

Tax & Legal Services

Corporate Tax Reform III & Base Erosion and Profit Shifting (BEPS)

An overview

8 July 2015

pwc

Agenda

Page

1. Base Erosion and Profit Shifting (BEPS) 1
 - a) How come?
 - b) Overview on action items
 - c) Impact on a typical asset management structure
 - d) Key messages for Asset Managers

2. Swiss Corporate Tax Reform III 9
 - a) Measures in reform package
 - b) Measures considered but not included in reform package
 - c) Next Steps
 - d) Outlook/ political agenda

3. Q&A 18

Base Erosion and Profit Shifting (BEPS)

1

BEPS - How come?



BEPS

- Increasingly **interconnected world**
- **Outdated national tax laws** not kept pace with globalization, fluid capital & digital economy
- (Legal) tax planning practice seems more and more in conflict with changing **public perception** of tax fairness and morale
- **Allocation of profits not appropriately** in line with where value is created?
- Launch of **Base Erosion & Profit Shifting ('BEPS')** initiative by OECD at request of G20 Finance Ministers in February 2013
- Publication of **BEPS Action Plan** in July 2013
- **15 specific actions** identified to address challenge of base erosion and profit shifting

⇒ ***Not directly addressing harmonisation of tax rates & tax base***

BEPS – Overview on action items (1/4)

ACTION 1: Address the challenges of the digital economy	ACTION 2: Neutralise the effect of hybrid mismatch arrangements	ACTION 3: Strengthen CFC rules	ACTION 4: Limit base erosion via interest deductions and other financial payments	ACTION 5: Counter harmful tax practices more effectively, taking into account transparency and substance
ACTION 6: Prevent treaty abuse	ACTION 7: Prevent the artificial avoidance of PE status	ACTION 8: Assuring that TP outcomes are in line with value creation Intangibles	ACTION 9: Assuring that TP outcomes are in line with value creation Risks & capital	ACTION 10: Assuring that TP outcomes are in line with value creation Other high-risk transactions
ACTION 11: Establish methodologies to collect and analyse data on BEPS and the actions to address it	ACTION 12: Require taxpayers to disclose their aggressive tax planning arrangements	ACTION 13: Re-examine transfer pricing documentation	ACTION 14: Make dispute resolution mechanisms more effective	ACTION 15: Develop a multilateral instrument

BEPS – Overview on action items (2/4)

- **Action 1 – Address the tax challenges of the digital economy**
 - Include, but not limited to: the ability of a company to have a significant digital presence in the economy of another country without being liable to taxation due to the lack of nexus under current international rules, the attribution of value created from the generation of marketable location relevant data through the use of digital products and services, the characterisation of income derived from new business models, the application of related source rules, and how to ensure the effective collection of VAT/GST with respect to the cross-border supply of digital goods and services.
- **Action 2 – Neutralise the effects of hybrid mismatch arrangements**
 - Develop model treaty provisions and recommendations regarding the design of domestic rules to neutralise the effect (e.g. double non-taxation, double deduction, long-term deferral) of hybrid instruments and entities.
- **Action 3 – Strengthen CFC rules**
 - Develop recommendations regarding the design of controlled foreign company rules.
- **Action 4 – Limit base erosion via interest deductions and other financial payments**
 - Develop recommendations regarding best practices in the design of rules to prevent base erosion through the use of interest expense, for example through the use of related-party and third-party debt to achieve excessive interest deductions or to finance the production of exempt or deferred income, and other financial payments that are economically equivalent to interest payments.
- **Action 5 – Counter harmful tax practices more effectively, taking into account transparency and substance**
 - Revamp the work on harmful tax practices with a priority on improving transparency, including compulsory spontaneous exchange on rulings related to preferential regimes, and on requiring substantial activity for any preferential regime.

