Dear Reader,

The year may be nearing an end but not the EU tax dispute: what will happen next? The article entitled “Is the license box the simple solution?” provides a possible answer. The lump-sum taxation issue will continue to occupy us into next year.

Other subjects explored in this newsletter are the Expatriates Ordinance and its development, as well as the Swiss Federal Supreme Court’s rejection of offshore financing of Swiss real estate groups.

In the area of indirect taxes, we report this time on new VAT invoicing rules in the European Union (Council Directive 2010/45/EU) and on the “Gelangenbestätigung”, the new German draft bill on proof of intra-community supplies. You will also find in this last issue of 2012 our traditional overview of tax developments at cantonal level.

On a personal note: we are now publishing our eNewsletter in English and German only. If you need further information in French on any of the subjects we have reported on, please let us know and we will provide you with details of whom to contact!
Finally, we would like to wish you and your families a peaceful Christmas and a good start to 2013.

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By end of year Switzerland is expected to make major progress in resolving the tax dispute with the EU. In the center of the debate is the issue that the domestic and foreign income of cantonal mixed companies is taxed differently. This has drawn criticism from the EU and the OECD. The Swiss Federal Department of Finance is currently negotiating with the EU over the exact details. Now cantons like Zurich, Geneva and Basel-Stadt, which generate high tax revenues, are raising their voices and have calculated the tax shortfalls that would arise if tax privileges (for companies) were ended. These shortfalls are actually considerable. If extensive corporate income tax cuts had to be made across the board to preserve international competitiveness, the national financial equalization system (NFE) would of course be affected. The «recipient cantons» that benefit from the NFE are now making their voices heard and pointing to the importance of federalism and solidarity. It is debatable whether the potential tax shortfalls will be plugged by the federal government, particularly of course as the Federal Department of Finance is tasked with ending the dispute with the EU without raising taxes. It is therefore important not only to consider alternative tax models, but also to bring them to the table in the negotiations with the EU. As a lifeline, a number of parties have proposed a license box regime, as this is already used in the EU. On closer inspection, however, it is quickly apparent that for the cantons this has its drawbacks. Although the license box approach is good, it falls too short, as mixed companies primarily generate revenues from trading. Given the fact that mixed companies, which produce high levels of tax revenues, rarely carry out research and development, they also produce virtually no license income either. A conventional license box would therefore neither produce the desired outcome nor plug the tax shortfalls. Clarity on this issue is therefore needed so as not to raise false expectations. A possible way forward, however, would be a modified license box, in which distribution networks, sales of client lists and relationships, goodwill etc. would be considered license income. A license box with this structure would prove a real alternative to the mixed companies, as it would not only plug the expected tax shortfall, but would be compatible with EU law.

Lump sum taxation - current developments at federal and cantonal level

Lump sum taxation in Switzerland is still under the spotlight. After several cantons have agreed or are about to agree to abolish or intensify lump sum taxation, there is now movement at federal level. Almost at the same time as the Federal Parliament decided to amend the federal law on lump sum taxation, a Swiss popular initiative to abolish lump sum taxation at a national level was submitted to the Federal Chancellery by left-wing organizations.

Background

Lump sum taxation (Aufwandbesteuerung or Pauschalbesteuerung in German) is a simplified procedure to determine the basis of assessment for foreign nationals domiciled but not gainfully employed in Switzerland. In Switzerland currently less than one in a thousand taxpayers are subject to lump sum taxation. Nevertheless, lump sum taxation has recently come more and more under attack. The argument that this form of taxation is unfair and violates the constitutional principle of taxation according to economic capacity is mainly brought forth.

This article gives a short overview of the current developments relating to lump sum taxation at federal and cantonal level.

Developments at federal level

Amendment of federal lump sum taxation legislation

At federal level, the Federal Council and Federal Parliament still refrain from abolishing lump sum taxation, primarily for economic reasons. However, it is the intention to improve the fairness of the taxation system and the acceptance in the population. Therefore, the Federal Council submitted a motion for revision of the federal legislation regarding lump sum taxation to the Federal Parliament. In the final vote of the autumn session 2012, the Federal Parliament has now approved this amendment.

After a five-year transition period, the following changes will be adopted:
(i) The global expenditure will be at least seven times the annual housing costs (currently five times) or three times the annual board and lodging costs (currently twice the cost); 

(ii) at federal level, a minimum basis of assessment of CHF 400,000 will be introduced; the cantons will also have to set a minimum basis of assessment which they can define freely; and 

(iii) the cantons will also have to take wealth tax into account when levying lump sum taxes.

The cantons have been accorded a two-year transition period to amend their legislation. As at federal level, there is also a five-year transition period at cantonal level for people who, at the time of amendment, are already subject to lump sum taxation («old cases»).

