by the German Federal Finance Court, the clamp-downs introduced in 2011 with the German Law Combating Unreported Income, and the discontinuation of “partial voluntary declaration”, should be noted.

**Taxation of future capital income**

According to the agreement, the Swiss paying agents are obligated to retain withholding tax at a uniform rate of 26.375% and to forward it to the German tax authorities via the competent Swiss agency. The Swiss agency will retain a withholding commission of 1 % of the tax amount.

The individual paying the withholding tax can also have church tax additionally withheld and forwarded.

The assessment basis of this final withholding tax is, in essence, determined following the same rules as for German withholding tax.

Final withholding tax payments are effected anonymously. Here, too, the Swiss paying agent issues a certificate in accordance with the established procedure applicable to final withholding tax and the underlying data on which this is based.

As an alternative to the anonymous payment of final withholding tax, the taxpayer also has the option of having voluntary notification made to the German tax authorities. The content of the notification includes the taxpayer’s identity, place of residence and client number, the name and address of the...
Swiss paying agent, in addition to the tax year and the relevant positive and negative income figures.

**Securing the purpose of the Agreement**

In order to secure the purpose of the Agreement, namely of taxing assets held in Switzerland, Germany may request information for periods subsequent to the entry into force of the Agreement by providing the identity of the taxpayer residing in Germany and a plausible reason for the request. The name of the Swiss bank is not required. A plausible reason is present when the German authority considers it opportune to audit the figures reported by taxpayer, taking into account all of the circumstances regarding the taxpayer known to it (income situation, information returns, representations of the taxpayer, and knowledge of persons preparing the tax return).

The Swiss agency with whom the request is filed makes inquiries of all Swiss banks as to the existence of current and custody accounts for the specified time period and the German authorities are then informed of the bank and accounts as applicable. Otherwise a negative finding notice is issued.

The person with a German tax liability is informed of the information request by the German and Swiss authority. The person has the option of recourse to legal action to verify the legality of the request.

In order to obtain further information, the German authority must then seek administrative or judicial assistance.

The number of information requests is limited to a maximum of 999 for the first two years upon the entry into force of the Agreement. The maximum number for the year of entry into force and the year following is set by a joint committee composed of representatives of both states set up after the entry into force of the Agreement. From the third year on, adjustments will be made to the maximum number ranging from -20% to +20% of the initial figure.

As mentioned above, information requests are permitted only for the periods subsequent to the entry into force of the Agreement; inquiries as to data on previous periods may, however, also be made if the “first” query resulted in previously unknown bank or custody accounts coming to light.

Furthermore, Switzerland is obliged to notify Germany about the countries to which assets flowed during the period between 21 September 2011 and 31 May 2013. Notification is to be made for the ten most important countries, with the amount of the assets and the number of persons per country to be indicated.

**Ratification and entry into force**

The Agreement is scheduled to enter into force on 1 January 2013. The Swiss paying agents are then to notify the persons affected within two months.

Being an international agreement, it must be incorporated into national law by both states party to it and ratified by their respective legislative bodies.

Approval by the legislative body or by way of a plebiscite is currently not called into question.

In Germany, the legislative authority for income and wealth tax lies with the federal government. Ratification is also subject to the approval of the Bundesrat, the legislative body representing Germany’s sixteen states. The parties in government (CDU/CSU-FDP) do not currently have a majority in the Bundesrat.

The ratification process is expected to be completed by the autumn of 2012.

In a statement issued on 1 December 2011, the SPD group of members of the Bundestag commented at length on the agreement and put its hostile stance on record.

As well as expressing the views documented in the political media, it also makes reference to a possible violation of European law. However, it should be noted that the issue is not the illegality of individual national provisions contravening such principles as the freedom of establishment or free movement of capital, but rather the possibility of an EU member state (in this case the Federal Republic of Germany) acting beyond its
authority in matters exclusively reserved to the EU.

The core issue is that the treaty not only provides for the legalization of the past but also the taxation of future earnings as well. The latter, however, is already covered by the EU Savings Directive (2003/48/EC) and the agreement between the EU and Switzerland pertaining to the taxation of interest (part of the “Bilateral II” treaties).

