Switzerland

Private Tax Rulings in Switzerland

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The authors, in this article, consider the private tax ruling system in Switzerland, together with the relevant aspects and implications of using the system.

1. Introduction

The (formal) written tax law in Switzerland is, as in many other jurisdictions, set out in rather general terms. In contrast, the actual practice, as developed by the tax administration and the tax courts, contains the specific and partly very detailed rules and regulations regarding many situations in respect of both individuals and legal entities. It does not help that each of the 26 Swiss cantons applies its own practice. However, and this is a significant improvement, the major aspects of cantonal law have been harmonized for all cantons by way of federal framework legislation, aligned to the federal tax law. The same is true for the practice set out in the many written ordinances, circulars, guidelines, notices and other announcements of the Federal Tax Administration (FTA), the association of the FTA and the cantonal tax administrations, and the cantonal tax administrations themselves.

These regulations do not constitute formal tax law, but are, rather, addressed to the various tax administrations and not to taxpayers. Nevertheless, it is essential that taxpayers and advisors know the practice of the tax administration in detail, as, in general, both federal and cantonal tax administrations follow these strictly. This is helpful, as it gives rise to predictable and consistent practice on the part of the tax administration and the equal treatment of taxpayers.

Formal tax law is more or less stable in Switzerland. However, practice can be amended, either due to decisions of the courts, i.e. the Federal Supreme Court (*Bundesgericht/Tribunal fédéral*, BGer) or the Federal Administrative Court *(Bundesverwaltungsgericht/Tribunal administratif fédéral*, BVGer), or by developments in the cantons or discussion between the cantonal tax administrations.

In this respect, it should be noted that the cantonal tax administrations can not only assess cantonal income taxes in respect of both individuals and legal entities, but also direct federal tax (which also includes an income tax). The FTA supervises the cantons with regard to direct federal tax on a regular basis and also has the right to appeal against a particular assessment in respect of direct federal tax made by a cantonal tax administration, but cannot assess taxpayers directly. Other taxes, for example, withholding tax, stamp tax and VAT are assessed by the FTA without the involvement of the local (cantonal) tax administrations.

Given the complexity of taxation in Switzerland in terms of competences, the different types of taxes, i.e. income tax, withholding tax, stamp tax and VAT, which can all be affected by specific actions, and the various ordinances, guidelines, etc., which specify the written tax law, taxpayers and their advisors have an interest in discussing the more complex situations with the tax administrations at an early stage, prior to the implementations of any actions. In addition, international groups and companies considering Switzerland and a particular canton as their new domicile want to be in a position to obtain a high level of comfort in respect of future taxation. No Chief Financial Officer (CFO) of a company likes surprises in terms of taxes for which no provision has been made and which increase the effective tax rate of the company. The same is true for individuals, be it related to the sale of a company in connection with their estate planning and in many other situations.

Having said this, the Swiss tax administrations, both at federal and cantonal level, are aware of the needs of the taxpayers. They are usually open to discuss in advance the relevant facts and tax consequences of a particular situation, be it a specific undertaking or even just a tax liability in Switzerland, and may even give a binding private tax ruling (a

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"ruling") in respect of a particular situation, outside of an ordinary tax assessment. This article, therefore, considers the nature of rulings, the typical scenarios in respect of which a ruling may be obtained, the formal procedures regarding rulings, the necessary content of rulings, and the period of time for which rulings are valid.

2. Time Is the Key

A ruling does not provide for any more preferential taxation for a taxpayer than the applicable tax law does. Any agreement between either the FTA or a local tax administration and an individual taxpayer that purports to provide for a more favourable tax rate or other preferential tax consequences of an undertaking other than covered by the law is not permitted and would be void, i.e. would not be binding on any tax administration or tax court. Such types of agreements are only valid if the written law provides for a relevant exception, which is the case for full or partial so-called tax holidays granted to companies that become resident in certain regions in Switzerland, in respect of which the political authorities have decided to support the job creation and other economic benefits by granting relief from the ordinary income tax.