Swiss popular initiative
On 19 October 2012, almost at the same time as the Federal Parliament decided to revise the federal law on lump sum taxation, left-wing organizations jointly submitted the «Schluss mit den Steuerprivilegien für Millionäre (Abschaffung der Pauschalbesteuerung)» popular initiative with 103,000 certified signatures to the Federal Chancellery. The Federal Chancellery has now confirmed the valid conclusion of the popular initiative. Thus, Swiss voters will have to vote on this initiative in the next two to three years. The popular initiative seeks to abolish lump sum taxation at a national level. The initiators consider the intensification of the lump sum taxation decided by the Federal Parliament as unsatisfactory, as it does not go far enough to ensure that the taxation system is fair or respects the constitutional principle of taxation according to economic capacity. If approved, the initiative will result in the abolition of lump sum taxation no later than three years after the initiative was given the green light by popular vote and the majority of the cantons.

Developments in the cantons
Besides the changes at federal level, a number of developments regarding lump sum taxation have taken place at cantonal level over the past few years. Some cantons have already abolished lump sum taxation; others have intensified the conditions and provisions or corresponding motions are pending. A pattern is discernible: in cantons that are home to relatively few lump sum taxpayers this instrument is being abolished; whereas it is being retained or intensified in those cantons that accommodate a larger number of lump sum tax payers.

Cantons where lump sum taxation has been abolished
The Cantons of Appenzell Ausserrhoden, Basel-Stadt, Basel-Landschaft, Schaffhausen and Zurich have abolished lump sum taxation through referendum (or by a decision of the Great Council in the case of Basel-Stadt) respectively permit it only for the year of arrival regardless of nationality.

Cantons where the conditions and provisions on lump sum taxation have been intensified
The Cantons of Berne, Lucerne, St. Gallen and Thurgau have militated against the abolition of lump sum taxation and for an intensification of the conditions and provisions regarding lump sum taxation. Similar to the draft at federal level, they envisage to introduce a minimum basis of assessment (or a minimum tax burden in the case of Thurgau) and an increase in the minimum multiplier for housing costs. Furthermore, most of these cantons have also introduced a wealth tax.

Other developments
The Canton of Zurich, the first to abolish lump sum taxation back in January 2010, reported that around half of its lump sum taxpayers had left within a year. According to a study, half of the former lump sum taxpayers that have stayed in the canton now pay less tax than before. Overall the Canton of Zurich now reports, contrary to its expectations, lower tax receipts since lump sum taxation was abolished.

The Canton of Vaud, home to the highest number of lump sum taxpayers in Switzerland, intensified the conditions and provisions relating to lump sum taxation back in 2009 by change of the cantonal practice. Efforts to completely abolish lump sum taxation have always failed up to now.

Outlook
After the motion of the Federal Council to intensify conditions and provisions regarding lump sum taxation at federal level, it was initially expected that the tensions provoked by lump sum taxation would ease, particularly as some cantons have gone down this path too. But since the Swiss popular initiative to abolish lump sum taxation at a national level was submitted, the issue is now back on the agenda. It remains to be seen how the situation for the lump sum taxation regime will evolve in the near future. In any case, it is time to look at alternative tax planning for foreign taxpayers that are resident but not gainfully employed in Switzerland.
Expatriates Ordinance - Quo vadis?

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Legislative history of the Expatriates Ordinance
Over 12 years ago, the government and most cantons issued special guidelines allowing employees seconded to Switzerland to deduct from their income tax any special business expenses connected with the secondment (such as relocation costs, reasonable (double) housing costs in Switzerland, the cost of sending children under the age of majority to a foreign-language private school) in addition to general business expenses. These expat allowances were granted on condition that the seconded employee was gainfully employed for a limited period (maximum 5 years) and that the employee maintained a permanent residence in the home country or intended to return there in the foreseeable future.

While the practice of tax authorities was regarded as rather “generous” in the first few years after these guidelines were introduced, there has been a real sea-change in the past few years; in that tax authorities have now begun to interpret the guidelines much more restrictively, only allowing “classic” expatriates to claim special business expenses.

Practices tightened up through court rulings
Practices have been tightened up based on various cantonal tax court decisions in which expatriates had claimed special business costs. The actual leading case was that of the Zurich Tax Appeals Commission II (from 1.1.11: Tax Appeals Court) dated October 2007 which held that the Expatriate Ordinance was both unlawful and - at least to some extent - unconstitutional. The deductions claimed for (double) housing costs and private school fees were therefore rejected. This decision was followed by further court decisions on this issue:

- In another decision in February 2011, the Tax Appeals Court regarded a COO as an expatriate, but rejected the expat lump-sum of CHF 1,500 per month, as no evidence had been produced that a permanent residence was being maintained in the home country.
- In June 2012, the Zurich Tax Appeals Court subsequently set aside a claim involving equal treatment in cases of illegality, clearly reaffirming the view that the Expatriate Ordinance fell afoul of legal and constitutional provisions and therefore violated the principles of legality and equality before the law. The deductions claimed were rejected.
- In a recent decision (September 2012), the Aargau Tax Appeals Court made reference to the Zurich decision, denying a claim for deduction for double housing costs for an employee seconded to Switzerland from India.

Summary
Various courts have now held that the Expatriate Ordinance is unlawful. This unlawful state of affairs has been taken up at political level and the tax privileges granted to expatriates are being discussed in detail at the moment. A motion was also submitted in June 2012 requesting that the Federal Council amend the legal provisions to remove the tax allowances currently provided for in the Expatriate Ordinance. The Federal Council published its position on this in August this year, stating that it saw no reason to overhaul the existing legislation, but that the conditions and requirements for individual allowances should be reviewed. Based on previous experience, this political process is unlikely to be implemented any time soon.