On 25 October 2011, Algirdas Šemeta, the Commissioner responsible for taxation, responded to written questions put by the European Parliament to the European Commission on 3 October 2011 with regard to the German-Swiss and UK-Swiss tax treaties.

Commissioner Šemeta stated that, at 26.375%, the withholding tax rate contained in the German-Swiss agreement was substantially below the 35% tax rate provided for in the EU-Swiss Savings Tax Agreement. This result was achieved by way of a refund of withholding tax. In addition, a tax having the effect of final settlement (in contrast to a withholding tax functioning as like an advance payment) was less suitable for deterring tax evasion.

He emphasized that, while EU member states were free to enter into international agreements with non-EU countries at any time, EU law and the EU’s competence had to be respected. Member states must, he said, ensure that matters that are reserved exclusively to EU competence are not covered by such treaties, this extending in particular to areas that fall under the EU Savings Directive. He noted that in any event the agreement was having the effect of delaying the review of the Savings Directive. Nevertheless, the EU continued to be committed to an automatic exchange of information.

The political debate about the provisions of the agreement continues unabated in Germany as well.

Consequently the timeline for implementation into national law seems somewhat ambitious.

Summary and outlook

With the agreement Germany and Switzerland have a viable instrument for a simple and anonymous return to tax compliance. Taxpayers are able to choose the right option for their individual situation.

Based on the experience gained during the past few years with regard to voluntary declarations, back-tax liability including interest and penalties is substantially below the 19% minimum tax rate applicable to assets. This is particularly the case when tax credits are applied and no inheritance or gift tax is applicable during the period in question.

However, the taxpayer should always weigh the pros and cons of the individual options and consult tax specialists, particularly when confronted with criminal tax law issues. The risk of multiple taxation ensuing from letting the voluntary reporting date lapse must also be considered.

For the many issues raised here, the reader is referred to the guidelines published by the Swiss Federal Tax Administration on the application of the agreement.

How the situation pertaining to the possible violation of EU law will develop is uncertain. No predictions can be made at present whether this alone or the confluence of other implementation issues will result in attempts to renegotiate the deal or to a complete failure of the agreement.

Important changes apply to the documentation for exports and intra-Community supplies from Germany

The German parliament has approved important amendments to the German VAT regulations1 which will become legally effective on 1 January 2012. As a result, considerable changes apply to the documentary proof required to support the VAT zero-rating for exports and intra-Community supplies of goods2. These changes will affect all businesses that make cross-border sales of goods from Germany.

The German tax administration has announced that a transition period will apply until 31 March 2012. During the transition, the authorities will accept documentary proof according to the previous regulations (which expires on 1 January 2012). Furthermore, draft guidelines for these regulations are expected to be finalized by the Ministry of Finance soon, possibly early in 2012.

The main changes include the following:

**Documentary proof of exports of goods**

For exports of goods outside the European Union (EU), the current preferred requirements for documentation become compulsory. In other words, “should” rules are replaced by “must” rules. Generally speaking, it will no longer be possible to provide alternative proof of export during VAT audits. Under the new rules, the proof of export from the ATLAS3 system is defined as the “standard proof.”

Alternative forms of proof (such as bills of lading, airway bills or freight forwarder certificates) will only be accepted if the export has not been declared using the electronic ATLAS procedure or, in special cases, if the electronic export procedure could not be completed as required.

These changes mainly reflect the tax authorities’ position on preferred documentation as already laid down in the regulations and in various Ministry of Finance letters. However, the legal effect of the new rules is stronger.