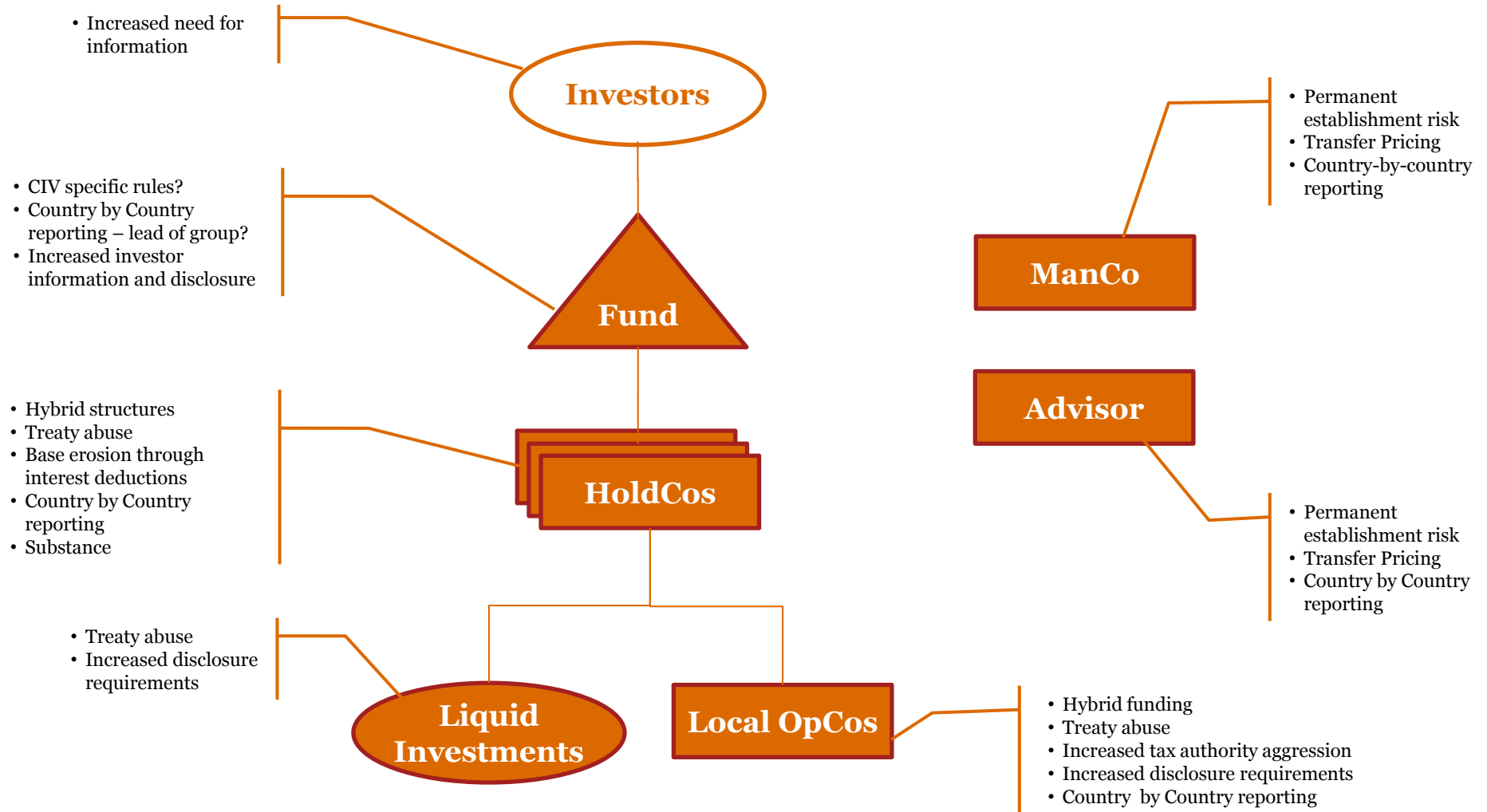
BEPS – Overview on action items (3/4)

- **Action 6 – Prevent treaty abuse**
 - Develop model treaty provisions and recommendations regarding the design of domestic rules to prevent the granting of treaty benefits in inappropriate circumstances.
 - clarify that tax treaties are not intended to be used to generate double non-taxation and to identify the tax policy considerations that, in general, countries should consider before deciding to enter into a tax treaty with another country.
- **Action 7 – Prevent the artificial avoidance of PE Status**
 - Develop changes to the definition of PE to prevent the artificial avoidance of PE status in relation to BEPS, including through the use of commissionaire arrangements and the specific activity exemptions.
- **Action 8 – Assure that transfer pricing outcomes are in line with value creation: intangibles**
 - Develop rules to prevent BEPS by moving intangibles among group members.
- **Action 9 – Assure that transfer pricing outcomes are in line with value creation: risks and capital**
 - Develop rules to prevent BEPS by transferring risks among, or allocating excessive capital to, group members.
- **Action 10 – Assure that transfer pricing outcomes are in line with value creation: other high-risk transactions**
 - Develop rules to prevent BEPS by engaging in transactions which would not, or would only very rarely, occur between third parties.