In terms of routine assessment practice, this means that the allowances for special business expenses should presumably still be granted, provided the expatriate in question is a “classic” expatriate, i.e. a key employee or specialist who is being sent to work in Switzerland by a foreign company under a special, fixed-term secondment agreement (maximum 5 years), who can provide evidence that a permanent residence is being maintained in the home country, establishes a tax domicile in Switzerland (i.e. is not an international weekday resident) and, if possible, remains covered under the social security scheme in the home country.

In February 2011, the Zurich Tax Appeals Court held that a citizen basically had a right to equal treatment in cases of illegality. This was because, in view of the cantonal tax authority’s illegal practice, it was inconsistent with the principle of equality before the law if the special deductions were granted by the cantonal tax authority, but denied on appeal. In the specific case in question, the deductions were rejected in any case, as the employee who had worked internationally for many years had not been seconded to Switzerland by a foreign group company, but was employed directly by a Swiss company.

Based on previous experience, this political process is unlikely to be implemented any time soon.
Swiss Federal Supreme Court rejects offshore financing of Swiss real estate groups

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On 5 October 2012 the Federal Supreme Court considered the issue of the tax recognition of offshore financing vehicles for Swiss real estate groups in a public hearing. The Federal Supreme Court denied such recognition, thus upholding the practice of the Swiss Federal Tax Administration. The Federal Tax Administration maintained that the financing of a Swiss real estate group through an offshore financing entity was unlawful, due to the fact that the income earned was effectively untaxed. The court’s written judgment has yet to be published.

Background
In the past, several Swiss real estate groups have managed their internal financing through financial entities in offshore countries (for example, Jersey, the Bahamas, Bermuda and the British Virgin Islands). To enable such financing, a subsidiary (financing entity), funded primarily by equity from the Swiss parent company, is usually established in an offshore country. Under this model, the foreign financing entity then provides the individual Swiss group companies with the necessary funding in the form of loans. Most of the interest earned on these loans remains untaxed in Switzerland as this falls under the applicable foreign tax legislation. The offshore finance income is then repatriated into Switzerland as dividend income that routinely becomes de facto untaxed income due to both, the absence of withholding tax provisions in foreign tax legislation and the tax relief claimed by the entity receiving such dividends in Switzerland.

The Federal Tax Administration clearly stated some years ago that financing a group through an offshore subsidiary, when the group companies are all based in Switzerland, constitutes tax evasion and is unlawful. This practice by the Federal Tax Administration led the majority of Swiss real estate groups to decide against having an offshore financing entity or to abandon any such entity given the pressure from the Federal Tax Administration.

The Swiss real estate group involved in this decision, however, continued to engage in offshore financing. As a result, the Federal Supreme Court was required to determine the issue of tax recognition in a public hearing on 5 October 2012 (Decision 2C_708/2011). The written judgment, including a detailed reasoning for the court’s decision, has yet to be published.

Case at hand
The case before the Federal Supreme Court involved a Swiss real estate group who only has Swiss subsidiaries. The group’s financing activities are managed by a permanent establishment of the Swiss-based financing company located in the Cayman Islands. The financing company maintains offices in the Cayman Islands and has 5 employees, each of whom works on a part-time basis at roughly 20% of a normal working week. The financing company has no employees in Switzerland. A tax ruling for the financing company with the Cantonal Tax Administration at the main tax domicile, attributed the income earned from financing activities wholly to its permanent establishment in the Cayman Islands, which unilaterally made such earnings exempt from Swiss taxation. The interest earned was also not taxed in the Cayman Islands. The Federal Tax Administration declared that the tax ruling would no longer be recognized in respect of direct federal tax. A corresponding tax assessment from the Tax Administration was contested by the financing company. The cantonal administrative court upheld the existence of a permanent establishment. On the basis of this decision, the Federal Tax Administration lodged an appeal with the Federal Supreme Court.

At the hearing the Federal Supreme Court concluded that the offshore financing of a Swiss real estate group was unacceptable and that the permanent establishment of the Swiss financing company based in the Cayman Islands could not therefore be recognized. Accordingly, all income generated from the financing activities in Switzerland was taxable.

Comments and future effects on practice
The decision of the Federal Supreme Court judges was unanimous. The court held that it was not the intention of the law to allow a group that is exclusively based in Switzerland to avoid taxation completely by outsourcing its financing activity within the group to an offshore branch. In terms of the rationale behind the decision, the Federal Supreme Court was divided into two fractions, which was the reason for a public hearing. Some judges were of the opinion that the financing activities in the Cayman Islands did not fulfill the requirements for a permanent establishment, which meant that all the income earned by the financing company was taxable in Switzerland. Other judges affirmed that a permanent establishment did exist, but held that the approach selected by the company was a form of tax evasion. The Federal Supreme Court ultimately found that the requirements for the approval of a permanent establishment had not been met in this case. The Federal Supreme Court remitted the case for further investigation by the cantonal administrative court with regard to the tax ruling.