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1 Umsatzsteuer-Durchführungsverordnung.
2 A cross-border supply of goods sold by a taxable person in one EU Member State to a taxable person in another EU Member State is called an intra-Community supply.
3 ATLAS is the German electronic customs administration system that has to be used in order to clear customs.
Changes regarding documentary proof for Intra-Community supplies

The changes that affect intra-Community supplies are even more extensive than the changes that apply to exports. In addition to a change from “should” to “must” rules, the tax administration has introduced a new “standard proof” document, the Gelangensbestätigung (a confirmation of arrival). In future, an intra-Community supply will only be accepted as zero-rated if a confirmation of arrival document is available. The confirmation of arrival document must contain the following information:

- The name and address of the customer
- The amount and tariff classification of the goods supplied
- If the goods are transported by the supplier or on behalf of the supplier or on behalf of the customer, the place and date of receipt of the delivered goods in another EU Member State
- If the goods are transported by the customer, the date and place of the end of the transport in another EU Member State
- The signature of the recipient or carrier as confirmation of the receipt or transportation of the goods, respectively

The Ministry of Finance has provided a draft form of the certificate – also in English and French. The documents are still being finalized by the German tax authorities.

Intra-Community transport supplies arranged by a freight forwarder

If the transport is supplied by a freight be kept by the transport company and forwarder, courier service or similar not by the supplier, provided that the supplies arranged provider, the tax administration accepts documentation can be shown to the by a freight forwarder that the confirmation of arrival proof can tax authorities without undue delay.

Intra-Community chain supplies

It is currently unclear what the tax administration expects the confirmation of arrival documentation to be in the case of chain supplies (ABC transactions). It seems likely that the first customer in the chain (the middle entity, or party B) will obtain information about the arrival of the goods to the final customer (party C) and then confirm this to the first supplier (party A). Of course, this may prove difficult in practice, especially in chains involving multiple parties.

What is the likely impact?

The requirements for proof of export and for intra-Community supplies under the new regulations are much stricter than applied previously. Whereas, in the past, intra-Community supplies could generally be proven using alternative documents (for example freight documents, haulage contractor certificates (Spediteurs-bescheinigung) or even subsequent confirmation from the customer) the tax authorities will now always require proof of receipt of the goods. Taxpayers should review their current documentation practices and assess whether they comply with the new rules.

The German tax administration’s strict position could potentially be challenged under community law and in the light of the Court of Justice of the European Union (CJEU) case Collée. Arguably, according to EU legal principles, zero-rating should be granted in all cases if it is certain that the goods have arrived in another Member State, even if the documentation does not accord with the rules set out by the tax administration. However, taxpayers should not rely on this defense. It seems likely that German VAT auditors and general tax auditors will insist on receiving the legally required confirmation of receipt (Gelangensbestätigung) for all transactions that take place after 31 March 2012 (the end of the transition period) and that they will at least initially seek to apply German VAT to transactions that are not supported by the required documentation.

Special caution should be exercised in situations where the supplier may need to rely on the defense that he “acted in good faith,” for example, because the customer is subsequently shown to be a fraudulent trader. The German tax courts (including the Supreme Tax Court) have repeatedly confirmed that one of the conditions that must be satisfied to apply this rule is having documentary proof that is fully in line with the legal requirements of the German law (Umsatzsteuer-Durchführungsverordnung).

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4 C-146/05 of 27 September 2007.
5 Section 6a paragraph 4 German VAT law.
VAT – Changes in the real estate sector

Susanne Gantenbein, Partner, Indirect Tax, Geneva, susanne.gantenbein@ch.ey.com
Mirjam Holzer, Manager, Indirect Tax, Berne, mirjam.holzer@ch.ey.com

The eagerly awaited second draft of VAT Sectors Information 17 "Property management/leasing and sale of real estate" was published on the website of the Swiss Federal Tax Administration on 26 October 2011. We do not expect the final Sectors Information to contain any changes from the second draft.

The changes primarily concern the following seven areas:

1. Taxation of services according to the destination principle;
2. Expansion of right to opt for VAT-exempt without credit turnover with respect to real estate;
3. Options for transferring property;
4. Distinction between taxable supply of installed goods and VAT-exempt without credit sales;
5. Input tax deduction regulations for the construction of buildings;
6. Input tax deduction on development costs;
7. More liberal rules on vacant properties.

The first fundamental change concerns the destination principle, which has generally applied to the supply of services since 1 January 2010. Under this principle, services are taxed based on the place of the recipient of the service. However, this change only concerns those services that do not relate individually or specifically to a particular property – such as legal services associated with neighbor disputes. By contrast, services that closely relate to a particular property will continue to be taxed based on the location of the property. This includes the procurement and management of properties, the coordination of construction work and accommodation services.

