Dear Reader

Once again in this issue of the Newsletter, we present an overview of the latest developments on the subject of Corporate Tax Reform III, with a briefing on the survey of the cantons’ views about the draft reform proposals. The generally positive result shows that the cantons largely support the proposed objectives. A broad majority favor the license box, but the cantons take a critical stance on the introduction of interest-adjusted corporate income tax. Even though tax policy is currently focused on implementing the Corporate Tax Reform, we should not lose sight of Switzerland’s traditional advantages as a business location. Advantages such as legal safeguards and a positive tax environment should not be underestimated and – especially in turbulent times such as these – they should be protected and cultivated.

We also look at real estate transactions in the context of succession planning. Many Swiss companies coming up to a generational change have operating or investment companies at their disposal. It is essential to identify the tax pitfalls involved in these real estate transactions in good time so that tax arrangements for succession planning can be optimized at the same time as economic and civil law aspects.

Our Newsletter goes on to review the latest ruling by the Federal Supreme Court on the assessment note following VAT inspections: The current Value Added Tax Act states that inspections by the Swiss Federal Tax Administration are concluded by means of the assessment note that take the form of orders. In its decision of 21 March 2014, the Federal Supreme Court has ruled against the systematic issuance of assessment note in the form of orders. This gives taxpayers greater flexibility and new procedural leeway which should be exploited.

Save the date: The Free Trade Agreement between Switzerland and China, its third most important trading partner, comes into force on 1 July 2014. It opens up substantial scope for savings on customs duties. To benefit fully from the advantages of this agreement, you should review its provisions and impact in depth so that you can take prompt action.

Finally, we brief you on the revision of the Expatriates Ordinance, which mainly impacts deductions for special business expenses, and on the regulations for using Swiss company cars in the EU. The temporary use of company cars in the EU’s customs territory still triggers procedures and sanctions on the part of the EU customs authorities. We point out some specific issues in this regard and show how our VAT and customs specialists may be able to assist you.

I hope you enjoy reading this issue, have a pleasant summer and relaxing vacation.
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Corporate tax reform III: report on the outcome of consultations with the cantons

Markus Frank Huber, Partner, International Tax Services, EY Geneva, markus-frank.huber@ch.ey.com
Philipp Roth, Knowledge Manager, Tax Services, EY Zurich and Academic Assistant at the University of Zurich, philipp.roth@ch.ey.com

The Federal Council has asked the Swiss Federal Department of Finance to consult the cantons regarding the measures set out in the final report on Corporate Tax Reform III. The cantons are largely in agreement. The report on the outcome of the consultations does not contain any major surprises, but it does prompt further consideration of the key factors that determine Switzerland’s attractiveness as a business location.

Background
The work on Corporate Tax Reform is mainly influenced by developments at the EU and OECD levels, especially as regards Base Erosion and Profit Shifting (BEPS). The OECD requested the Forum on Harmful Tax Practices to review the tax regimes of all the OECD member states. The EU had already voiced criticism at certain regimes under Swiss tax law back in 2005. In December 2013, the OECD Forum on Harmful Tax Practices classified the cantonal tax regimes for holding companies, management companies and mixed companies as potentially harmful, together with the practice of international profit allocation for principal companies; however, this has yet to be confirmed by the OECD Committee on Fiscal Affairs. The review of countries, which is due to be completed by September 2014, should shed some light on the position the OECD will adopt as regards the existing tax regimes in its member states. In this context, particular interest focuses on the existing solutions for preferential taxation of licensing income (known as “license boxes”). An investigation of this taxation model - and more specifically, the British patent box - by the Economic and Financial Affairs Council (ECOFIN) is also currently under way within the EU, with the aim of determining its compatibility with the Code of Conduct for business taxation.

In view of international developments, there is less and less scope for devising attractive approaches to taxation that are also internationally accepted. Given this overall situation, it may also be appropriate to reconsider certain principles of the Swiss tax system. Considering the limited leeway for action allowed by international standards, it is necessary not only for all the institutions involved in the reform process to work together constructively and to focus on solutions (e.g. through working groups, conferences and consultations) but also to maintain and foster the “soft” business location advantages; these include (but are not limited to) factors such as legal security (ruling practice) and a positive tax environment (service-oriented tax administration).

Final report by the Steering Committee
The Steering Committee’s final report published on 19 December 2013 regarding measures to enhance fiscal competitiveness provides the basis for consultation with the cantons.