The oral submissions made at the public hearing failed to clarify certain matters, leaving a number of issues unresolved. It can only be hoped that these will be dealt with in more detail in the written reasoning for the decision. Further clarification of the following matters is needed in particular:

- With regard to maintaining an international permanent establishment, the requirements for the tax recognition of such a permanent establishment were discussed. This discussion suggested in principle that certain material characteristics are implicit in the term “permanent establishment”. The exact requirements for these material characteristics have yet to be defined in detail. It is to be hoped that the requirements for the qualification as a permanent

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establishment will be defined more fully in the decision to allow the taxpayer to plan better and achieve greater legal certainty in the implementation of permanent establishment structures abroad.

- The issue of the binding effect of the tax ruling is also of particular interest. Given that the court of lower instance upheld the existence of a permanent establishment, it did not address the protection of legitimate expectations or the binding effect of the tax ruling. For this reason, the Federal Supreme Court remitted the case to the lower instance court for a more thorough investigation into the issues. Regardless of this, the judgment could establish interesting legal principles on the termination of rulings and the granting of an appropriate transition period for implementing any new structure.

This decision arguably has the potential to create greater legal certainty on a wide range of issues which are still unresolved. The extent to which the Federal Supreme Court will implement these will only become clear when the Court issues its written judgment. Nonetheless, it is already clear that the Federal Supreme Court decision will make the practice of implementing offshore structures in such circumstances all the more difficult.

VAT treatment of recharges - expenses with no added value

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Within their activity, many companies acquire services or incur costs on behalf of third parties, such as their clients or other business partners. Those services or costs, of diverse nature, are subsequently recharged to the effective recipients of the goods or services with no mark-up, i.e., for the exact same amount.

Though familiar with this frequent phenomenon, the truth is that companies are often faced with doubts regarding the correct treatment of recharges from a VAT perspective.

This article discusses some common recharge situations and provides functional and effective guidance on how to best deal with these transactions VAT-wise.

1 Basic situation
In a typical recharge situation company A acquires goods or services in its own name but on behalf of company B from a supplier who is unaware of this fact.

Fig. 1 shows a day to day example of a recharge and the questions that it entails, namely how company A should invoice company B for the expense recharged, i.e., should it apply VAT or not, and how should it book and deduct the VAT incurred.

The correct VAT treatment of the recharge will be dependent on various factors, i.e. whether the expense being invoiced to B separately or not. The following examples describe these different options. In any case, it is important to make a distinction between recharges and disbursements. The latter presume the taxable person incurred in costs in the name and on behalf of another party whereas a recharged service is acquired in its own name (see below § 5).

2 Absorption by the main supply
As a basic rule, art. 24 para. 1 Swiss VATL states that the consideration paid for the supply of a service or good includes in particular the reimbursement of all costs, even if they are invoiced separately. This means that if the expense...
is recharged in conjunction and linked to other goods or services charged by A which may be deemed to be the main supply, the expense will qualify as an ancillary cost and follow the same VAT treatment as the main supply.

In Fig.2 an example of such a case is shown. If company A is Ernst & Young and B a Client, both located in Switzerland, the main supply will be the advisory services performed by Ernst & Young. If, for the purposes of providing those services, Ernst & Young incurs hotel accommodation costs, it will recharge those exact costs to the Client with no mark-up (fig. 2):

The recharge of the hotel accommodation will be subject to VAT at the rate applicable to the advisory services (i.e. 8% Swiss VAT), even if the hotel is located abroad. Ernst & Young can recover the VAT paid on the accommodation either as input VAT in Switzerland or through a refund procedure abroad.

3 Duplication of the initial transaction

If the expense is recharged separately, i.e., independent of any other supply from A to B, we believe it should then follow the same VAT treatment as the initial transaction.

In effect, if A adds no value to the initial transaction and the expense is not ancillary to another supply performed by A, the VAT nature and qualification thereto remain the same. This follows from art. 20 para. 1 VATL according to which a supply is deemed to be made by the person who appears to the outside world to be the supplier. From B’s perspective, A is the supplier of the good/service which is the reason for the recharged expense.

A does not act as representative as he does not act in the name and for account of the hotel.

In the example portrayed by Fig.3 the recharge from A to B should follow the exact same tax treatment as the initial hotel supply. As such, A may apply the reduced VAT rate applicable to hotel accommodation when recharging this cost to B. This is the meaning of art. 20 para. 3 VATL according to which the supply relationship between the person appearing to the outside world (A) and the person actually making the supply (hotel) is qualified in the same way as the supply relationship between the person acting in relation to the outside world (A) and the person receiving the supply (B).

A is entitled to fully deduct the VAT irrespectively of its own deduction right - i.e., even if A carries out both taxable and exempt activities. In effect, as there is a direct link between the input and the taxable output - the recharge of the hotel cost - the input VAT is fully deductible.

However, B’s right to deduct the VAT on the recharge will be limited to its pro rata if B is a taxable person performing both taxable and exempt transactions.

