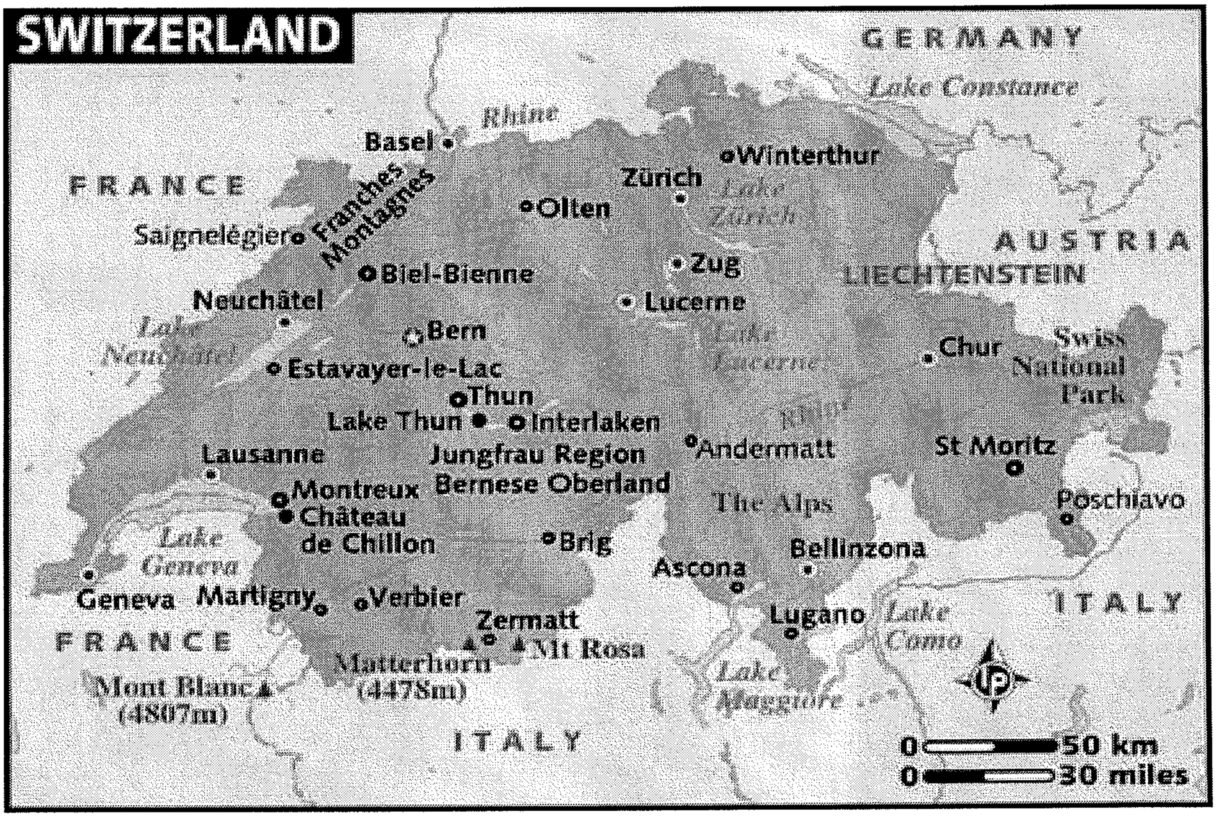
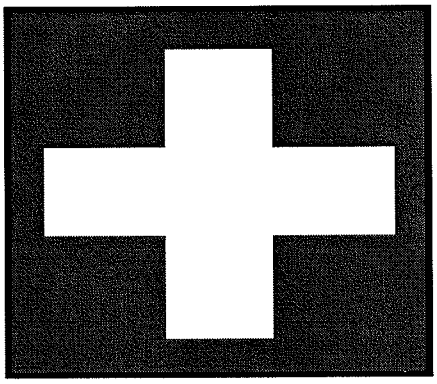


Tax System in Switzerland



Fehlmann & Associés S.A. - October 2011

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Disclaimer

The information contained in this document is not exhaustive. While effort has been made to offer current and accurate information, errors can occur. The information is solely intended to furnish the users with general information and should not be taken as legal advice. It should not be used without prior advice from professionals on the matter.

INTRODUCTION TO THE LOCAL TAX SYSTEM

Switzerland has a federal tax which is identical for all its territories, a cantonal tax, specific to each of the 26 cantons (although a law to harmonize the differences is in progress), plus communal taxes which are added to the cantonal tax with varying rates according to the wealth of the community.