BEPS – Overview on action items (4/4)

- **Action 11 – Establish methodologies to collect and analyse data on BEPS and the actions to address it**
 - Develop recommendations regarding indicators of the scale and economic impact of BEPS and ensure that tools are available to monitor and evaluate the effectiveness and economic impact of the actions taken to address BEPS on an ongoing basis.
- **Action 12 – Require taxpayers to disclose their aggressive tax planning arrangements**
 - Develop recommendations regarding the design of mandatory disclosure rules for aggressive or abusive transactions, arrangements, or structures, taking into consideration the administrative costs for tax administrations and businesses and drawing on experiences of the increasing number of countries that have such rules.
- **Action 13 – Re-examine transfer pricing documentation**
 - Develop rules regarding transfer pricing documentation to enhance transparency for tax administration, taking into consideration the compliance costs for business.
- **Action 14 – Make dispute resolution mechanisms more effective**
 - Develop solutions to address obstacles that prevent countries from solving treaty related disputes under MAP, including the absence of arbitration provisions in most treaties and the fact that access to MAP and arbitration may be denied in certain cases.
- **Action 15 – Develop a multilateral instrument**
 - Analyse the tax and public international law issues related to the development of a multilateral instrument to enable jurisdictions that wish to do so to implement measures developed in the course of the work on BEPS and amend bilateral tax treaties.

Impact on a typical asset management structure



Key messages for Asset Managers

1

The BEPS agenda is not directly targeted at asset management operations – however there will be consequences for the asset management industry to consider directly arising from changes in approach, interpretation or legislation.

2

There will be a greater focus on financing instruments/transactions (hybrid instruments, interest deductions etc.) and the qualification of the respective cash flows for tax and tax treaty purposes.

3

Treaty abuse and general anti avoidance considerations might become even more important compared to today, potentially leading to additional substance requirements. Depending on the outcome of the proposals, investment structures might be less complex going forward.

4

A significant amount of the BEPS Action Plan approach is consistent with the current attitude of certain key fiscal authorities – this will only serve to increase those fiscal authorities' confidence in their approach.