The second change concerns the right to opt for VAT-exempt without credit turnover with respect to real estate. Revenues resulting from the sale and lease of properties can now be taxed on a voluntary basis provided the properties are not used solely for private purposes. Furthermore, this option no longer requires an option application to be submitted to the Swiss Federal Tax Administration, Main Department VAT (SFTA), merely that the tax be included on the invoice or purchase/rental contract. If an option is subsequently exercised on a lease, this is classified as a rent increase and the contract must be amended accordingly.

The third change concerns the option to transfer real estate via the notification procedure, provided the parties to the contract are registered for Swiss VAT purposes and the real estate is not used solely for private purposes. In addition to a transfer via notification procedure, it is still possible to transfer real estate with or without option. The advantages/disadvantages of the different methods of transfer should be analyzed at an early stage in the sales process and we recommend that the selected option is taken into consideration when drawing up the purchase contracts by including specific VAT clauses.

The fourth clause concerns the VAT qualification of land development costs. Under the new VAT law, land is no longer qualified as part of the building costs and are taxed at the standard VAT rate. However, if development costs are clearly presented upon sale, they are qualified as part of the building costs and are taxed at the standard VAT rate. If, when purchasing the land or initially developing it, expenses are incurred on which input tax has been charged, these may be deducted according to the use of the buildings (both existing and future) erected on the land.

The seventh change concerns the rules on vacant properties. Under the old VAT law, in cases where real estate that was previously used for taxable purposes is subsequently left vacant for more than 12 months, self-supply could have occurred as a result of a change of use. However, under the new VAT law, there are no restrictions on the period a building remains vacant.
On 1 November 2011 the Swiss Federal Tax Administration (FTA) published its VAT Financial Brochure 14 on the Financial Sector and the catalog of services in the second, now presumably definitive version. Compared to the previous VAT brochure no. 14 dated 1 October 2009, the second draft contains – along with numerous, smaller changes – a substantial new element: a redefinition of the term “brokerage” for the financial sector.

The new VAT Info 14, Financial Sector, redefines the term “brokerage”. While previous practice used only the very restrictive regulations governing agency in determining the existence of brokerage services, the new definition of intermediation is broader. It includes any activity carried out by an intermediary in this function that consists of working towards concluding a contract between two parties without being a party to that contract. The nature of the compensation and the designation of the broker will in future also have no influence on the qualification of a service.

The new interpretation of brokerage will also have the effect of restricting the term “Finder’s Fee”. Finder’s Fees will now only be taxable where the intermediation is not based on a specific sales transaction or is unrelated to transactions that are subsequently carried out with the client (e.g. provision of client data or client information, performance of a market analysis or participation in client events). This redefinition will particularly affect asset managers, who up to now have usually only collected taxable retrocessions. Retrocessions will now have to be split between those that are taxable and those that are VAT exempt without credit, with broker thus facing an input tax correction. While this in principle widens the scope of VAT exempt without credit retrocessions, a limitation is, however, imposed by the fact that in the case of a contractual duty to deliver financial payments in accordance with Art. 400 para. 1 CO, the tax authorities will assume a self-interest in the contents of the contract and thus deny VAT exemption for the brokerage service being supplied. The definition of brokerage will from now on also include sub-intermediaries.

Although the key elements of the new definition strongly coincide with those appearing in European case law, we cannot yet say to what extent legal practice under the new VAT Info 14, Financial Sector will also follow that of the European Court of Justice. This will require further analysis, in particular as regards the practical consequences of the restricted definition of brokerage due to the contractual duty to deliver in accordance with Art. 400 para. 1 CO.

Another noteworthy change in relation to the first draft and previous practice relates to VAT exempt without credit revenues where there is no entitlement to claim VAT input tax deduction. The omission of the addendum “necessity for the unchanged supply” of an outsourced VAT exempt without credit bank service to a recipient of the service from the outsourcing bank indicates that it is likely that the VAT qualification will be retained.