It should be noted that if the initial transaction is exempt or outside the scope, so will the recharge be. As a corollary, if the expense was incurred abroad and attracted foreign VAT, A should also apply foreign VAT on the recharge to B.

In the example above, if A and B are based in Switzerland and the hotel is in France,
A would be required to register for VAT in France – appointing a fiscal representative therein – just for the purpose of recharging said cost to B with French VAT. This is, of course, hardly practical and may be avoided by way of invoicing the expenses jointly, as described above.

4 Disbursements
A distinction should be made between recharges and disbursements. The latter presume the taxable person incurred in costs in the name and on behalf of another (transitory items, Article 24 para 6 b VATL). The main difference is that the original invoice sustaining the initial expense is issued in the name of the final recipient (fig. 4):

In the example above, A merely pays the expense as it is not a recipient thereto. The hotel accommodation service is rendered to B and the invoice is issued in its name.

A should book this expense in a suspended account (transitory item) and recharge the full amount, including the VAT, to B. The invoice issued by A for the disbursement is not subject to VAT thus it should not and not include VAT autonomously. A is naturally incapable of deducting the VAT charged by the hotel.

B is then entitled to deduct said VAT as the invoice is addressed to it.

5 Conclusion
Recharges can reach considerable amounts in a company, especially in holding structures, where often a service is centrally procured and then charged on to the entities actually using it. As seen above, businesses have some room for maneuver when dealing with these transactions. Bearing in mind that the VAT treatment is dependent on the way the expenses are recharged – i.e., jointly or autonomously – the VAT situation can be influenced and e.g., the place of supply may change. This may help to achieve the most practical result and avoid unnecessary obligations such as VAT registrations. In any case, the correct handling of recharges avoids unpleasant surprises in the event of a VAT audit.
The German regulations regarding the proof of (VAT exempt) intra-Community supplies set in force in January 2012 have caused much irritation and insecurity within companies involved in cross-border transactions in Germany.

In particular, the newly introduced requirement of a so called “Gelangensbestätigung” gave reason to much discussion. It should be noted that the respective regulations refer to documentation requirements for so called (VAT exempt) intra-Community supplies only, i.e. supplies of goods between two (or more) entrepreneurs within the EU, whereas the goods are dispatched from one Member State (in cases relevant for the “Gelangensbestätigung”: dispatch from Germany) and destined for another Member State. Accordingly, the «Gelangensbestätigung» is not relevant for the VAT exemption of export supplies (goods dispatched from Germany and destined for a non-EU country, e.g. Switzerland).

In a first reaction to the negative public response to the new regulations, the German tax authorities agreed that the taxpayers are not required to implement the changes to the proof of intra-Community supplies until a new regulation in this regard is in place (Ministerial Decree dated 1 June 2012).

The Federal Ministry of Finance (BMF) has recently presented its long-awaited new draft amendment bill regarding the “Gelangensbestätigung”. The draft has been circulated for further discussion within the various lobby groups. Once the interest groups have provided their input, the BMF will decide whether further amendments to the bill are required. Otherwise, the German government may consider initiating the legislative procedure in order to set the bill in force.

The current draft foresees for the implementation of the new bill as of 1 July 2013. The new draft bill considers the criticism and provides substantial relief in some areas. The following key elements of the draft should be mentioned in particular (more details are laid down in the draft bill):

- The “Gelangensbestätigung” remains as one, but not the sole evidence of the cross border movement of the goods.

- Alternative proofs are equally possible. In particular, the freight forwarder certificate is clearly mentioned. The confirmation issued by the freight forwarder must however - at least when the freight forwarder is instructed by the supplier - relate to the secluded, not only to the intended shipment. If a forwarder is instructed by the customer, it should be sufficient to confirm the planned shipment (including relevant details of the supply) if parallel proof of payment of the goods can be substantiated.

- The requirements regarding the proof of the intra-Community movement of the goods shall also be fulfilled if provided by several documents rather than only one single document.

- The freight forwarder certificate as alternative proof can now also be submitted electronically.

- In case of “tracking and tracing” the electronic order and the shipment process protocol shall suffice as proof of transport.

- Summary confirmations may be issued (summarizing up to one quarter).

- Where the “Gelangensbestätigung” is used, there are specific provisions with regard to the electronic transfer of such proof (e.g. for the supplier claiming the VAT exemption, it must be “recognizable” that the document originates from the recipient or a person authorized by the recipient). A signature on an electronically submitted “Gelangensbestätigung” by the recipient or a person authorized by the recipient is not required.

- The stating of the month (rather than the exact day) of arrival in the country of destination will suffice.

- In case of chain transactions either the intermediate customer or the end customer (final recipient of the shipment) may confirm the arrival of the goods in the country of destination.

- The requirements in pickup cases are strengthened considerably. In pickup cases, the evidence may no longer be provided by a “Verbringensversicherung” issued by the recipient at the time of pickup (a document stating the intention of the recipient that the goods will be moved cross border). Rather, the cross border movement of the good must be proven by way of the (now “simplified”) “Gelangensbestätigung” (or other documents respectively confirming the arrival of the goods in the country of destination).
VAT invoicing in the European Community

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Council Directive 2010/45/EU was adopted on 13 July 2010 and its provisions shall be applied by Member States as from 1 January 2013. It aims to promote and further simplify invoicing rules by removing existing burdens and barriers. It establishes equal treatment between paper and electronic invoices (the same process for paper invoices can be applied for e-invoices) without increasing the administrative burden on paper invoices and has the aim to promote the uptake of e-invoicing by creating the freedom of choice in ensuring the authenticity of origin, integrity of content and legibility.