These **direct taxes, levied on three levels**, represent two-thirds of the Government's tax levy, given that **indirect taxes are relatively low**, as for VAT (maximum 8,0%), inheritance and donation tax (none for direct descendance) and other stamp and registration tax. On an international scale, direct tax in Switzerland is relatively moderate with an average income tax for individuals at 24,2%, which **can rise to around 40%** on a single person's income for the more expensive cantons.

Tax reforms have been frequent and numerous the last few years. There were a number of tax relief policies introduced to optimize the Swiss marketplace and the introduction of stricter tax policies to counteract tax evasion operations. Due to pressures from foreign Governments, Switzerland had to agree, in 2010 and 2011, with various countries that in case of tax investigations or introduction of withholding taxes on wealth revenues earned by foreign individuals, assistance will be deployed.

1. Taxation for individuals

Persons whose official **place of residence is based in Switzerland** are t axed without limit on the totality of their income and fortune, except for income relating to real estate or permanent establishments abroad.

For persons residing abroad, taxation is limited to their real estate and permanent establishments in Switzerland and income from any lucrative activities they hold in Switzerland unless a double tax treaty invalids this measure.

Taxpayers complete their **tax returns** before March 30, in most of the cantons (deadlines can be granted up to September 30, the tax is then determined by the tax authorities. The taxpayer unity is the family but separate calculations for the husband and his spouse are possible. Taxation is on a yearly basis and usually paid in installments.

Tax is progressive depending on the importance of income; the latter is rarely broken down into its different sources (salary, revenue from capital, pensions, etc.). All charges and contributions stemming from a professional activity and any charges necessary to the acquisition of income (training costs, bank charges, etc.) are deductible. Compulsory insurance premiums and interest paid are fully deductible, while the deduction of private insurance, medical costs, transport expenses, etc. is limited.

1.1 Salaries

Salaries are part of the taxpayer's taxable income.

Compulsory social charges, such as pension schemes, a minimum staff benefit fund, accident insurance, etc., represent on average 16,8% for the employer and 12,2% for the employee. These percentages can vary according to age, work hazards and, in particular, if the employer proposes enhanced pension funds as for large companies.

For **foreigners working in Switzerland**, a tax is withheld on salaries **in most cantons**. Various deductible standard expenses are specifically allowed depending on their status.

1.2 Capital gains on disposals, dividends and interest

Dividends and interest constitute normal taxable income and, if the debtor is Swiss, the withholding tax of 35% paid directly to the tax authorities, is recuperated by compensation to the beneficiary.

In order to reduce the double economic taxation for both the company and the shareholder, the second taxation of the shareholder benefiting from the dividends is reduced of 40%.

There is no taxation in Switzerland on capital gain obtained from the disposal of transferable securities by and individual, unless the tax authorities consider the individual to be acting in a professional capacity.

Therefore, an entrepreneur who sells his company (limited company, limited liability company) is not taxable on the capital gain he makes.

The taxation on the capital gain made on real estate is degressive the longer the property has been owned.

1.3 Taxation on stock options

A collaborator who receives options at a preferential price is considered to have received **an income from a dependent profitable activity**, which is taxable income.

If the option received is freely transferable, the taxable income corresponds to the difference between the price of the option and the actual value at the time of its distribution. However, the capital gain made on realization is no longer taxable.

If the option is blocked for a number of years or accompanied by conditions, the income is only taxable once the option has been paid up according to its actual value determined at that date, or if not, later when it is realized. In the latter case, the entirety of the capital gain made is taxable.

1.4 Wealth tax

Movable assets, apart from antiques or works of arts for a majority of the cantons, and property situated in Switzerland, net of debts, constitute taxable wealth on a progressive rate.

Lacking objective criteria to judge the market values of assessed property, the tax authorities practice different assessment methods that give values, which are a little inferior to the economic reality of assets (property, unlisted securities, etc.).

To avoid paying wealth tax, it is often the case that rich people arriving in Switzerland first found a trust that is not usually subject to wealth tax or non-withheld income tax. They can also apply to be taxed only on their expenditure if they never have had any lucrative activity in Switzerland.

1.5 Tax breaks

The most important tax break consists in a relatively low tax weighting in Switzerland as mentioned above in comparison to most other countries. Some 21% including obligatory social security on revenue.

The non-assessment of capital gains mentioned above is considered to be a tax break.

Individuals arriving in Switzerland who have no intention of exercising a professional activity (person of private means, stars, etc.) could be taxed on their expenditure, estimated at a minimum of 5 times the yearly cost of their residence.

1.6 Others

Concerning Swiss tax specificities, home owners are taxed on a fictive rental income. However, any interest paid is deductible from the tax assessment.