As regards passive investment companies, the draft redefines the term “passive investment company” and stipulates the conditions under which liability can be enforced against the beneficial owner. The wording here largely corresponds to that of Brochure 14, Financial Sector of September 2000.

The question as to whether paying-in slips provided for a consideration represent a taxable supply of forms, or a VAT exempt without credit payment transaction is being resolved; such supplies are definitively liable to tax.

Furthermore, the catalog has now been extended to include gold held by banks.
The merger of a company with a company that it wholly owns (a parent/subsidiary merger) raises the question of how any merger profit or loss is to be treated under commercial and fiscal law. The following brief description is intended as a non-technical explanation of the treatment of merger profits and losses in practice.

1. The recording of merger profits and losses from parent/subsidiary mergers under commercial law

1.1. Merger profits

If the book value of the net assets acquired exceeds the book value of the investment, the result is a merger profit. There are several different ways of recording a merger profit resulting from a parent/subsidiary merger in the acquiring company’s books. In particular, a merger profit resulting from a parent/subsidiary merger can be recognized either in income (affecting profit) or in equity (not affecting profit). The Swiss Auditing Manual (Handbuch der Wirtschaftsprüfung) states that the following options in particular are permissible:

- Recognition in income: this option acknowledges the fact that a profit has been realized.
- Recognition in equity via statutory reserves, analogous to the treatment of the merger agio in the event of a merger with capital increase. This option is in line with the fact that the merger is similar to an investment.
- Recognition in equity via free reserves: this option acknowledges the fact that no formal capital increase has been conducted, and that accordingly, a surplus can be allocated to uncommitted equity capital.

1.2. Merger losses

If the book value of the investment is higher than the book value of the net assets acquired, the result is a merger loss. A merger loss can also be recognized in income or in equity (charged directly to freely disposable equity capital). Business-management factors may often speak in favor of the latter option, for example in order to avoid a reduction in profit in consequence of a matter not arising as part of operational business.

A merger loss can also be capitalized as goodwill, provided the intrinsic value of the holding is at least equal to the book value of the relevant investment. The effect of this is that there is no immediate charge to the acquiring company’s equity capital. Instead, as a rule, the asset shall basically be written off over five years.

2. Treatment under income tax

2.1. Merger profits

If the acquisition of assets and liabilities under a parent/subsidiary merger generates a merger profit at the level of the absorbing company, then the profit is in principle liable to income tax. It should be noted at this point that such treatment of any merger profit from a parent/subsidiary merger is independent of whether the profit was recognized in income or in equity in regard to commercial law. In the latter case there is a deviation from the authoritative principle (deviation to the taxpayer’s detriment) for the purposes of income tax. The income tax burden of any merger profit can be lessened at most by the participation relief, but due to the application of the concept of the indirect exemption of investment income, the absorbing parent company would not benefit from such relief if there are tax loss carry forwards.

2.2. Merger losses

If the acquisition of assets and liabilities under a parent/subsidiary merger generates a book loss at the level of the absorbing company, then in principle the loss is not tax-deductible. However, this applies only to what are known as “unreal” merger losses (i.e. when hidden reserves and goodwill at the level of the transferring subsidiary make up for the book loss at the level of the absorbing company). If, however, the merger loss can be attributed to an overvaluation of the investment in the transferring subsidiary (known as a «true merger loss»), then the merger loss is in principle tax-deductible by the absorbing company. The reference date for determining whether the merger losses are «real» or «unreal» is the day on which the merger takes effect. In the case of the recognition in income of a (real) merger loss, the expense is also justified on commercial grounds for tax purposes. In our view, tax deductibility should also be granted in the case of the recognition in equity of a (real) merger loss, particularly in light of considerations from a tax-system perspective in connection with the treatment of merger profits described above. In this case there is once again a deviation from the authoritative principle, but this time to the taxpayer’s benefit.

3. Summary

In each individual case, clarifications must be made in advance about the appropriate method of recording the transaction under commercial law. In parallel to this, the qualification of the transaction under tax law must be agreed with the responsible tax authority by means of an upfront tax ruling.
The non-applicability of statutory limitations in tax criminal law

Federal law on adapting the Law on Direct Federal Taxes and the Federal Law on Tax Harmonization to the general conditions of the Swiss Penal Code.