The Directive recognizes the obligation for invoices to accurately reflect actual supplies of goods and services and therefore requires that the authenticity of the origin, the integrity of the content and the legibility of invoices are insured from their issue until the end of the period of storage. This can be achieved through business controls that provide a reliable audit trail between the invoice and the supply, and that assure the identity of the supplier or issuer of the invoice (authenticity of origin), that the VAT details (the invoice content required by the VAT Directive) on the invoice are unchanged (integrity of content) and that the invoice is legible.

The use of business controls creating a reliable audit trail between the invoice and the supply can be used to ensure the authenticity of origin, integrity of content and legibility for all invoices, whether paper or electronic. Other than business controls, advanced electronic signatures based on a qualified certificate and created by a secure signature creation device or electronic data interchange (EDI) are examples of how the authenticity of the origin and integrity of the content of electronic invoices can be ensured through specific technologies. They provide a guarantee for businesses to ensure that the authenticity of the origin and the integrity of the content are met, and as such provide legal certainty. However, they are only examples and other technologies or procedures may be used.

Business controls that provide a reliable audit trail between the invoice and the supply have always been important, but with the implementation of the Council Directive 2010/45/EU their relevance will even increase. Therefore, it is highly recommended that businesses review their applied business controls with respect to the audit trail, amend them if necessary and document those business controls. In addition it is recommended to review the ERP (e.g. SAP) set up ensuring compliance with the new invoicing rules.

ECJ decision on the formal requirements to 0% rate an intra-Community supply of goods

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It is common practice among EU Member States to require that a supplier who performs an intra-Community supply of goods (ICS) discloses the customer’s VAT number on the invoice in order to be allowed to zero rate the transaction. In its judgment of 27 September 2012, the ECJ softens this position by stating that “th[e] exemption should not be refused on the sole ground that the requirement [of disclosing the VAT identification number of the customer] was not fulfilled where the supplier, acting in good faith and having taken all the measures which can reasonably be required of him, is unable to provide that identification number but provides other information which is such as to demonstrate sufficiently that the person acquiring the goods is a taxable person acting as such in the transaction at issue”.

In the case at end, the customer was a non EU company, not registered in the European Union so unable to provide a VAT number. Therefore, this ECJ decision allows companies performing ICS to apply the VAT exemption even though they do not disclose a VAT number of the customer. However, they should carefully monitor how this decision will be impact the practice of Member States, especially as to what “sufficient proof” means.
Canton of Basel-Stadt

No further reduction of the maximum corporate income tax rate in the Canton of Basel-Stadt

As before in 2010 and 2011, a further partial cut – of 0.5% down to 20.5% – was made in the maximum corporate income tax rate for 2012 in the Canton of Basel-Stadt.

The maximum corporate income tax rate will be cut for the last time – by 0.5% – with effect from 1 January 2013, and will be 20% from that date onwards.

The Basel-Stadt Cantonal Council had planned to progressively reduce the maximum corporate income tax rate from 2013 onwards, taking it down to 18% by 2017, but this was rejected by the voters.

Lump-sum taxation to be abolished

Lump-sum taxation will be abolished in the Canton of Basel-Stadt with effect from 2014. More specifically, the option of being taxed on the basis of living expenses after the year of arrival in the canton is being removed without being replaced. The option of lump-sum taxation in the year of arrival will continue to be available.

Canton of Basel-Landschaft

No more tax-deductible building finance from 2013 onwards

From 2013 onwards, saving to finance building will - following a vote at the national level - no longer be tax-deductible in the Canton of Basel-Landschaft. In view of the requirement of saving for a minimum of five years to get the canton’s building finance premium, the use of the saved capital for its intended purpose of building will be subject to the following transitional rule for a period of five years (i.e. until 2017):

- there will be no change to rules applicable to the use of capital accumulated for building purposes on the basis of a building finance agreement concluded before 1 January 2006. The capital must be used for new residential property occupied by the owner within 12 years of the agreement being concluded.
- Capital accumulated for building purposes between 2006 and 2012 inclusive under a building finance agreement concluded after 1 January 2006 must be used for new, owner-occupied residential property by the end of 2017.
- From 2013 onwards, interest on capital already saved will be subject to income tax, and capital saved for building purposes to wealth tax.

Lump-sum taxation to be abolished

Basel-Landschaft's electorate has approved the “End tax privileges” legislative initiative. This means that, from the new year (2013) onwards, lump-sum taxation will no longer be available in the canton, although lump-sum taxation in the year of arrival will continue to be available.