1.7 Tax scales

- Revenues

Given the three levels of taxation: federal, cantonal and local and the different scales applied according to place of residence and taxpayer status, it exists a multitude of scales in Switzerland. The example below shows a scale for withholding tax in Geneva in 2011, which applied to the income of employees, incorporates all tax and takes into account deductions of social security contributions and family expenditure.

Income	Single	Married, two children
50'000.00	7.32	0.00
75'000.00	12.71	0.00
100'000.00	16.15	7.54
150'000.00	20.92	9.59
200'000.00	24.31	14.92
300'000.00	28.87	21.86
500'000.00	33.40	28.05
1'000'000.00	37.17	33.82

The Geneva revenue tax index is about 10% higher than the average one in Switzerland because few so-called “primitive rich cantons” are offering an index up to 50% lower.

- Wealth tax

Tax rate calculation on net wealth for a Geneva taxpayer (single):

Net wealth	% rate
200’000.00	0.21
400’000.00	0.35
1’000’000.00	0.55
3’000’000.00	0.80
10’000’000.00	0.95

2. Taxation of corporations

Legal entities whose head office is in Switzerland are taxable, as well as permanent establishments of foreign companies.

2.1 Corporate tax

To federal tax on company profits is 8.5% is added a fixed cantonal and local tax, applicable in most of the cantons and which is on average around 24%. This global tax of 32.5% applied to after tax profit corresponds to a rate of 24.5% compared to profit before tax.

There is another taxation on shareholders’ funds, which is local and cantonal but not federal, constituting capital, retained earnings, carried forward profit and even “hidden” capital in some cases of under-capitalization. Such taxation is applied in most cantons only when the income tax is inferior.

The taxable income results from the accounts, except for specific cases where the tax authority refuses some charges reported or if the income is from real estate and permanent establishments in other countries.

Losses can be carried forward for 7 years in compensation of eventual profits.

2.2 Capital gain on share disposals

Capital gains reported constitute a product which is subject to standard taxation except if the shares constitute a substantial interest, characterized by an investment of more than 10% in share capital and durable (held for at least one year) (cf. 2.4. below).

There is also usually an exemption from cantonal tax on the capital gain on share disposals of all types when the company is a pure holding or benefits from the income tax status known as "auxiliary company" (cf 2.4 below). With such fiscal status, the interests received are levied at lower rate.

2.3 VAT and other indirect tax

Any party who runs a company is liable to VAT registration. However, they are not subject to such tax in the event of a company's annual turnover of less than CHF 100'000.00.

Modes of enforcement of VAT. The rates are considerably low as they vary from 2.5% for basic commodities (food, pharmaceutics, newspapers, etc.) to a maximum of 8.0%.

A number of companies are exempt from VAT: for example, those that offer educational of health benefits or companies. The company can then not get back VAT on purchases, except if the VAT registration is made on a voluntary basis.

Companies in the financial, insurance and real estate sector use a hybrid system.

The VAT is nil on the exportation of goods and services (invoiced to a foreign entity to be used abroad).

VAT returns are filed quarterly and assess the net VAT to be paid to the Federal Administration, or an amount to be refunded when refundable VAT is higher than VAT due, as for exporting companies.

Foreign companies can pay VAT through a tax representative.

Other major indirect taxes in Switzerland are constituted by stamp duties applied under the following circumstances:

- An issuing stamp duty of 1% on the constitution or increase in capital and other shareholders' funds of more than CHF 1'000'000.00.

- A transaction stamp duty on the transfer of shares made by a financial intermediary (bank, major holding, etc.). The rate is 0.15% for Swiss shares and 0.3% for foreign shares.

There is also a business tax in Geneva, but not in other cantons, based on turnover, the number of employees and rental expenses, which is relatively low.

2.4 Tax breaks

The most important tax break consists in a relatively low corporation tax, on average around 24%.

Most cantons grant new companies, especially those introduced from abroad which present an economic value (job opportunities, know-how, etc.), temporary and degressive tax relieves (5 to 10 years).

In economically weak areas, exemption of federal tax is also possible, along with other financial incentives offered by the Federal Government.

“Basic” companies also benefit from reduced taxation from the canton regardless of whether it is a holding, an auxiliary company or a service company.

A holding is characterized by the absence of business concern and by the existence of long term financial interest (shares, long term loans, etc.) in affiliated companies. Although application criteria may vary from one canton to another, accompany with recognized holding status is not subject to corporation tax (except for income derived from real estate in Switzerland) but to a reduced tax on equity capital (0.07% in Geneva).

Federal tax is more restrictive in that it only allows a tax exemption on dividends derived from substantial interest (more than 10% of the equity capital or representing an economic value of more than CHF 1’000’000.00), and on capital gain on the disposal of substantial and long term interest (holding of more than 10% over a year).