However, in practice, the real value of a ruling lies not in receiving preferred taxation rates but rather in getting the comfort of knowing the tax consequences, or even more important, knowing that there are no tax consequences of a planned undertaking, be it an intercompany restructuring, a mergers and acquisitions (M&A) transaction, or even relating to transfer pricing between related parties, international and/or inter-cantonal profit allocation and other issues. Numerous examples could also be cited for individuals.

As timing is critical in many transactions, it is important to obtain the relevant clearance in a matter within weeks or even days rather than months. Most of the tax administrations in Switzerland are aware of this and do their best to have a short response time on oral or written ruling requests. Some are also open to discuss the planned undertaking in advance on an oral basis and then grant a written ruling even quicker. Sometimes a simple telephone call to the relevant tax administration may result in a clearance that is sufficient for the taxpayer or the person responsible for legal entities taxation without the need to file a specific ruling request.

In fact, experience reveals that the possibility to discuss critical undertakings or potential risks with the tax administration and to obtain written confirmation of the particular tax consequences quickly is a key element in relation to international tax competition. This significantly increases the attractiveness of Switzerland as a tax location, irrespective of any taxation model or special "boxes" providing for preferred tax rates in respect of certain types of income, for example, those relating to intellectual property (IP).

3. Typical Ruling Scenarios

Although other authors or even court decisions may indicate that private tax rulings can be granted with regard to the clarification of certain fact patterns or certain elements of the relevant facts, whereas so-called legal questions or the legal consequences of the relevant facts could not be subject to a ruling,[1] the practice is slightly different.

Typically, a taxpayer involved in a more complex transaction is supported by an advisor who is familiar with the applicable law, ordinances, guidelines, etc. Nevertheless, the advisor may realize that there is a risk that the competent tax administration could treat the relevant facts in a different way to that in which the advisor has treated them, be it with regard to the alignment of the facts from an economic perspective with their formal qualification, so that the advisor wants to receive confirmation of his own legal qualification of a planned intercompany transaction or where the nature of the relevant issue implies a certain degree of discretion and, therefore, uncertainty. Other cases may focus on the determination and proof of the relevant facts, for example, in relation to international and/or inter-cantonal profit allocation regarding different sources of income, transfer pricing and the particular requirements needed to obtain the benefits of a tax treaty.

These examples also make it clear that rulings may either be obtained in respect of a specific case, for example, regarding the VAT consequences of a particular M&A transaction or for a longer duration, such as the determination of the facts relevant for the international profit allocation of a multinational enterprise (MNE).

It is common to all these situations and generally a condition for the binding effect of any ruling (*see* section 4.) that the relevant issues must be discussed and clarified in advance. Once a transaction has occurred or a certain price is paid for the delivery of goods or services, there is no reason for the tax administration to give a binding ruling with regard to

1 *See* M. Beusch, *Zulässigkeit und Wirkungen von Verständigungen (Ruling)*, ZSIS 1, p. 4 et seq. (2009).

that situation that is outside of an ordinary tax assessment. Indeed, there is no legal basis to grant such a ruling after the realization of the relevant actions.

The same is broadly true for those scenarios that relate to a longer duration, such as international profit allocation. For instance, if the method applied to determine the relevant portion of profit subject to tax in Switzerland was not agreed in advance, the tax administration is free to request the taxpayer to disclose all of the facts required to assess the appropriate portion of the profit. Should the taxpayer not be able, or be unwilling, to produce the relevant information and proofs on request, the tax administration will have to estimate the profit. This might not be advantageous to the taxpayer. In such a case, a consensual determination of the profit could only be agreed with the tax administration in respect of future tax years.

Experience shows that, in practice, even in a situation such as just described, it may be possible to arrive at a reasonable solution and method to determine the appropriate profit allocation retroactively, even if not agreed in advance. However, such a solution would not fall within the terms of a private or an advance ruling, but would rather be treated as a unanimous settlement of a controversy in the course of a pending assessment procedure. Although the result is similar, the latter has nothing to do with a ruling.