The final report envisions a fiscal policy thrust comprising the following three elements, in order to cushion the impact of discontinuing individual tax regimes that currently exist:

- Introducing new taxation models that correspond to the international regulatory changes regarding mobile income (license box and interest-adjusted corporate tax with a restriction on the deduction of notional interest on equity capital in excess of a defined minimum).
- Reduction of the cantonal corporate tax rates.
- Strengthening the attractiveness of the business location via additional fiscal policy measures.

As regards financial policy, the final report proposes adaptations to the inter-cantonal equalization of resources together with vertical compensatory measures for the cantons at the federal level. The inter-cantonal equalization of resources is intended to reduce differences between financially strong cantons and their weaker counterparts. The vertical compensatory measures should ensure that the cantons have sufficient leeway on financial policy to implement the corporate tax reform; in this respect, the final report envisions various measures to counter-finance the anticipated additional burden at the federal level.

Outcome of the consultations
A questionnaire about the proposed tax and finance policy measures was sent out to the cantons and other participating institutions. Most of the cantons commented on the questions.

The main results of the consultation are as follows:

- The cantons agree that certain cantonal tax regimes, such as holding companies, domicile companies and mixed companies, can no longer be reconciled with international standards. Several

Cantons and other institutions taking part in the consultations
All the cantons except Lucerne submitted comments.

The following institutions also commented:

- Conference of Cantonal Finance Directors (FDK)
- Conference of Cantonal Governments (KdK)
- Swiss Business Federation (economiesuisse)
- Union of Swiss Cities (SSV)
- Fédération des Entreprises Romandes (FER, Business Federation of French-speaking Switzerland)
- City of Geneva
The cantons consider that discontinuation of “ring fencing” (privileged treatment of foreign income) would suffice to ensure the international acceptance of existing tax regimes. This should be examined in advance.

- The abolition of the cantonal tax regimes would trigger a change of status from “preferential” to “ordinary” taxation. It is to be welcomed that most cantons envision the tax-neutral disclosure of untaxed hidden reserves in this case (“step-up”). Accordingly, the tax basis of the assets could be stepped up on a tax-neutral basis in the event of a switch to ordinary taxation.

- Most cantons welcome the introduction of a license box and they are of the opinion that it should be stipulated in the Tax Harmonization Act as a mandatory requirement. Half of the cantons also appear to prefer a narrowly-defined license box while only five cantons back a broad definition of the reported intangible assets. Some of the cantons and various stakeholders also want to review the introduction of a license box at the federal level.

- However, most cantons appear to reject the introduction of interest-adjusted corporate tax (notional interest deduction).

- Most cantons do not accord priority status to the other fiscal policy measures to make the business location more attractive (e.g. abolition of one-time capital duty on equity capital, step-up on relocation to Switzerland, changes in connection with the participation deduction and adjustments of withholding tax and capital tax). The cantons of Zurich and Basel-Stadt view the issue of step-up (i.e. tax-neutral disclosure of hidden reserves on relocation to Switzerland) as a priority. Zurich also has adjustments of capital tax as one of its priorities.

- As expected, all the cantons back vertical compensatory measures, and all of them also find that the inter-cantonal equalization of resources must be adjusted to the new conditions.

- As regards financial policy, the cantons tend to reject the idea of financing the corporate tax reform by imposing an additional burden on individuals. The counter-financing measures should primarily be targeted at legal entities and their shareholders. This essential message is also echoed by 14 cantons that advocate consideration of the introduction of a tax on capital gains on privately held securities, whereas an increase in value added tax is strongly rejected.

In summary, it may be said that the outcome of the consultations is largely positive and that the cantons back the proposed overall approach.

The introduction of a license box appears to meet with widespread support. The specific form that it would take still depends on the positions adopted by the OECD as well as ECOFIN, but the cantons generally seem to prefer a somewhat narrow option. The cantons’ critical attitude to interest-adjusted income tax should be examined in depth. The notional interest deduction on equity capital is already implemented in various countries; it can be justified in the context of the tax system, it complies with the postulation for an increased equity base and it enhances international competitiveness in group financing. Moreover, this measure represents an attractive alternative to the fiscal practice of Swiss finance branches for tax purposes, which has also attracted criticism.

**Outlook**

By September 2014, the Swiss Federal Department of Finance will elaborate a consultation draft that will take international developments into account and will be based on the Steering Committee’s final report, the outcome of consultations with the cantons, and other comments.