With the consultation procedure of 15 June 2011, the Swiss Federal Tax Administration (SFTA) presented the federal law on adapting the Law on Direct Federal Taxes and the Federal Law on Tax Harmonization to the general conditions of the Swiss Penal Code. This initiative is intended to adapt the limitation periods for prosecution and sanctions for offenses in the Law on Direct Federal Taxes and in the Federal Law on Tax Harmonization in line with the general section of the Swiss Penal Code. Efforts will also be made to achieve alignment with the Federal Supreme Court Act (FSCA), although this aspect is not covered by this article.

As a particular consequence of these new rules, by applying the objectives defined in Art. 333 of the Swiss Penal Code to the tax laws (Law on Direct Federal Taxes and Federal Law on Tax Harmonization) the limitation periods for prosecution are also to be adjusted at the same time in line with the Swiss Penal Code. The limitation periods for offenses (e.g. tax fraud, embezzlement) will therefore be increased from 10 to 15 years. Furthermore, according to the draft, there should no longer be any grounds for interruption of the limitation period. The limitation period for prosecution will no longer apply if a ruling has been made by the court of first instance, before expiry of the limitation period, meaning, for the purposes of the draft amendment, the issuing of an order by the relevant cantonal tax authorities or the relevant cantonal prosecution authorities. For infringements such as tax evasion, for example, this means that the regulatory provisions of the cantonal tax authorities are sufficient to trigger the non-applicability of statutory limitations even in straightforward violations of requirements. The proposed law is to be discussed at the meeting of the Federal Council on 9 March 2012, and is likely to be approved.

The statute of limitations is not new; Roman law called it «longi temporis praescriptio». Even in those days there was clearly a desire, after a certain period, to establish legal repose and it was in the interests of law enforcement to require prosecutors to do their work without delay. The statute of limitations for criminal offenses constitutes a procedural impediment, i.e. it means that the offense can no longer be prosecuted. It follows that a rule making statutory limitations non-applicable means that offenses or infringements can be prosecuted indefinitely. The basic aim of the legal mechanism of statutory limitation is to establish legal certainty and legal repose. Since – depending on the severity of the offense – society’s interest in pursuing a prosecution may also decline with the passing of time, a period of limitation may still be justified particularly in criminal law.

Swiss criminal law distinguishes between three types of crime depending on severity: infringements, punishable by fines (and sometimes also by imprisonment); offenses, punished by fines and/or imprisonment, and finally felonies, which carry a custodial sentence.

The definition of infringements includes the following for direct federal taxation and for cantonal and municipal taxes: the violation of procedural obligations, tax evasion, attempted tax evasion and the concealment or diversion of legacies in the inventory process. A tax offense means tax fraud involving the deliberate use of false, forged or untruthful documents for the purpose of tax evasion or for substantiating false information entered on the tax return.

The question therefore arises as to why the legislators are so keen to intensify the criminal law as it applies to tax. By proceeding with this standardization, the legislators’ primary intention is to adjust the limitation periods for tax fraud (an offense) which are shorter on the basis of Article 333 paragraph 6 of the Swiss Penal Code, in contrast to the less serious crime of tax evasion an (infringement). It is further intended to prevent tax evaders from being able to extricate themselves simply by recourse to the statute of limitations as a legal remedy. However, as previously shown, this adjustment does not increase limitation periods for serious felonies, but actually results in a further tightening for infringements.

It should also be mentioned that, owing to the non-applicability of statutory limitations to the aforementioned infringements where an order has been issued by the tax authorities, there is now a risk that proceedings may now become inordinately protracted for the taxpayer. Although the draft does consider this circumstance, it does oblige the taxpayer to make a complaint on the basis of the prohibition on delay in Article 8 of the Federal Constitution or the promptness requirement under Article 6 of the European Convention on Human Rights. It is therefore no longer up to the authorities to check that they are guided by the limitation rules, but rather the responsibility of citizens themselves to claim their right to be dealt with quickly under the complaints procedure.