It should also be noted that a particular tax assessment does not, unless otherwise agreed with or communicated by the competent tax administration, provide for the same treatment or qualification of a particular single transaction or of a situation of a longer duration. In other words, if an intercompany transaction, for example, the transfer of a group company to another group company, was not treated as a taxable event in course of the ordinary tax assessment, this does not protect a taxpayer from taxation if another similar transaction is effected in a later tax year.

4. How To Obtain Rulings

With one exception in the Swiss VAT Law *(Bundesgesetz über die Mehrwertsteuer/Loi fédérale régissant la taxe sur la valeur ajoutée*, MWSTG),[2] Swiss tax law does not refer to rulings. Consequently, there are no guidelines that are set out formally in law describing the process to be followed to obtain a binding ruling. Some cantons have issued their own rules, or rather recommendations, which a taxpayer should follow to obtain a ruling within a reasonable time frame.

It should also be noted that, with the exception in the MWSTG noted in the previous paragraph, there is not even a legal entitlement for a taxpayer to obtain a binding ruling. This means that a tax administration can refuse to grant a ruling even if the application meets the relevant "standard" in terms of content and accuracy, and can postpone any decision regarding the relevant question to a later stage after the formal assessment has been made. The taxpayer requesting a ruling can appeal neither against such a denial on the part of the tax administration nor against a negative response to a ruling request. In these circumstances, the taxpayer will either have to find a different, depending on the particular case, less aggressive or less comprehensive solution to realize the respective undertaking or take the risk of any adverse tax consequences, realize his undertaking and wait for the assessment against which an appeal could be made to the next (court or tax authority) instance.

However, as noted in section 1., most tax administrations in Switzerland recognize the taxpayers' need to obtain clearance in respect of any potential risk prior to the realization of an undertaking, be it a condition of the decision to move its headquarters to Switzerland, to open a subsidiary or branch, or to perform a single transaction, which could result in a significant exposure for the taxpayer in the event of any adverse tax consequences. Some Swiss tax administrations also adopt the approach that they must ultimately legally qualify a given situation either in the course of an advance ruling request or later when a formal assessment is made. Given such an approach, Swiss tax administrations are willing to deal with ruling requests. This, however, does not mean that any ruling requests will be granted at all.

Prior to even starting to draft a ruling request, a taxpayer or the advisor must have a clear idea or knowledge of the planned undertaking, the relevant facts and the purpose in respect of which the ruling is being requested, i.e. of the legal consequences of the relevant facts. For instance, a ruling request for confirmation regarding the entitlement to the benefits of a tax treaty to get relief from Swiss withholding tax on dividend payments requires the disclosure of the balance sheet of the recipient entity in the other jurisdiction. This means that it does not make sense to file the ruling request without being in a position to provide information regarding the relevant balance sheet, and, indeed, without filing the relevant documents with the ruling request. The same is true with regard to a financing arrangement in respect of which the counterparties have not yet agreed the particular conditions, i.e. regarding interest, security, etc., as the

2 CH: *Bundesgesetz über die Mehrwertsteuer* (MWSTG)/*Loi fédérale régissant la taxe sur la valeur ajoutée* art. 63.

tax administration cannot, and is also very unlikely to be willing, to make any generic statements regarding such a transaction.

Once the relevant facts are clear or at least a specifically distinguished set of alternatives in respect of a given transaction can be presented, it may make sense to first contact the competent tax administration and discuss the situation in advance so that the facts, the planned transaction and the legal qualification can be dealt with by telephone or at a personal meeting. This allows the parties to discuss any relevant open issues, to amend the planned transaction and to collect any additional information that may be relevant to the tax administration, instead of requiring the parties to enter into a protracted and time-consuming correspondence.

