

## **EXCERPT FROM THE INSTRUCTIONS FOR TAXATION OF ASSOCIATED COMPANIES, HOLDING COMPANIES, FOREIGN BASE FIRMS AND MIXED COMPANIES (HDW)**

### **Foreign base firms (Art. 76 para 1 StG)**

#### **I. Requirements for Taxation as a Foreign Base Firm**

Foreign base firms under Art. 76 para 1 StG (Schwyz tax code) are corporations, cooperatives and foundations as well as branches of foreign legal entities that carry out administrative activities but do not conduct business in Switzerland.

For purposes of this law “administrative activities” means first and foremost the management of its own wealth, that is, assets that the firm already possesses and which increase without any active commercial business being conducted. Auxiliary activities like the sale of intangible assets, conveyance of know-how and billing and collection are also considered administrative in nature, provided they require no actual office activities or a large staff located in Switzerland. In contrast, activities like for example acquisition, market research, trading, sales, consulting and marketing in Switzerland are considered business activities.

A configuration of business abroad and administrative functions in Switzerland is presumed if, in response to instructions arriving in Switzerland from abroad, business transactions are conducted that take place outside of Switzerland and do not involve the Swiss market to any significant degree. As used in the previous paragraph, instructions comprise both general directives for action and specific orders from top management or, in the case of combines, on the part of the paramount executive bodies.

#### **II. Tax on Profits**

##### *1. Revenue from Equity*

No profit tax is assessed on domestic or foreign profits derived from equity or capital gains. “Equity” means title to shares of ownership in another firm, provided it exceeds 20 per cent thereof or has a market value over 2 million francs (Art. 74 para 1 StG).

Profits and capital gains from foreign equity that do not meet these requirements are treated as income from a Swiss source and equivalent to profits from domestic equity.

Respective administrative and financing expenses as well as capital losses are deducted from profits. Financing expense is determined as a proportion of the equity’s book value to the book value of total assets.

A total loss from equity may not be set off against profits from Swiss or foreign sources.

#### *2. Other income from Switzerland*

Other income from Switzerland comprises earnings from administrative activity in Switzerland, profits from equity and capital gains from debtors domiciled in Switzerland, provided they are not considered equity under Art. 74 para 1 StG (see Part B), as well as earnings from Swiss real property. Any business expenses required to obtain these earnings are deducted from the latter. Financing expenses may be allotted in the same proportion as that existing between the assets in question on one hand and total assets on the other. However, in other respects net profits from Switzerland are determined on the basis of an industry/line of business calculation.

Net profits from Switzerland are taxed at the regular rate. Net losses may be set off against the taxable portion of profits from abroad.

#### *3. Other income from abroad*

Other income from abroad includes earnings from foreign business activity and earnings from debtors domiciled abroad.

Any business expenses arising from these earnings are deducted from the latter. Financing expenses may be allotted in the same proportion as that existing between the assets in question on one hand and total assets on the other. In other respects net profits from abroad are determined on the basis of an industry/line of business calculation.

Net profits from abroad are taxed at a rate of 10 per cent. Proportional net losses may be set off against net profits from Swiss sources.

#### *4. Income applying for an exemption from foreign withholding taxes*

If you receive income from abroad applying for an exemption from foreign withholding taxes and that is subject to a double taxation agreement, and this agreement, to be applicable, requires that you pay regular taxes in Switzerland, then you must pay regular Swiss taxes on an amount that is determined as follows: your foreign income plus your income from Switzerland minus the expenses incurred in obtaining the foreign income (Art. 76 para 3 StG).

#### *5. Rate of taxation*

The rate of taxation of profits is determined solely on the basis of that portion of net profits that is subject to the tax.

### **III. Capital Levy**

Under Art. 79 para 1 StG taxable equity capital comprises the share capital paid in, the open reserves and the hidden reserves accumulated from taxed profits, plus the hidden reserves that would have accrued from taxable profits if profits had been taxed. Moreover under Art. 80 StG taxable equity capital is augmented by that portion of borrowed capital that is economically equivalent to equity capital.

The simple capital levy is collected at a rate of 0.025 per thousand of taxable equity capital, but at least 100 francs (Art. 83 para 1 StG).

Under Art. 83 para 2 StG the rate of the simple capital levy on real property located in Canton Schwyz is 0.4 per thousand.

### **IV. Change in Status**

The first time a firm is taxed as a foreign base company, any existing hidden reserves are included in the tax base. Nonetheless such reserves may be exempted from the capital levy if they remain fully taxable in Switzerland (real property, Swiss securities, etc.). Under Art. 77 StG the firm may demand

that taxation of its hidden reserves on equity and intangible assets be deferred (see Arts. 74, 243 and 244 StG).

The prerequisites for being considered a foreign base company must be met in every fiscal year. Should a firm fail to meet these conditions in any given year, the tax privilege is inapplicable for that year, even if the conditions are met again later.

Hidden reserves that accrue while a firm has foreign base company status may be declared in a tax balance sheet before the firm becomes subject to regular taxation. Losses from fiscal years preceding the change in status may be set off only against those earnings that are subject to taxation.

## **V. Procedure**

Foreign base firms are subject to the regular tax assessment procedure. They must submit a tax declaration at the conclusion of each fiscal year. In this same return they may apply for foreign base tax treatment. Furthermore they must furnish a report showing a breakdown per lines of business. Under Art. 76 para 1 StG the tax inspector decides which tax regimen will be applied.