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OUTCOME OF PROCEEDINGS

From:	General Secretariat of the Council
To:	Code of Conduct Group
Subject:	Switzerland's Practice of the Federal Tax Administration regarding finance branches (CH005) – Final description and assessment

ROLLBACK REVIEW PROCESS (JANUARY 2019)

Background

Member States signed a Joint Statement with Switzerland in October 2014[1]. In the Statement Switzerland agreed to amend or abolish its tax legislation in relation to 5 preferential regimes, including the Federal Tax Administration regarding finance branches (CH005). In return, Member States agreed to lift their national countermeasures linked to these regimes, once they are abolished.

[1] See doc. 6972/18 ADD 43.

Assessment

This regime has been closed to new entrants as of 1st January 2019[2], which has the same practical effect as abolishing it.

Taxpayers already benefitting from this regime have been allowed to continue benefitting from it until the general corporate tax reform enters into force on 1st January 2020 after the positive outcome of the 19 May 2019 referendum. The regime will then be abolished without further grandfathering.

The COCG meeting of 13 September 2019 therefore approved the rollback of this regime. This conclusion was endorsed by the ECOFIN Council on 10 October 2019.

Annex 1: Assessment of the old CH005 regime in 2017 (standstill review)

[2] https://www.efd.admin.ch/efd/en/home/dokumentation/nsb-news_list.msg-id-72938.html

Annex 1: assessment of the old CH005 regime in 2017 (standstill)

a. Description

The Swiss finance branch is a branch of a foreign based legal entity, usually resident of a state with which CH has agreed a DTC. The foreign based entity is fully equity financed. It usually has limited presence in its country of residence, but enough to ensure its residency abroad. The branch has significant substance in the form of premises and personnel and typically engages in group financing activities. Its income therefore will primarily consist of interests received from group companies. It is not allowed to provide financial services to Swiss based group companies.

At federal level, a special ruling is available reducing the taxable income for federal corporate tax purposes. At cantonal level, the branch will likely be eligible for the mixed company status, provided no more than 20% of the financing activities are domestic.

b. Preferential features

At federal level, 85% to 90% of the financing income will be exempt from tax subject to a ruling establishing a deemed loan between the foreign head-office and the Swiss branch. In other words, at federal level a deduction in the amount of 85% to 90% of the financing income is allowed as a deemed interest expense.

At cantonal level, the branch will likely be eligible for the mixed company status, provided no more than 20% of the financing activities are domestic (80% deduction).

As a result, effective tax rates of 2% to 5% can be achieved.

c. Possible concerns

Since the company is fully equity financed and all the essential functions with respect to the financing activities are conducted in Switzerland, all or the main part of the group financing income should normally be subject to tax in Switzerland and exempt from tax in the state of residence of the foreign legal entity.

This will also typically be the treatment in the foreign country of residence.

By allowing a deemed deduction of interest (which is not recognised in the country of the head office), the financing income is in part effectively taxed nowhere.

In case of an assessment against the Code criteria, the regime would probably fall foul of criteria 1 and 2 (limited to foreign source interest), criterion 4 (profit determination departs from internationally accepted rules) and criterion 5 (negotiable effective tax rates lack transparency).

d. Assessment by the COCG

Switzerland has committed to abolish this regime under the EU-Swiss 2014 Joint Statement.