There is no taxation based on consolidated balance sheet in Switzerland.

The domicile and/or auxiliary company is run from abroad (even though its shareholding is mainly in Helvetian hands) and performs the major part of its activities abroad (usually more than 70% of purchases, sales of foods not transiting via Switzerland, royalties on intellectual ownership exploited abroad, etc.). The cantonal tax is in this case either canceled or considerably reduced (i.e.: 5% in Geneva). In certain circumstances, and when the company does not have its own organization to manage its business in Switzerland, as for companies domiciled by a professional (trust company, lawyer, etc.), the Federal Tax Administration may allow up to 50% deduction on the gross margin achieved under the cover of credible costs, with no supporting document needed. If applicable, the reduced cantonal tax applies to the reduced tax basis, as well as the withholding tax due on the distribution of dividends.

The service company, which provides services to other branches abroad, is obliged to realize a benefit representing at least 5% of its operating overheads, which is generally taxed under the common tax system.

2.5 Miscellaneous

A withholding tax of 35% is withheld on distribution of dividends, or payment of interest by a bank, but not on royalties, rents or fees. This tax is not in full discharge for the beneficiary of this income, but it will be credited on the tax advice.

This withholding tax is also levied when an audit proves that there was a hidden distribution of dividends by estimating the transfer price too favorable to the shareholder. It often represents a charge for the company since it cannot be transferred to the shareholder.

Non-profit-making association and foundation are not taxable. When they develop profitable activities, they benefit from a tax basis and reduced rates.

2.6 Tax scales and rates

The following schedule shows in percentage the global corporation tax (federal, cantonal, communal and parochial if any) applied to the net income (CHF 50'000.00 after tax deduction) and to the capital (entire shareholders' equity of CHF 100'000.00) of a company in various cantons:

Cantons	Global Corporation tax
Geneva	24.3
Neuchâtel	22.9
Bern	18.0
Zoug	12.8
Zurich	21.5
Tessin	21.3

3. Non resident (individuals and corporate entities)

3.1 Local law

Non resident individuals, or companies whose head office is not in Switzerland, are taxed in Switzerland in a limited way based on the following items:

- Profits made by permanent establishments, agencies or branches;
- Profits derived from a business in partnership in Switzerland;
- Profits derived from real estate located in Switzerland;
- For individuals, income derived from a professional activity in Switzerland, including director fees paid by a Swiss company;
- Payment from a pension fund in Switzerland (individuals).

Advance tax of 35% withheld on payment of dividends or interest (cf 2.5) represents a tax expense for whom do not declare its income abroad or cannot be refunded by arguing a treaty to avoid double taxation.

3.2 International tax treaties

Switzerland has concluded sixty treaties to avoid double taxation. Besides attribution rules, these treaties essentially provide for a cut in taxes withheld on dividends, interest and royalties. Non-refundable foreign tax gives a tax credit called “standard deduction”. When no convention can be applied, foreign incomes are taxed in Switzerland after deduction of foreign taxes paid.

The foreigner has to ask for a partial or entire refund of the withholding tax of 35% withheld in Switzerland (no tax withheld on royalties and on interest paid by non-banking companies).

Switzerland prevented a misuse of treaties concluded between Switzerland and a non resident through a Federal order in 1962. Conditions required by this order, as capital holding, minimum capitalization, preferential income, etc. are sometimes recapitulated in conventions concluded by Switzerland.

In accordance with new treaties signed in 2010 and 2011, the Swiss Authorities are disposed to assist more foreign fiscal administrations in case of tax evasion. Regarding the United Kingdom and Germany, a system of withholding tax on revenues and capital gains on portfolios will be implemented. Their applications are not yet well identified.

Property held in trust, (at ones name on behalf of a third party), specifically admitted by an internal tax law, does not allow the enforcement of such conventions.

3.3 Tax breaks

Tax breaks are coming from tax and legal sophistication hard to develop.

The constitution of a branch in Switzerland rather than a subsidiary allows to avoid the payment of the 35% advance tax when profits are transferred abroad.

4. Other taxes

Gift and inheritance tax is levied by cantons and municipalities, but not by the Confederation.

Donors, namely the deceased, domiciled in Switzerland are taxed on their entire assets, except real estate located abroad, whereas non residents are taxable on their real estate located in Switzerland.

Rates may vary depending on family relationship. They do not exist (Fribourg, Valais, Geneva, etc.) or are very low for the spouse and children, and reach up to around 50% when the beneficiary is a third party.

Other taxes are also levied on alcohol, tobacco, gas, etc.