The guaranteed rule of law is fundamental, and, while legal certainty, as an element of it, will indeed always need to be balanced against fairness, it does seem that, where the prosecution of infringements in particular is concerned, a boundary should be drawn here and, in view of the «minor» criminal nature of these offenses, that a period of limitation should continue to be allowed in tax criminal law.
New tax regulations for public transportation companies

Serge Migy, Senior Manager, Corporate Tax Lausanne, serge.migy@ch.ey.com
Benjamin Marchat, Assistant, Corporate Tax Lausanne, benjamin.marchat@ch.ey.com

With the entry into force on January 1, 2010 of the Federal Act on Railways Reform 2, the tax regulations governing public transportation companies have been quite substantially amended insofar as direct taxes are concerned. Only concessional activity is tax-exempt from now on. A circular published recently by the Federal Tax Administration (Circular No. 35 of December 11, 2011) clarifies the implications of the new tax regulations for such companies.

Introduction
The overall intention behind the Railway Reform 2 Bill is to promote equal treatment among transportation companies in different areas (financing, access to infrastructure, etc.).

In spring 2009 the Federal parliament adopted an initial package of amendments to the law, within the afore-mentioned bill (Federal Law on Railway Reform 2 of March 20, 2009). This new law has a tax section which has led to a major change to the system with respect to exemption for public transportation companies.

In the past, under the former legislation, concessional transportation companies were exempt from direct federal tax if they were considered relevant from a transportation policy point of view and, if they had made a net profit during the fiscal year considered, provided no dividends had been paid out during the two preceding years.

At a cantonal level, the Federal Law on the Harmonization of Cantonal and Communal Direct Taxes granted the cantons major flexibility to determine the extent of the exemption of public transportation companies.

The flexibility with which the cantons could define the exemption conditions led to undesirable differences in the way transportation companies were treated. This problem is corrected in Railways Reform 2. Hence the tax exemption conditions of public transportation companies have been clearly and consistently established for direct federal taxes and for cantonal/communal taxes.

New tax exemption regulations
Henceforth, in order to benefit from a tax exemption, public transportation companies must benefit from a concession from the Confederation. These transportation companies must also receive indemnities for this activity or must, because of their concession, run a service of national importance throughout the year.

These new tax regulations now consider a single criterion: the federal concession. The subjective rules for determining whether or not a company should be tax exempt are no longer applicable.

According to the newly-adopted tax regulations, there is from now on no tax exemption for ancillary businesses and real estate property which would not be essentially connected with the activity under concession.

The Swiss Federal Tax Administration: Circular No. 35 of December 11, 2011 (hereinafter FTA Circular No. 35) takes an in-depth look at complementary and ancillary activities in order to define criteria to help determine whether or not a particular activity should benefit from tax exemption. The Swiss Federal Tax Administration (FTA) has adopted the criterion of the 'essential connection' so as to permit the exemption of an accessory business.

Tax opportunities granted under FTA Circular No. 35
The existence of a taxable sector of activity requires the public transportation company to identify the values on the basis of which the tax on the profit and the capital of this activity is to be determined. In that respect, the issue of how to deal with hidden reserves must be looked at carefully. FTA Circular No. 35 grants taxpayers a period until the end of financial year 2012 for reporting hidden reserves in the commercial balance sheet without tax consequences. The Circular states that, provided the reporting of hidden reserves is allowed by commercial law, disclosure of hidden reserves shall be done through the commercial balance sheet. Hidden reserves that cannot be mentioned in a commercial balance sheet under commercial law can be entered in a complementary fiscal balance sheet.

The possibilities offered by the Circular for considering hidden reserves on certain assets without tax consequences, must be carefully examined by the taxpayers concerned. The practice of the tax authorities will help to define the conditions for applying this important provision of transitional law more precisely.

Actions to be undertaken by taxpayers
Public transportation companies that carry out a taxable activity must make sure that the activities undertaken are properly delimited in the accounts kept by sector. The accounting of figures by sector will be determining for filing the tax return.