Canton of St. Gallen

Lump-sum taxation retained

On 27 November 2011, the Canton of St. Gallen held a vote on abolishing lump-sum taxation. The St. Gallen voters rejected the tax fairness initiative in favor of the counterproposal by the government and Parliament. Under the counterproposal, which takes effect on 1 January 2012, taxable income must be at least seven times the annual rent or rental value, but no lower than CHF 600,000. Taxable assets must equate to twenty times taxable income, i.e. a minimum of CHF 12 million.

Partial amendment of tax legislation in 2013

On 1 January 2013, several changes adopted as part of a partial amendment to the tax law will take effect in the Canton of St. Gallen, provided the decision is not reversed in a referendum. As well as a general “tidying up” of the tax law, several amendments to the legislation to bring it into line with federal law have been adopted and the latest Federal Supreme Court decisions taken into account. These decisions relate to technical improvements in international tax allocation and legal clarifications in the half-rate procedure for dividend taxation and replacement procurement under real estate gains taxation legislation. Inter-cantonal income from real estate is now subject to income and corporate income tax (instead of real estate gains tax).

Canton of Appenzell Innerrhoden

No changes.

Canton of Appenzell Ausserrhoden

Lump-sum taxation abolished

On 11 March 2012, the voters of the Canton of Appenzell Ausserrhoden approved the abolition of lump-sum taxation. The amendments to cantonal tax legislation take effect on 1 January 2013.

Partial amendment of tax legislation

On 29 October 2012 the cantonal parliament approved the partial amendment of tax legislation. The referendum deadline ends on 3 January 2013. Besides compulsory changes to bring the legislation into line with federal law (taxation of employee stock options, tax deductions for childcare), compensation for the effects of “cold progression” from a change in the Swiss consumer price index of 3% is planned. The provisions on voluntary contributions will be amended (new: donation discount of 20% for legal entities and individuals).

Canton of Thurgau

Partial amendment of tax legislation in 2013

On 9 May 2012, the Great Council of the Canton of Thurgau approved the partial amendment of its cantonal tax laws. The amendment comprises the following key points: implementation of the Federal Employee Stock Options Act, introduction of annual compensation for the effects of cold progression, creating the legal
principles for a digital archive (“full tax”) and changes to inheritance and gift taxes in an international context and in relation to step and foster children. The amendments will take effect on 1 January 2013 by resolution of the Cantonal Council.

Consultation on amendments to cantonal and municipal taxes legislation

The Thurgau Cantonal Council is considering switching from a monistic to a dualistic system in respect of real estate gains taxation (only for real estate owned by individuals as business property). The dualistic system is already in use for legal entities. Lottery winnings below CHF 1,000 will also be exempt from the tax. The consultation period ends on 6 December 2012.

Value-added duty on redesignation of land as building land

On 17 June 2012 the Thurgau voters approved a new planning and building law. The key change in the law is the introduction of an added value duty. Where land is designated as building land for the first time, a tax equivalent to 20% of the land added value is levied and used as compensation, when land is redesignated as rural land, to pay for the demolition or renovation of old buildings, or to clear and decontaminate the site. The law is expected to take effect at the start of 2013.

Canton of Zurich

Losses can be offset even after holding privilege removed

The previous practice in the Canton of Zurich was that losses incurred by companies qualifying for holding status could not be offset against earnings generated after the transition to ordinary taxation. The Federal Supreme Court’s ruling of 13 March 2012, 2C 645/2011, upheld an appeal against the stance of the Zurich Cantonal Tax Authority which confirmed the practice through a literal interpretation of Article 25 (2) of the Tax Harmonization Act. The Federal Supreme Court based its ruling on the equal treatment of profits and losses. As hidden reserves that had previously arisen under a company’s holding status could be taxed if capital gains were realized on participations, it also seemed reasonable to offset corresponding losses against taxable gains, even after the privilege had been removed. The Canton of Zurich has amended its practice accordingly, such that hidden reserves can now be realized on a fully tax-neutral basis upon transition to ordinary taxation. However, losses that arose prior to the removal of the privilege still cannot be offset.

Anti-discrimination rules not restricted to loss apportionment

The Federal Supreme Court’s ruling of 25 July 2012, 2C_482/2011, stated that anti-discrimination rules were not restricted to loss apportionment in relation to intercantonal income from real estate. This was therefore contrary to the Zurich Cantonal Tax Authority’s standard practice. For example, a company based in Zurich reported participation relief of more than 100%. Because of intercantonal anti-discrimination rules, the canton in which the real estate is located could not tax the income from the real estate if a company based in the canton in the same situation could declare a net gain of zero.

Canton of Grisons

On 31 August 2012, the Great Council of the Canton of Grisons approved the partial amendment of its cantonal tax laws. Besides making a number of changes to bring the legislation into line with federal law, the legislative amendments also take account of the latest Federal Supreme Court decisions. Lump-sum taxation will be retained and adjusted to bring this in line with the proposed Federal Lump-Sum Taxation Act. This gives the government leeway to define the minimum basis of assessment. Other changes relate to real estate taxation. Real estate taxes will be treated as maintenance costs and made tax deductible in future. There are also plans to create a legal framework for the introduction of electronic data traffic between the taxpayer and tax authorities. The Great Council will also have more discretion over the (corporate) tax multiplier in future. Under the current law, the difference between income and corporate income taxes may not exceed 10 percentage points. This limit will be raised to improve flexibility and competitiveness in terms of tax competition. Most amendments will take effect on 1 January 2013 (subject to a referendum).