Because of the imminent and far-reaching reforms to the Swiss tax system, the companies involved are currently on thin ice with their planning for the future. It is critically important for them that the upcoming reform should not only create legal security in the future, but also that legal security should be upheld as far as possible during the ongoing reform process. All the institutions involved should feel committed to this proposition. As well as a constructive and transparent process leading to a fair legal solution, this also calls for a cautious and reliable approach to existing tax rulings. Legal security and a positive tax environment are trump cards for countries trying to make their tax regimes more competitive and attractive than elsewhere, and they should not be surrendered unnecessarily.
Almost one quarter of Switzerland’s enterprises will face a change of generation in the coming years. Many of these companies have operational or investment properties, so issues concerning real estate transactions often arise in connection with corporate successions. Some tax pitfalls involved in real estate transactions of this sort in Switzerland are detailed below.

Real estate gains tax
As a general rule, gains from the disposal of real estate are taxable. In the case of legal entities (and of natural persons with real estate in their business assets), such gains are subject to corporate or ordinary income tax on the basis of the annual result at Federal level and in most cantons (what is known as the “dualistic system”); in other cantons, however, these gains are subject (in what is known as the “monistic system”) to real estate capital gain tax in the same way as real estate gains earned by natural persons on their private assets. The dualistic cantons are in the majority, but several important cantons (including the two Basel cantons, Berne und Zurich) implement the monistic system.

For tax purposes the sale of the majority of voting rights in a real estate company is treated equivalent to the sale of real estate (this is known as a “transfer of economic ownership”) and is also subject to real estate capital gain tax (in case of sales from private assets and, in monistic cantons, also in case of sales from business assets). In cases where the transfer does not involve a real estate company in the strict sense, but rather a business with real estate (e.g. a hotel), there is generally no transfer of economic ownership.

Although real estate capital gain tax is generally owed by the vendor, it may also impact the purchaser: on the one hand, the tax can be passed on in part to the purchaser, depending on bargaining power. On the other hand, the ownership period is interrupted in case real estate capital gain tax should be triggered. Taxation at the time of purchase followed promptly by resale (or by a restructuring that is not tax-neutral) may therefore result in a substantially increased tax burden. It is therefore equally advisable for the purchaser to clarify the consequences regarding real estate capital gain tax in advance.

Real estate transfer tax
Most cantons levy a real estate transfer tax on real estate transfers for consideration (in some cantons such as Aargau this takes the form of an administrative tax (“Gemengsteuer”) as part of the land registry fees). The cantons of Glarus, Uri, Schaffhausen, Zug and Zurich do not levy a real estate transfer tax but merely a land registry fee (generally limited to a maximum amount that will cover costs). The canton of Schwyz does not levy a real estate transfer tax, nor does it charge a land registry fee.

In all cantons with a real estate transfer tax, the transfer under civil law as well as the transfer of economic ownership are both taxable. In this regard, reference can therefore be made to the previous comments on the real estate gains tax.

Securities transfer tax
If the disposal concerns shares in a real estate company rather than the real estate itself, there may always be potential liability for securities transfer tax. This tax is due if either the vendor and/or the purchaser is deemed to be a securities dealer as defined by the Stamp Duty Act. In addition to banks and similar institutions, this category specifically includes limited companies and cooperatives having participation rights (shares, capital contributions, participation and dividend right certificates etc.) with a book value in excess of CHF 10 million.

If the purchaser itself is not deemed to be a securities dealer, it should be ensured that the share purchase agreement does not make provision for any securities transfer tax (which may be due from the vendor) to be passed on (in part) to the purchaser.

VAT
The sale of a real estate company (share deal) is exempt from value added tax, so no tax problems should arise for the purchaser in this regard. However, if the real estate itself is purchased, the transaction may be treated in three ways for VAT purposes:
Sale without VAT
Sale with VAT (option)
Sale with notification procedure, if both purchaser and vendor are liable for VAT

With the notification procedure, the purchaser adopts the vendor’s assessment basis and degree of use (and, therefore, any attendant tax risks), so this option is likely hardly ever to be applied among independent third parties. Moreover, the purchaser should only ever agree to a purchase with option either if it can claim the input tax in full or if it can pass it on to the vendor as a reduction in the purchase price. Finally, a purchase without VAT usually represents the most favorable option for the purchaser. It does, however, entail the risk that the vendor of real estate that was hitherto used for taxable purposes will attempt to pass on any correction of input tax (due to a change of use) to the purchaser, as part of the purchase price.