Once the situation has been clarified and both sides, i.e. the taxpayer and the competent tax administration, have arrived at a conclusion on which they can agree, the written ruling request can be filed and is then usually confirmed by the tax administration very quickly. In less complicated cases, it may make sense to contact the tax administration quickly by telephone to identify the person in the administration who will deal with the ruling request. This also helps speed up the process and ensures that the ruling request and the supporting documents are sent to the correct person from the outset. In addition, an advance telephone call helps to discuss the timing and, if the timing is critical, to explain the urgency to the relevant person. Such individuals will usually do their best to work on the ruling request as quickly as possible.

Although a ruling would generally be binding if it were granted on an oral basis only, it would be for a taxpayer to prove that he had obtained such a binding ruling from the tax administration. Most tax administrations are also reluctant to give binding rulings on a purely oral basis, as they want to avoid any later dispute as to whether the relevant facts were presented in full or whether there was any misunderstanding. Consequently, in order to be able to rely on a binding ruling from the tax administration, a written ruling request should be made.

The accuracy of the information regarding the relevant facts relating to a particular undertaking or situation regarding which a ruling is requested is a prerequisite for the validity and the binding effect of the ruling. The competent tax administration must be in a position to recognize and understand the context of the planned behaviour, including the facts behind and surrounding it. This requires the applicant requesting a ruling to provide the relevant facts in sufficient detail, but not too extensively, which could unintentionally misdirect the tax authorities. It is also unacceptable to omit certain facts that, however important, might have a negative effect on the requested ruling on the basis that it is for the tax administration to ask for further details if they think that this is required. Should it transpire at a later stage, i.e. in the course of the formal assessment (in this respect it should be noted that a private ruling is not an assessment and only an answer from the tax administration with binding effect), that certain relevant facts with adverse implications for the legal qualification for the situation at hand were not presented to the tax administration when the ruling was granted, such a ruling could be held to be void by either the tax administration or the tax courts. It is also usually necessary to disclose the identity of the taxpayer requesting the ruling. In an initial stage, a request might be made on a no-name basis in order to clarify a generic question, but binding effect (*see* section 7.) requires that the ruling identifies the relevant taxpayer.

Rather than presenting the relevant, true and complete facts when a ruling is obtained, it is, in practice, often a challenge for both the taxpayer and the advisor to ensure that these facts are not rendered incorrect by later developments that were not initially planned or even foreseen. For instance, transfer prices in respect of intercompany services may become too high or low if the services are later extended or reduced. The same applies to a financing arrangement in respect of which a ruling was obtained confirming that no withholding tax was due on interest payments if the number of non-bank creditors becomes larger than when the ruling was requested, thereby exceeding more than 20 non-bank creditors. Many similar examples can be cited, especially in respect of rulings granted for long-term situations.

Consequently, whenever the relevant actions are not realized as described in the ruling request with regard to a single transaction or change from when the ruling in respect of situations of a longer duration was requested, the ruling may lose its binding effect, i.e. become void. In order to ensure the validity of an existing ruling, it is, therefore, recommended that an updated or amended ruling is obtained by presenting the planned amendments of the relevant facts and circumstances to the competent tax administration prior to making the changes.

5. Where To File

As stated in section 1., the cantonal tax administrations are competent to assess cantonal and direct federal income taxes, whereas the FTA is competent to assess withholding tax, stamp tax and VAT. Some other taxes, for example, taxes relating to real estate, are assessed by local (municipal) tax administrations.

In order to obtain a binding ruling, it is essential that the application is filed with the competent tax administration. This means that a ruling request relating to direct federal tax and cantonal income tax must be filed with the cantonal tax administration of the domicile of the taxpayer and, if no cantonal but a municipal tax administration is competent to assess these taxes, with that municipal administration. Should clearance be requested in respect of withholding tax, stamp tax and VAT, the ruling request must be sent separately to the relevant department in the FTA, as it is not for the various departments of the FTA to liaise or coordinate with each other regarding such issues. However, if, in a particular case, one department of the FTA grants a ruling covering all of the taxes in respect of which the FTA is competent, without conditions, a taxpayer who is acting in good faith can rely on such a ruling. It should, however, be noted that an advisor is supposed to be aware of the relevant competencies and their order. If these competencies are disregarded, in such circumstances, the advisor and the taxpayer would, in most cases, not be held to be acting in good faith. (*See* section 6. for more on good faith.)

