Swiss Taxes Newsletter – October 2021

Swiss Federal Finance Department Comments on the Parameters of the Two-Pillar Solution of the OECD/G20 Inclusive Framework

Concurrently with the OECD's announcement on 8 October 2021 of the agreement reached by 136 countries (Switzerland among them) on the initial key parameters in international corporate taxation published by the OECD's Inclusive Framework in early July 2021 (two-pillar solution), the Swiss Federal Finance Department (FFD) issued a press release. The agreement will reallocate more than USD 125 billion of profits from around 100 of the world's largest and most profitable MNEs (those having annual global turnover above EUR 20 billion and profitability above 10%) to countries worldwide (Pillar I), and it ensures that multinational enterprises (MNEs) will be subject to a minimum 15% corporate income tax rate from 2023 (Pillar II). The FFD's press release reiterates Switzerland's demand that the interests of small, robust economies be taken into account in the implementation, and that legal certainty be established for the companies concerned.

According to the FFD, the new taxing rights for market jurisdictions (Pillar I) are moderate, unilateral digital taxes have to be abolished (Switzerland is not among the countries that have introduced such taxes), and the global minimum tax rate is to be set at 15% (rather than "at least 15%"), whereby the minimum taxation rules are to be introduced in stages. The last-mentioned point is important for Switzerland, given its lengthy legislative processes. It must be noted in that context that the "Undertaxed Payments Rule" is set to become applicable as from 2024. ¨

The FFD points to the fact that several points of importance for Switzerland are still open and will be detailed in the coming months. Switzerland is supportive of rules that foster innovation and prosperity, that are applied uniformly worldwide and that are subject to a dispute settlement mechanism. All this aims to create legal certainty for the companies concerned.

The FFD warns that Switzerland won't be able to introduce the new rules by 2023, as envisaged by the OECD, given the complicated Swiss legislative process. In that context, the Swiss federal structure must be borne in mind. Corporate income taxes are not only imposed at the federal level, but also at the level of the 26 cantons and their municipalities. The introduction of the minimum 15% tax rate poses a particular challenge. Even though a federal law harmonizes federal as well as cantonal/municipal taxes among each other, tax harmonization does not extend to the setting of applicable tax rates. While corporate taxpayers are subject to a flat rate of federal income tax of 8.5%, the cantons are essentially free to set their own tax rates; municipal taxes are generally defined as a multiple of the cantonal tax. Furthermore, under the harmonized rules, all federal, cantonal and municipal taxes are principally deductible from the taxable profit at all three taxation levels. As a result, the effective income tax rates are lower than the nominal rates stated in the tax codes, which apply to net income after taxes. In the tax year 2021, the cantons Bern, Zurich, Aargau, Basel-Land, Solothurn, Valais and Ticino have combined effective corporate income tax rates above 15%; in the remaining 19 cantons, the combined effective rate is currently below the 15% mark. Implementation of Pillar II will require legislative changes at both federal and cantonal levels. The same is true for Pillar I, which may however be controlled at the federal level through the tax harmonization framework.

It is estimated that the Pillar I measures will affect Swiss MNEs Nestlé, Novartis and Roche (and perhaps a few more), as well as a few dozen Swiss subsidiaries of foreign MNEs. The new minimum tax rate is likely to affect some 200-300 Swiss groups, as well as a low 4-digit number of foreign groups with a Swiss presence.

The FFD has announced that in parallel with Switzerland’s participation at the ongoing works of the OECD, it will in collaboration with other federal departments and involving the Swiss cantons, cities, business organizations and academia come up with ”internationally accepted proposals” for the Federal Council to offer businesses the best possible framework conditions for sustainable growth by Q1/2022, depending on the progress of the OECD works. It remains to be seen what this will entail; the FFD has referred to other countries’ measures such as providing companies support in form of granting access to infrastructure or credit at favorable conditions, subsidies, state contributions for research and development activities, support for sustainable business management, as well as internationally compatible tax benefits.