Given the various options for structuring, it is advisable to take account of VAT at an early stage of the negotiations, so that any tax consequences can be taken into account accurately when drawing up the contract and calculating the purchase price.

Planning options for business successions
As already explained, the consequences of property tax can be avoided if properties are transferred as part of an operating company rather than in isolation, because there is no change of economic ownership in such cases. If the purchaser does not wish to continue the business itself (which is probably the rule rather than the exception for real estate corporations), there is nevertheless a risk that a cessation or resale of the business operation (without the properties) would be regarded as tax evasion by the tax authorities. We therefore advise that a procedure of this sort should always be reviewed in depth and where appropriate, should be submitted to the competent tax authorities for review in advance.

Another option is the acquisition of a real estate company by quasi-merger: if the purchaser has at least 50% of the voting rights in the real estate company after the transaction and if at least half of the sale price is paid with the purchaser’s participation rights, the transaction generally constitutes a tax-neutral restructuring. Property taxes are eliminated and in addition, the quasi-merger is exempt from securities transfer tax. The tax burden for both parties can therefore be minimized by the vendors’ participating interest in the purchaser. However, a structure of this sort should also be submitted to the competent tax authorities for approval in advance in order to avoid unpleasant surprises.

Summary
As with other transactions, any succession planning procedure requires that tax issues are addressed promptly, alongside the economic and civil law aspects. If the tax risks are identified in good time, they can be taken into account with guarantee clauses, reductions in the purchase price or other measures. This approach also opens up the possibility of optimized tax structuring for the acquisition. If the tax pitfalls are avoided, the future business successors may also be an attractive investment target for real estate companies.

Legal nature of the assessment note: latest decision by the Federal Supreme Court

Claudio Fischer, Senior Manager, Indirect Tax, Zurich: claudio.fischer@ch.ey.com
Urs Kipfer, Consultant, Indirect Tax, Zurich: urs.kipfer@ch.ey.com

According to the current Value Added Tax Act (VATA), VAT inspections carried out by the Swiss Federal Tax Administration (SFTA) are concluded with an assessment note. Until now, the SFTA has issued its assessment notes in the form of legal orders. With its decision 2C_805/2013 dated 21 March 2014 the Federal Supreme Court has ruled against the systematic issuance of assessment notes in the form of legal orders. This gives taxpayers new procedural leeway which should be exploited.

Conclusion of a VAT inspection by issuance of an assessment note
According to the current VATA (in force since 1 January 2010), the SFTA has the right (and the obligation) to carry out inspections of taxpayers in order to establish the tax due.

According to the law, an inspection is concluded with an assessment note issued by the SFTA. The assessment note states the extent of the tax claim for the inspected period, and it may mean an additional tax claim in favor of the SFTA or a tax credit in favor of the taxpayer. The VATA stipulates the SFTA’s authority to issue legal orders with no restrictions as regards content. On this basis, the SFTA has issued its assessment notes in the form of legal orders according to the Federal Act on Administrative Procedure (Administrative Procedure Act, APA).

Legal effect of the assessment note (legal order)
The issuance of an assessment note in the form of a legal order entails certain consequences for the taxpayer as well as for the SFTA.

An assessment note issued as legal order can only be challenged with legal remedy of an objection to the SFTA. The objection period, which cannot be extended, is 30 days. Moreover, restoration of this period – after it has expired – is only possible in exceptional cases.

Considering the procedural right of taxpayers, the SFTA has to adhere to certain formal requirements, i.e. the assessment note must be issued in writing, must include instructions on the right to appeal, and must be adequately substantiated. As the assessment note is issued in the form of a legal order, the SFTA cannot simply revisit it after disclosure in order to amend it either to the advantage or to the detriment of the taxpayer.

In 2011 the SFTA did not appraise an objection raised by a taxpayer. As a result the Federal Administrative Court (as the court of first instance) and the Federal Supreme Court (as the final instance) had to look into the legal nature of assessment notes.
**Decision of the Federal Administrative Court (BVGer A-707/2013)**

The Federal Administrative Court stated in its decision that an assessment note as such must not be embellished as legal order. Referring to the VATA, the decision points out that a tax claim becomes legally binding either by a legal order which has become legally binding, or by written acknowledgement / payment without reservation of an assessment note, or by the prescription to establish the tax. According to the court decision, the systematic interpretation of the Value Added Tax Act indicates that an assessment note and a legal order must be understood as two different pronouncements of the SFTA.