Following decisions of the BGer, the question has recently arisen as to whether a ruling granted by the FTA and not the competent cantonal tax administration in respect of direct federal tax would still have a binding, i.e. protective, effect on the taxpayer or, vice versa, a tax ruling granted by the cantonal tax authority with regard to direct federal tax could still be challenged by the FTA if the ruling request was not presented to this authority as well.[3] The latter question is of particular significance, as a taxpayer needs to know whether it is sufficient to involve the cantonal tax administration to the extent that only federal income taxes, and not any other federal taxes, are concerned, or whether any ruling request must also be sent to the FTA by default.

Given the clear competence for the assessment of direct federal income tax, it should be sufficient to involve only the cantonal tax administration where a single transaction is concerned. However, if the ruling request is based on a long-term situation, for example, with regard to international tax allocation, it would be wise to also involve the FTA, as the FTA could otherwise, as part of its function as a supervisory authority, inform the cantonal tax administration to deny the application of the ruling after a certain period of time. Although an existing ruling for a longer duration can be terminated, this would be more difficult if the FTA had also agreed to the ruling.

Under no circumstances is it recommended to involve only the FTA and not the relevant cantonal tax administration, as that administration would, should it adopt a different position from that of the FTA, enforce its competence to assess direct federal taxes and, therefore, not recognize the ruling. In addition, although direct federal tax and cantonal income tax are aligned with each other, a ruling only granted in respect of direct federal taxes has no binding effect with regard to cantonal taxes.

Finally, although the question has not yet been decided by the BGer, it is recommended to not only involve the tax administration of the primary domicile of a taxpayer, but also that of any secondary domicile, i.e. where a branch is maintained. This ensures that the tax administration of the secondary domicile respects the ruling and has adopted the same position of the primary competent tax administration. Unfortunately, experience indicates that, in the absence of specific rulings confirmed by the tax administration of the secondary domicile, the latter might not regard itself as bound or even influenced by the ruling obtained from the primary competent tax administration.

6. Validity and Expiry Dates

The reason for obtaining a private ruling is the desire on the part of the taxpayer for advance clarification of potential tax issues of a particular undertaking or for clear guidance with regard to the determination of the relevant facts with regard to future taxation. In any case, as a ruling does not constitute an ordinary assessment, the taxpayer expects to be protected against tax administration taking a different position, which could result in an adverse or less favourable taxation of the situation that was the subject of the ruling.

Such protection is granted by the relevant tax administration or the tax courts only if specified criteria are met. As stated in section 4., a ruling is only valid if the facts presented to the tax administration when the ruling was obtained were true and have not changed in the interim. It is also beneficial if the ruling was granted without being subject to conditions. For instance, the tax administration might grant a ruling with regard to the entitlement to rely on a specific tax treaty subject to the condition that the foreign, i.e. non-Swiss, company can provide for sufficient substance or for a sufficient debt:equity ratio. Should such a ratio not be achieved by the time the tax treaty is applied, the taxpayer cannot rely on such a ruling.

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3 *See* U. Broger & L. Aebi, *Bindungswirkung kantonaler Steuerrulings für die direkte Bundessteuer, Bemerkungen zum Bundesgerichtsurteil 2C_708/2011 vom 5. Oktober 2012*, Der Schweizer Treuhänder, p. 605 (2013).

In addition, again as stated in section 4., a ruling must have been granted by the competent tax administration. If it was granted by a different tax administration, for example, by a municipal tax administration and not the competent cantonal tax administration, the ruling would not be binding, unless the taxpayer was, acting in good faith (*see* section 7.), unable to recognize the fact that the wrong tax administration had granted the ruling.