No reduction in corporate taxes

Zurich’s Cantonal Council and Parliament submitted a proposal to the voting public on capital tax breaks as part of implementing the Corporate Tax Reform II. This proposal, which would allow corporate income tax to be offset against capital tax, was narrowly rejected by voters on 17 June with 50.16% of votes.

Amendment of Cantonal Council Ordinance due to incompatibility with the Tax Harmonization Act

On 3 November 2010, the Cantonal Council of Zurich adopted an Ordinance as a transitional solution due to the delayed enactment of the cantonal law implementing the government’s Corporate Tax Reform II at the beginning of 2011. In a decision of 29 July 2012, 2C_809/2011, the Federal Supreme Court found that this Ordinance be contrary to federal law. At the beginning of October, the Cantonal Council finally redrafted the problematical sections on the separate taxation of liquidation gains on cessation of self-employment, so that notional pension fund buy-ins would be separated from hidden reserves and both elements taxed separately.

Repurchase value of life annuity to be declared an asset

The Federal Supreme Court’s ruling of 1 May 2012, 2C_337/2011, stated that contrary to the Zurich Cantonal Tax Authority’s standard practice, the repurchase value of a life annuity should also be declared an asset during its duration. Any statutory provisions stating otherwise have no effect.

Compensation for “cold progression”

The inflation levels accrued since 2002 were compensated for during the 2012 tax period. The Cantonal Council has adopted an Ordinance within the scope of its powers that adjusts rates and deductions.

Outlook

The Cantonal Council rejects the “Against tax breaks for the super-rich” popular initiative

The Cantonal Council has rejected the “Against tax breaks for the super-rich” popular initiative. The initiative demands a 40% – 50% increase in tax rates on assets of more than CHF 2.1 million. The Cantonal Council based its decision on the disadvantageous position of the Canton
Canton of Aargau

New tax law approved by the voting public

Voters have approved the Canton of Aargau’s amendment of its tax law. The argument in favor of a competitive and attractive canton in which to live and work for the years ahead won the popular vote. The amendment will be implemented in four stages focusing on the following measures: firstly, wealth and income tax rates will be reduced, secondly, child and childcare cost allowances will be increased for families, thirdly, lump-sum payments will be taxed less with “cold progression” compensated for annually, and fourthly, companies will see a decrease in their tax rates.

Developments at cantonal level in Central Switzerland

International and national tax competition has become markedly fiercer in recent years. In response, the cantons in Central Switzerland have amended several laws to retain their attractiveness for companies. Changes affecting individuals, particularly amendments to bring the legislation into line with federal rules, have been implemented.

This article examines the changes in each of the cantons.

Canton of Lucerne

The corporate income tax cut approved last year took effect on 1 January 2012. The Canton of Lucerne now boasts the lowest corporate income tax rate among the cantons in respect of ordinary taxation. Depending on the municipality it is 4.3-6.5%. For individuals, several changes have been made based on federal rules, including a flattening of the progressive tax system for higher incomes. The lump-sum taxation system has also been amended, with stricter provisions likely to come into effect from 2013.
Canton of Nidwalden

Several changes were already made in the Canton of Nidwalden with the amendments to the tax legislation of 1 January 2011. These included the cut in corporate income tax for legal entities to 6% and in capital tax to 0.1‰ referred to in the last article. No major changes are envisaged over the next few years. The main changes made to bring the system in line with federal rules affect individuals, for example the taxation of employee stock options, a tax exemption for firefighters’ salaries, childcare costs and deductions for political party donations.

Canton of Obwalden

The Canton of Obwalden has not made any significant changes to the taxation of legal entities. Individuals in the lower and medium income brackets have been granted tax relief through a special deduction and the child deduction has been increased. The legislation has also been brought into line with federal rules.

Canton of Schwyz

Since the last set of amendments, which took effect in 2011/2012, the Canton of Schwyz has not made any significant changes. Only formal amendments in respect of inventories (responsibility for tax inventory entries) and amendments to bring the legislation in line with federal rules are expected next year. The next round of legislative amendments is not due until 2015.

Canton of Uri

No major changes took place in the Canton of Uri this year. The necessary amendments bringing the legislation in line with federal rules have been made at ordinance level.

Canton of Zug

Corporate income tax on earnings over CHF 100,000 was lowered from 6.5% to 6.25% (the first step in the phased reduction to 5.75% from 2014) on 1 January 2012, following the vote on 25 August 2011. The Canton of Zug is therefore expected to remain in 10th place among the cantons. SMEs will benefit from a reduction in the corporate income tax rate on the first CHF 100,000 to 3%.

The cut has also reduced the difference in the tax burden between ordinary taxation and domicile and mixed companies, which could lead in the medium term to an easing in the tax dispute with the EUR and greater legal certainty.

A number of federal provisions affecting individuals were also implemented in the Canton of Zug. These relate in particular to the deductibility of contributions to political parties and relief for families.

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