In other words, the court found that the assessment note cannot be equated to a legal order. This view is supported on the basis of the systematic interpretation of the legislation. This also makes it clear that an order is not necessarily required in order to establish the legal effectiveness of a tax claim.

In addition to the systematic consideration of the VATA, the view that an assessment note may not take the form of a legal order is also supported by the Swiss Government's Message on the Simplification of Value Added Tax dated 25 June 2008. According to the Message, taxpayers should be entitled to discuss an assessment note with the SFTA on an informal basis. The taxpayer should only initiate an administrative procedure (on the basis of a legal order) if no agreement is reached.

Finally, the Federal Administrative Court’s decision stated that the SFTA’s assessment notes are not permitted to systematically take the form of legal orders.

**Decision of the Federal Supreme Court (BGer 2C_805/2013)**

As the court of final instance, the Federal Supreme Court upheld the decision of the Federal Administrative Court, which had been appealed by the SFTA. In the grounds for its decision, the Federal Supreme Court also pointed out that an assessment note as such does not constitute a legal order, and that it is not compliant with the structure of the VATA to issue assessment notes systematically as legal orders.

However, assessment notes in the form of legal orders will continue to be allowed in the future if this seems to be appropriate in justified, individual cases (e.g. upon request of the taxpayer).

**Summary**

The Federal Supreme Court’s decision on the legal nature of assessment notes is welcomed. On one hand, this decision is in accordance with the system of the VATA and the legislator’s intention. On the other hand, it entails a certain degree of flexibility and also has economic advantages for taxpayers, because there is no longer an a priori requirement to contest assessment notes with legal remedy of an objection. Basically, taxpayers have time to contest an assessment note or announce their reservation(s) until they acknowledge the assessment (e.g. by payment) or until the SFTA issues a legal order.

It is only at first glance that the decision seems to entail a degree of legal uncertainty for the taxpayer, because the SFTA can potentially revisit an assessment note that has already been issued. However, the recipient of an assessment note has the option of establishing the legal force of the assessment, either by acknowledging it in writing or by paying without reservations. On the other hand, payment of a tax claim before issuance of an assessment note (e.g. after receipt of the inspection report) has no impact on the legal force of the subsequent assessment note.

The impact of the Federal Supreme Court’s decision on SFTA inspections that have already been concluded will need to be clarified in greater detail. According to this decision, assessment notes that have already been issued are not void, but they may be contested. In the future too, this should make it possible for taxpayers to revisit tax periods that have already been audited as long as the tax claim set out in the assessment note has not yet been acknowledged.
The Swiss-Chinese Free Trade Agreement enters into force on July 1, 2014

Dr. Lars Henschel, Executive Director, Indirect Tax Services, Berne, lars.henschel@ch.ey.com
Oliver Hulliger, Senior Consultant, Indirect Tax Services, Zurich, oliver.hulliger@ch.ey.com
Dominique D. Bolliger, Consultant, Indirect Tax Services, Zurich, dominique.bolliger@ch.ey.com

The Free Trade Agreement (FTA) signed last year by Switzerland and the People’s Republic of China enters into force on July 1, 20141. This FTA between Switzerland and its third-largest trade partner will improve market access for goods and services for both sides and will improve legal protection for those trading with the world’s second largest economy. In order to benefit from the reductions in customs duties (some of which are subject to transitional periods), the provisions of the FTA and its effects need to be carefully scrutinized and appropriate actions need to be taken.

Cuts in duties
As the scope of the agreement covers all goods of chapters 1 to 97 of the customs tariff, most Swiss exports of industrial and agricultural products to China will be wholly or partly exempt from customs duties from July 1, 2014 onwards (with transitional periods of 5 or 10 years in some cases and of 12 or 15 years in isolated instances). The Swiss customs duty concessions will be granted without any transitional periods from the date the agreement enters into force. In consequence, Chinese textiles and footwear will also enjoy duty-free access to the Swiss market when the remaining Swiss customs duties on Chinese industrial goods are eliminated under the FTA. With the entry into force of the FTA, China will lose its status as a preferential developing country under the terms of the Generalised System of Preferences for developing countries (GSP). The FTA’s territorial scope covers the entire territory of the People’s Republic of China2 and Switzerland’s customs territory (including the Principality of Liechtenstein).