The same applies to erroneous decisions made by the competent tax administration in the course of granting the ruling. Such a ruling would only be binding on that tax administration if the mistake was not recognized by the taxpayer, or the advisor, and they could not be expected to realize that a mistake had been made. A ruling being erroneous means that it violates the law or a clear and consistent practice that is known to the taxpayer or the advisor.

The binding effect of a ruling, however, only makes sense (or, in other words, the interest of a taxpayer in being protected against a different position or treatment by the tax administration is valued higher than the "correct" application of the law), if the undertaking that is subject to the ruling has already been realized and if the taxpayer cannot revise or amend the undertaking without suffering damage or other adverse consequences. For instance, if a ruling is granted in view of a planned intra-group restructuring, the binding effect would not apply if the tax administration discovered and communicated their mistake prior to the restructuring. Although a ruling, broadly, does not provide for a time limit within which a planned undertaking must be realized, it is recommended a taxpayer should not wait too long once the ruling has been granted in effecting the relevant actions, as, otherwise, the tax administration could consciously rethink their position and withhold the ruling.

The latter also applies to a change of law. Should, for example, the FTA have granted a ruling confirming that there are no withholding tax consequences arising from the acquisition of a participation through a special purpose vehicle (SPV), such a ruling does not provide any protection against different taxation if, when the acquisition takes place, the applicable law has changed, compared to when the ruling was granted.

It should be noted that a change of the applicable law "overrides" any existing ruling, which is basically relevant to long-term situations. For instance, the special tax privileges of mixed or holding companies, which are often confirmed by way of rulings, should be noted in this regard. If such special tax regimes are abolished by a change of law, no ruling can provide for the continuation of such a status.

Although there is a certain degree of controversy as to whether a contradicting decision by a court, even the BGer, or a change in the practice applied by the tax administration makes an existing ruling void, it is the authors' opinion and also that of others[4] that such a change does not automatically make a ruling void, but, rather, permits the tax administration to give notice of termination of an existing ruling, especially where a ruling applies for a longer duration. The length of the notice period will depend on the effect and the consequences that the termination of the ruling has on the taxpayer. Nevertheless, as the Swiss tax administration in general has signed numerous rulings and is anticipated to continue doing so in the future, the taxpayer is expected to review the relevant long-term rulings on a regular basis, as it would be too much to expect the tax administration to terminate rulings on a case-by-case basis should the relevant tax administration have amended its practice, thereby giving rise to adverse tax consequences compared to those under the ruling.

7. In Good Faith

The application of a ruling requires that both the taxpayer and the tax administration act in good faith. A taxpayer that has not acted in good faith, for example, by not presenting all of the relevant facts to the tax administration, does not deserve protection against the tax administration taking a different position at a later stage. On the other hand, if all of the relevant criteria have been met, the binding effect of a valid ruling is a valuable asset that permits a taxpayer to make a broad range of decisions while always remaining aware of the precise exposure towards the tax administration. This is essential to preserve the ability to discuss a case with the Swiss tax administration in general on a colleague-to-colleague basis and to arrive at constructive solutions for particular cases outside of the formal assessment procedure.

8. Conclusion

No company likes surprises in terms of taxes, be it an intercompany restructuring, an M&A transaction, transfer pricing issues between related parties, international and/or inter-cantonal profit allocation. Many examples could also be listed for individuals (for instance, a company sale in connection with estate planning). In order to be in a position to obtain a high level of comfort in respect of future taxation in Switzerland, it is possible to apply for a tax ruling. However, a

4 *See* C. Morf, A. Mueller & T. Amstutz, *Schweizer Steuerruling – Erfolgsmodell und Werthaltigkeit, Bedeutung und Verbindlichkeit für den Steuerstandort,* Der Schweizer Treuhänder, p. 813 (2008).

ruling has a binding effect only if the relevant issues are discussed and clarified in advance with the competent tax administration and based on all relevant information in detail. Otherwise, such a ruling could be held to be void by either the tax administrations or the tax courts at a later stage.