Swiss National Council rejects changes to the capital contribution principle

Executive summary

The Swiss National Council (first chamber of Swiss Parliament) has rejected a parliamentary initiative addressing the alleged loss of tax receipts due to the enactment of the capital contribution principle.

The rejection by the Swiss National Council is final and, therefore, this initiative has failed definitely. This means that the current regulations relating to the capital contribution principle remain unchanged and Swiss companies can continue to benefit from unrestricted tax-free repayment of capital contribution reserves. Unlike regulations in other jurisdictions, this particularly includes an unrestricted entitlement to choose whether a distribution is made out of capital contribution reserves or retained earnings.

This is a positive and important decision in light of legal certainty and withholding tax planning possibilities. Following this recent decision, no further parliamentary initiatives or motions/requests concerning this matter are anticipated in the near future.

The capital contribution principle

Through the end of 2010, any distribution by a Swiss company to its shareholders was subject to withholding tax and income tax at the level of the individual shareholder receiving such dividend income. Only repayments of paid-in nominal share capital were exempt from these taxes. In other words, all repayments of previous capital contributions in the form of share premium were in principle subject to Swiss withholding tax and income tax for individual shareholders.
With the introduction of the capital contribution principle as of 1 January 2011, repayments from so-called “capital contribution reserves” are also exempt from Swiss withholding and income taxes. In principle, the term “capital contribution reserves” covers contributions made by the direct shareholders since 1 January 1997 which were accounted for in a separate account and have been reported to the Swiss Federal Tax Administration.

This change was particularly important for (1) all foreign shareholders of Swiss legal entities, including foreign multinationals and individuals, and (2) Swiss resident individuals, who kept their shares as a private asset. Whereas the first group does benefit from a withholding tax exemption, the second group is, in addition, exempt from Swiss income tax on repayments out of capital contribution reserves.

Parliamentary discussions
The introduction of the capital contribution principle was part of the Corporate Tax Reform II. In 2008, Swiss citizens voted for the enactment of the Corporate Tax Reform II. Following enactment, it was debated whether the Swiss citizens were misled by the communication by the Federal Council regarding the “loss of tax revenue” caused by the introduction of the capital contribution principle. This gave rise to political discussions regarding potential amendments to the capital contribution regulations.

Several parliamentary motions/requests aimed at confining the use of capital contribution reserves to specific situations were then filed. This included proposed provisions stating that companies are only entitled to the distribution of capital contribution reserves once they have distributed all their retained earnings available for distribution, often referred to as the “priority rule.” However, none of these motions/requests were further pursued.

The latest parliamentary initiative itself was mainly aimed at inquiring about the facts and circumstances that led to the statements made regarding the loss of tax revenue. Nevertheless, this initiative could have resulted at the very end in restrictions for the tax-free repayment of capital contribution reserves.

Final decision by the Swiss National Council
On 19 March 2013, the Swiss National Council rejected this latest parliamentary initiative. As both chambers of Swiss parliament need to approve a parliamentary initiative for it to be binding, this decision can be considered final. It is considered unlikely that similar parliamentary initiatives or motions/requests will be filed in the near future.

Endnotes
1. 50.5% voted for the enactment and 49.5% voted against it.
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