Preferential origin
The FTA is a bilateral agreement between Switzerland and the People’s Republic of China. Under the terms of the FTA, agreed tariff preferences on the import of goods can only be granted to products which qualify as originating from one of the contracting states and which have undergone the relevant processing steps in one of the contracting states. As already familiar from other agreements, in order to qualify as originating products according to the FTA, the respective goods must either have been “wholly obtained” in the country concerned or must have undergone sufficient working or processing. Goods are deemed to have been sufficiently worked or processed if they comply with the so called “Product Specific Rules”. These Rules, set out in Annex II of the FTA, define the necessary working or processing steps which non-originating primary materials must undergo so that the manufactured product can be given “originating” status. Working or processing in a third country is not permitted. All countries other than Switzerland and the People’s Republic of China are deemed to be third countries. The “direct transport rule” is also applicable. Therefore, in order to retain their originating status, the goods must be transported directly between Switzerland and China or vice-versa, and must remain under customs supervision in countries through which they transit. However, the agreement does allow a consignment to be split up in third countries. Due to the discontinuation of the GSP, third countries will no longer be able to issue replacement certificates of origin. In such cases, a certificate of origin will have to be issued retrospectively.

In order for Swiss exporters to take advantage of preferential customs treatment for goods imported into China, they must either complete the special movement certificate (EUR.1 CN) and have it authenticated, or if they are Approved Exporters, they may include the declaration of origin on the invoice. The Swiss Federal Customs Administration (FCA) grants Approved Exporters the right to enter declarations of origin on their commercial documents, with no limit on value, and they are exempted from signing by hand. The declaration of origin must correspond precisely to the wording in the FTA and must be formulated in English, as a mandatory requirement. A further critical point is that the declaration of origin must include the Approved Exporter’s registration number and a 23-digit “serial number” for the declaration. Preferential imports into Switzerland are possible only if a Chinese certificate of origin in line with Appendix 1 to Annex II of the agreement is submitted to the Swiss Federal Customs Administration. However, it is envisaged that China will create the status of Approved Exporter in the future.

As a special feature of the FTA Switzerland and the People’s Republic of China have agreed in a Memorandum of Understanding that declarations of origin are being exchanged electronically (known as the Data Exchange System). When exporting goods, Approved Exporters are required to upload the relevant commercial documents with their declarations of origin onto the web-based application EA Data Exchange with China (EACN) before the goods clear customs in China. However, this does not apply to EUR.1 CN movement certificates, which can only be submitted as authenticated original documents. The commercial documents must be uploaded in pdf format, and in the initial phase this must be done for each separate export declaration. The Swiss Federal Customs Administration is currently examining whether and how this process could be automatized. Approved Exporters must therefore complete a self-registration in order to register an

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1 The agreement on labor and employment issues already entered into force on June 9, 2014.
2 The agreement does not apply to the Special Administrative Regions of Hong Kong and Macao or to Taiwan.
The link to the application will be activated on July 16, 2014. The FCA has published a manual to assist with self-registration. It should nevertheless be noted that a hard copy of the commercial document with the declaration of origin completed by the Approved Exporter also needs to be submitted to the Chinese customs authorities. During customs clearance of the imported goods, the Chinese customs authorities will compare the electronic file with the hard copy. If an Approved Exporter is unable to complete the self-registration procedure, EUR.1 CN movement certificates may be used as an alternative.

Summary

Depending on the sector and product, the agreement between Switzerland and China offers considerable potential for tariff savings. Although the FTA is a bilateral agreement between Switzerland and the People’s Republic of China, implementing the right supply structures could enable exporters to exploit the advantages and tariff preferences of other agreements as well. However, this requires an analysis of the product portfolio, the primary materials used for manufacture and their (preferential) origin as well as an analysis of the production costs. In order to benefit from the advantages offered by the FTA, analysis of the facts and appropriate measures should be carried out as soon as possible.

Expatriates Ordinance

Andreas Tschannen, Executive Director, Tax Human Capital, Zurich, andreas.tschannen@ch.ey.com
Sabrina Osterwalder, Senior Consultant, Tax Human Capital, Zurich, sabrina.osterwalder@ey.ch.com

Consultation on the revision of the Expatriates Ordinance

At the beginning of April 2014, the Swiss Federal Department of Finance (FDF) announced that tax deductions for employees seconded to Switzerland (i.e. expatriates) had been reviewed and amended by a working group. The planned revision involves a narrower definition of the term “expatriate” and more specific provisions concerning deductions for living costs, the costs of education and flat-rate deductions. The proposed amendments are now the subject of an FDF consultation which will remain open until 10 July 2014.