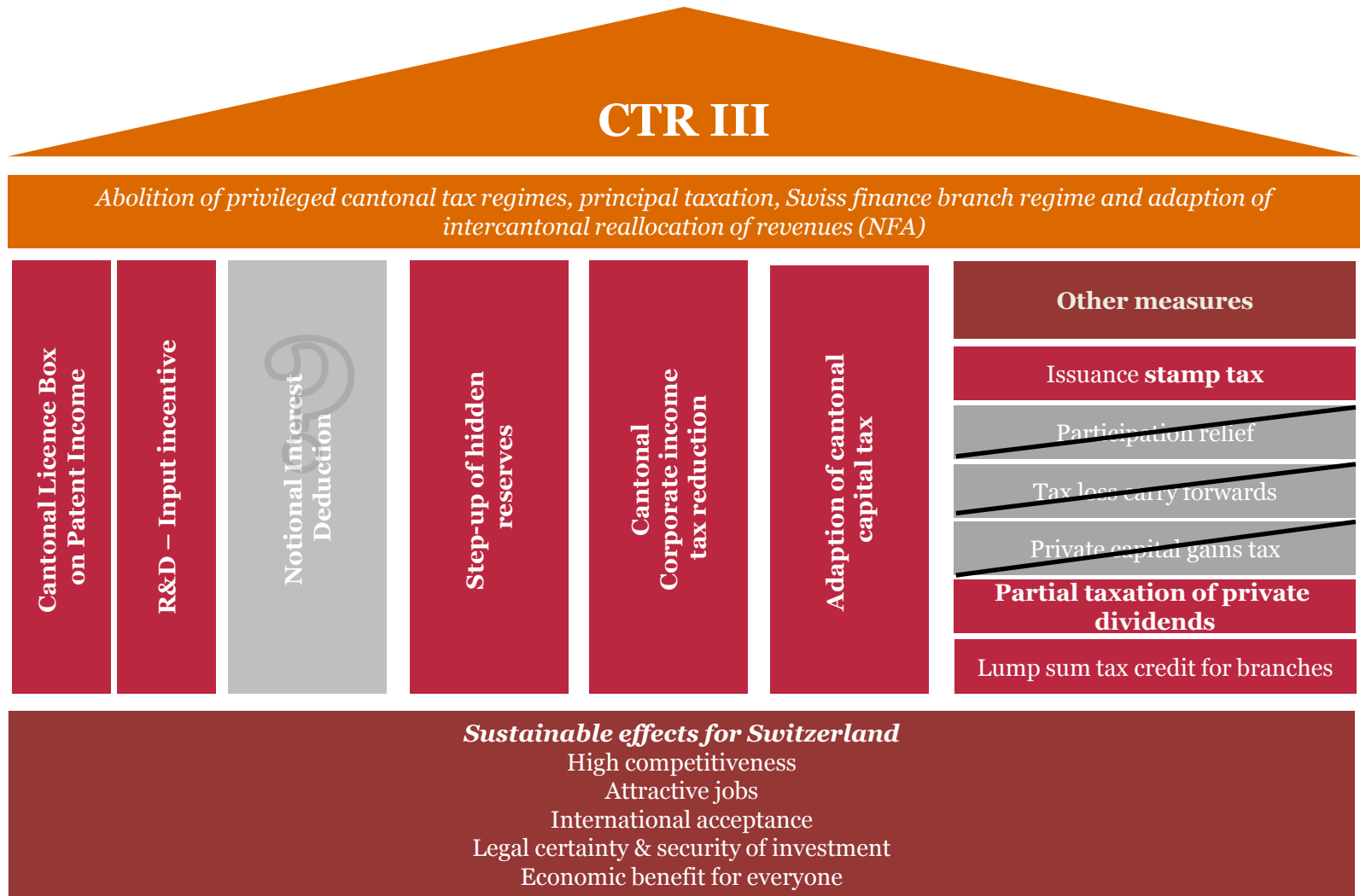
5

The risk areas highlighted by BEPS (in particular PE threshold and transfer pricing related to risks and capital) are current issues not ones to leave for the future – groups should be reviewing their positions now.