Public transportation companies affected by these amendments to the legislation should carry out an in-depth examination of the impact of such amendments on their year-end financial statements. Indeed, lack of action in this respect while setting up the commercial balance sheet might, in the long run, have significant consequences on the determination of the tax base of an operating asset in the event of its sale or change in use.

The new tax regulations limiting the exemption of concessional activities will call for taxpayers to pay great attention to changes in allocation of assets. As an example, hidden reserves which would be allocated from a taxable sector to an exempt sector are immediately taxable (tax settlement as soon as the allocation changes).
Developments at cantonal level in Central Switzerland

Viktor Bucher, Partner Tax Services, Zug, viktor.bucher@ch.ey.com
Jessica Beller, Assistant Tax Services, Zug, jessica.beller@ch.ey.com

In an attempt to maintain their attraction as business locations, a number of cantons in Central Switzerland have modified their tax regimes. The revisions essentially involve the transposition of superordinate federal laws into cantonal laws. The advent of Corporate Tax Reform II has made various adjustments to cantonal tax legislation necessary such as easing the burden of the double taxation of income or the introduction of the capital contribution principle.

The following sections introduce further interesting changes that have been introduced in the cantons in Central Switzerland.

Canton of Lucerne
In the revision of its tax legislation in 2011 the Canton of Lucerne decided to reduce corporate income tax in a number of stages, having already reduced it by 25% in 2010. From 2012 it is to be halved. This will result in a basic corporate income tax rate of 1.5% (Lucerne tax multiplier: 350% (provisional rate for 2012), thereby making Lucerne one of the most attractive Swiss cantons in terms of corporate income tax rates.

Canton of Nidwalden
The Canton of Nidwalden amended its tax legislation with effect from 1 January 2011. In an attempt to increase its competitiveness, it reduced its corporate income tax rate to 6% and its capital tax to 0.1% (flat tax rate). Particularly worthy of mention is its unique «patent box» regime aimed at promoting academic and economic progress by reducing by 80% tax on net income derived from patents, resulting in a cantonal corporate income tax rate of 1.2% (flat tax rate). At the same time, the limit in terms of proportion and amount imposed on provisions for research and development costs has been eliminated.

Canton of Obwalden
On the basis of its long-term 2012+ strategy introduced in December 2002, the Canton of Obwalden has modified its tax legislation in a series of partial revisions in response to ongoing tax competition. These revisions have involved the introduction of the flat tax rate and the reduction of the corporate income tax rate to 6%. As a result of positive developments in tax revenue, with effect from 1 January 2012, tax relief will be available to families (a deduction for children) and to persons in the lower and middle income brackets (a special deduction).

Canton of Schwyz
The corporate income tax rate is 2.25% and the minimum tax rate (capital tax) 0.4% (Schwyz tax multiplier: 343%). If corporate income tax proves higher than the minimum tax, the latter can be offset against the corporate income tax or only the corporate income tax is to be paid.

Canton of Uri
The Canton of Uri modified its tax legislation with effect from as early as 1 January 2011 in order to remain attractive in tax competition with the other cantons. It reduced its basic corporate income tax rate to 4.2% (Altdorf income tax rate: 5.098%).

Canton of Zug
In the referendum of 25 August 2011 the Canton of Zug voted in favor of amending its tax legislation. In an effort to secure its attractiveness as a place to live in and to enhance its status as a business location, the amendment to its tax legislation will bring relief to families, tenants, SMEs and large entities in particular.

SMEs will benefit mainly from having the corporate income tax rate payable on their first CHF 100,000 reduced from 4% to 3%. The corporate income tax rate for profits in excess of CHF 100,000 will be reduced in stages in order to remain competitive in the international arena. In 2012 the corporate income tax rate payable on profits in excess of CHF 100,000 will amount to 6.25%, which represents a reduction by 0.25%. In 2013 the basic corporate income tax rate payable on profits in excess of CHF 100,000 will be 6% and from 2014 5.75% (Zug tax multiplier: 148.8210%).

However, as in 2012, the Canton of Zug will not recognize deduction of corporate income tax from capital tax.

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