1 Deductions under scrutiny

In 2012, two members of the National Council put forward motions to abolish the deductions granted to expatriates for special business expenses. The Federal Council, however, decided not to fundamentally challenge existing regulations and asked that the motions be rejected. But it did offer the prospect of a review of the conditions and modalities of individual deductions. This review was conducted by a working group and the findings are now available.

The working group has concluded that the costs of moving, living and private education are tax deductible, finding sufficient legal basis in Article 26 of the Federal Law on Direct Federal Tax (DBG). This has long been a disputed point, especially in the Canton of Zurich. Neither the abolition of any particular deduction nor a new deduction are therefore necessary. It also concludes that expatriates and other individuals who are tax liable in Switzerland are ensured equal treatment.

However, the working group has also highlighted a number of weaknesses in the Ordinance. These findings now form the basis of the FDF’s proposed revision to the Expatriates Ordinance. This will involve restrictions on the scope of the Expatriates Ordinance (e.g. so that it only extends to specialists with particular professional skills) and more specific wording for the provisions on deductions for living costs, education costs and flat-rate deductions.

2 Recent experience in this area

The narrower definition of expatriate was already confirmed in a decision by the Zurich Administrative Court on 2 April 2014. Deductions will no longer be permitted for special business expenses if the seconded employee:

a) arrives in Switzerland from a third country (in the case in question a UK employee was first seconded to the Netherlands before being sent directly to Switzerland, i.e. they did not arrive from their home country);

b) has already been renting out their permanent place of residence in their home country for a number of years;

c) extends the secondment in Switzerland to a total period of more than five years (e.g. secondment to Switzerland for three years followed by an extension of another three years), thus exceeding the five-year limit stipulated in the ordinance.

The Administrative Court argued that in such cases the link with the home country has become so tenuous that the conditions for the special deductions are no longer met. In particular the last point (i.e. exceeding the five-year limit) could have a significant impact since the special deductions will be rejected immediately (and potentially retroactively) as soon as a secondment is extended beyond five years or a person's residence in Switzerland ultimately exceeds this amount of time.

3 Summary

In everyday assessment practice, this means in future that deductions for expatriates’ special business expenses will only be granted to those falling within the “classic” definition. The person concerned must be either an employee in a management position or a specialist, and must be seconded to Switzerland by a foreign company under a temporary secondment agreement for a period of no more than five years. The period of residence in Switzerland must not exceed five years and the employee must arrive in Switzerland directly from their home country rather than via any third country. The employee will also be required to provide evidence of retention of a permanent place of residence in their home country and may not rent that place of residence out to any third party.
Swiss Company Cars in the EU

Barbara Henzen, Partner Indirect Tax, Zurich, barbara.henzen@ch.ey.com
Roger Jaun, Manager Indirect Tax, Berne / Basel, roger.jaun@ch.ey.com

Rules on temporary use by employees living in the EU

Swiss company cars in the EU spotlight

Practice shows that Swiss company cars that are used temporarily in the EU customs territory still regularly trigger procedures and sanctions on the part of the EU customs authorities. Persons employed by Swiss companies but resident in the EU can be hit by measures ranging from fines to seizure of the vehicle or even criminal proceedings if they use a company car for their journey home or for private use in general.

Moreover, only a few Swiss companies are aware that the use of a company car for private purposes by their employees who live in the EU can require registration for VAT purposes in the EU member state.

Background

Anyone who is out and about after work or at the weekend in the areas bordering Switzerland is familiar with the sight of cars with Swiss company logos and number plates parked outside residential buildings. It’s not difficult to work out that Swiss companies clearly employ staff who live in bordering EU member states and who mainly carry out their work in Switzerland as cross-border commuters or weekday residents.

Swiss employers often provide these employees with company cars which are also regularly used for private purposes. Employees resident in the EU cross the border and thus regularly use Swiss company cars within the EU customs territory without paying any duty or taxes on the vehicles in question. Swiss companies often overlook the fact that such a “duty-free transfer” of their company cars into the EU may have legal consequences if the restrictive requirements are not met. The exception rules applicable to temporary duty-free use have previously tended to be interpreted rather loosely by the authorities.

The EU’s requirements with regard to customs duty and taxation

In its judgment of 7 March 2013 (C-182/12), the CJEU clarified that full exemption from import duty on a company car belonging to a “person” domiciled outside the EU customs area and used temporarily for private purposes by an employee resident in the EU is available only if the subordinate nature of the private use is specified in this employee’s employment contract.

The CJEU thereby focuses predominantly on the conditions permitting the private use of company cars in the EU without payment of import duties, namely that (a) the employee in question is an employee in the “traditional” sense of the word and that (b) the subordinate private use must be explicitly provided for in the employee’s employment contract. On the other hand, the CJEU opts not to define in more detail the legal relationships that are to apply to the employment contract conditions within the context of EU legislation.

In contrast, full exemption from import duties for a company car that belongs to a “person” resident outside the EU customs territory and which is temporarily used for business purposes by an employee resident in the EU requires only “other authorization”.

The above criteria are interpreted by the individual EU member states. In addition, the formal requirements of the applicable customs process for temporary use must be observed (e.g. formal or informal process).

If companies located outside the EU customs territory allow their employees who live in bordering member states to use a Swiss company car temporarily enter the EU customs territory these employees have the opportunity to temporarily enter the EU customs territory using a Swiss company car.

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If companies located outside the EU customs territory allow their employees who live in the EU to use a company car for private purposes, this may mean that the company is obliged to register and pay the VAT in the EU member state in question – for Germany in particular (long-term “rental”).

Who is affected by the rule?

From a local point of view, the above rules specifically affect Swiss companies and their employees who live in an EU state if they are out and about after work or at the weekend in the areas bordering Switzerland. Anyone who is out and about after work or at the weekend in the areas bordering Switzerland is familiar with the sight of cars with Swiss company logos and number plates parked outside residential buildings. It’s not difficult to work out that Swiss companies clearly employ staff who live in bordering EU member states and who mainly carry out their work in Switzerland as cross-border commuters or weekday residents.

Swiss employers often provide these employees with company cars which are also regularly used for private purposes. Employees resident in the EU cross the border and thus regularly use Swiss company cars within the EU customs territory without paying any duty or taxes on the vehicles in question. Swiss companies often overlook the fact that such a “duty-free transfer” of their company cars into the EU may have legal consequences if the restrictive requirements are not met. The exception rules applicable to temporary duty-free use have previously tended to be interpreted rather loosely by the authorities.

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The temporary use of company cars for private purposes free of import duty by persons who no longer fall under the traditional definition of “employee” is prohibited by EU law. Depending on how individual member states interpret this, demarcation issues arise for members of the board of directors, the executive board, management and shareholders or partners of a company in particular. The same applies to workers employed on a temporary placement.

The entitlement accorded to “traditional” employees resident in the EU to make temporary subordinate private use of company cars without being required to pay duty will have to be underpinned by an explicit agreement to that effect in their employment contract. In this context, employers and employees should know, for example, whether the journey from the Swiss place of work to the place of residence on a workday or at the weekend is considered to be temporary use for private purposes in the EU member state and therefore whether it requires a provision in the employment contract.

How can Ernst & Young help?

The use of company cars on which no duty has been paid by persons resident in the EU in contravention of the applicable rules can lead to the confiscation of the company car by the EU customs authority in question and its release only on payment of the customs duties and any fines due.

The VAT and customs specialists at Ernst & Young are happy to support you in the review or modification of the employment contracts and additional rules used at your company with consideration of the relevant provisions in the respective EU member states.

We recommend

Ernst & Young recommend that Swiss companies with employees resident in the EU check the following points in particular:
We offer
When it comes to the temporary use of Swiss company cars in the EU customs territory by employees resident there, we are happy to provide efficient support with:

- the assessment and estimation of potential tax-related consequences on the basis of existing employment contracts and company car regulations;
- the creation of the necessary formal and material bases for fulfillment of the requirements of the respective EU member state;
- the clarification of possible registration obligations for VAT purposes and the identification of association of obligations.

If this Indirect Tax Alert has got you interested in the topic of cross-border use of company cars, or if you have further questions, we look forward to being able to help you.

From the perspective of the EU member state in question, do employees resident in the EU temporarily use the company car for company use only within the EU customs area or also for private purposes?

Is the employee driving the car able to produce sufficient authorization for business use in the relevant EU member state?

Is the employee driving the car able to provide evidence of authorization for private use by means of a suitable provision in the employment contract?

Do the internal company regulations for company cars ensure correct temporary use in the EU customs area (for example, no use by family members, partners, etc.)?

Are the regulations relating to customs law known (e.g. form confirmations, etc.)?

Is the company liable to VAT as a result of private use in an EU member state?