Swiss Corporate Tax Reform III

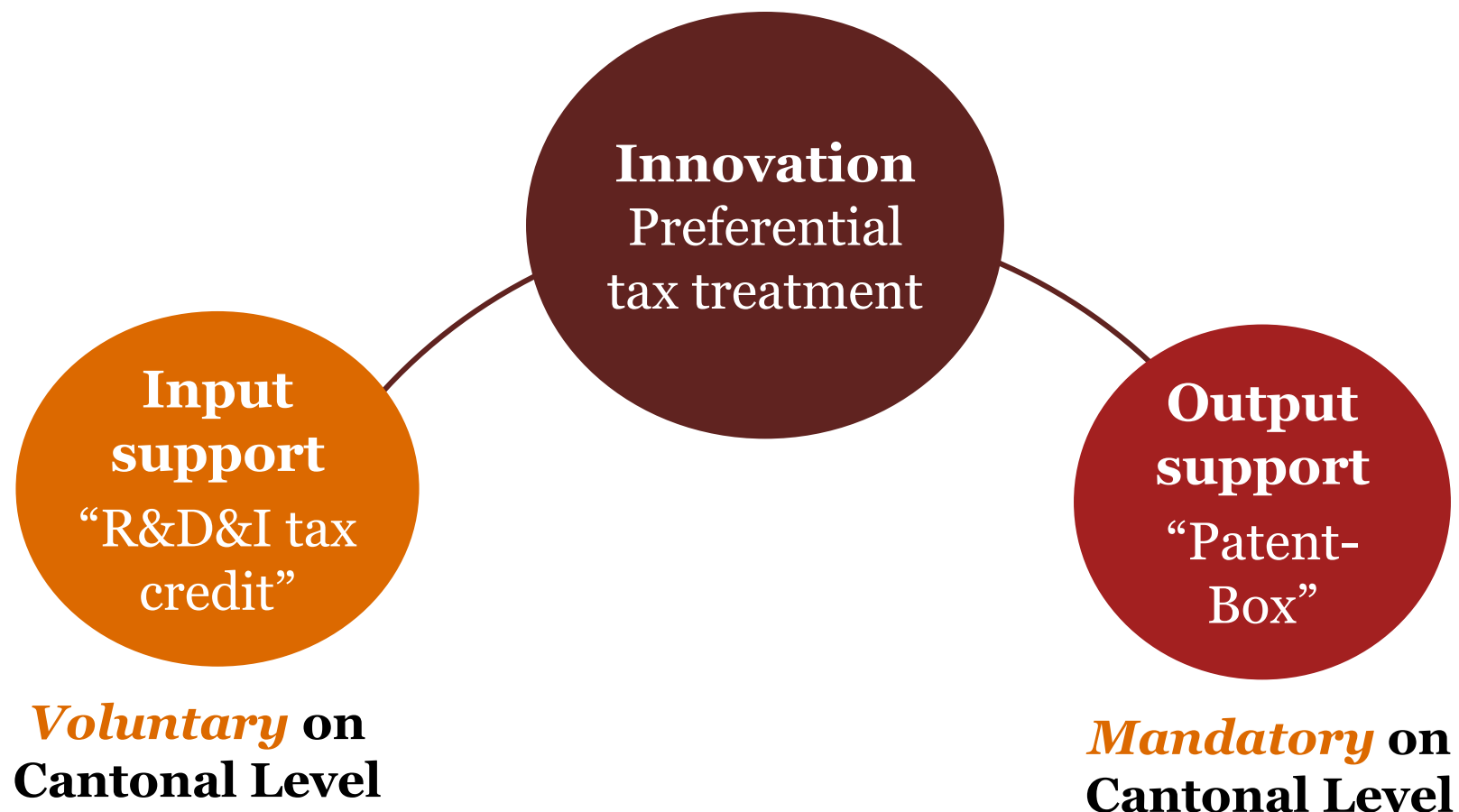


Overview of the parameters to be addressed



Measures in reform package (1/3)

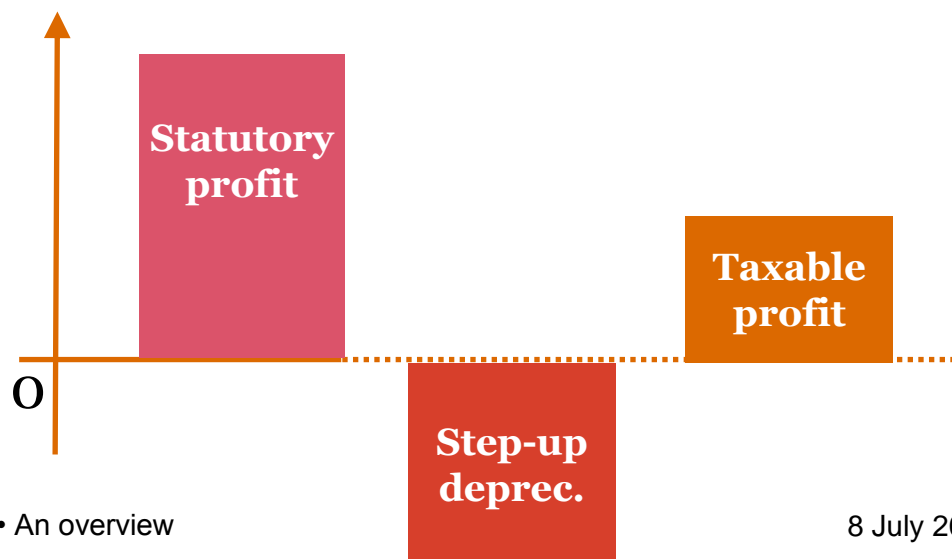
1. Cantonal Patent Box and R&D input promotion



Measures in reform package (2/3)

2. Systematic realisation of hidden reserves – step-up

- **Hidden reserves** (including goodwill) will be **reported in the tax balance** sheet without tax impact at the beginning of the Swiss tax liability (step-up in basis).
- Reported hidden reserves will then mean **higher tax deductible depreciation potential** for all concerned companies;
- **Separate rules** for:
 - Transition rule upon abolition of current StHG Art. 28 status → Art. 78g StHG
 - Rules concerning entry into patent box → Art. 24a Lit. 2 StHG
 - Harmonised rules upon entry into tax liability → Art. 24b StHG; Art 61a DFT
 - Harmonised rules upon exit out of the tax liability → Art. 24c StHG; Art 61b DFT



Measures in reform package (3/3)

3. Cantonal corporate tax rate reductions and other measures to increase attractiveness

- **Reduction of cantonal corporate income tax rates** at the discretion of the cantons
- Various cantons announced **target tax rates**:
 - Geneva, Vaud: Target rate of ~13% announced;
 - Fribourg: 13.72% (cantonal income tax for legal entities: 4%);
 - Zug: Target rate of 12% announced;
 - Zurich: Depending on positioning of neighbouring cantons;
 - Lucerne, Schwyz, Nidwalden: Current rate already approx. 12.5%.

4. Further measures to increase attractiveness

- Optional adaption of cantonal capital tax;
- Abolition of issuance stamp tax on equity capital;
- Amendment of partial taxation of dividend income from qualified investments for individuals for min. 10% shareholdings
- Lump sum tax credit for Swiss branches of foreign companies

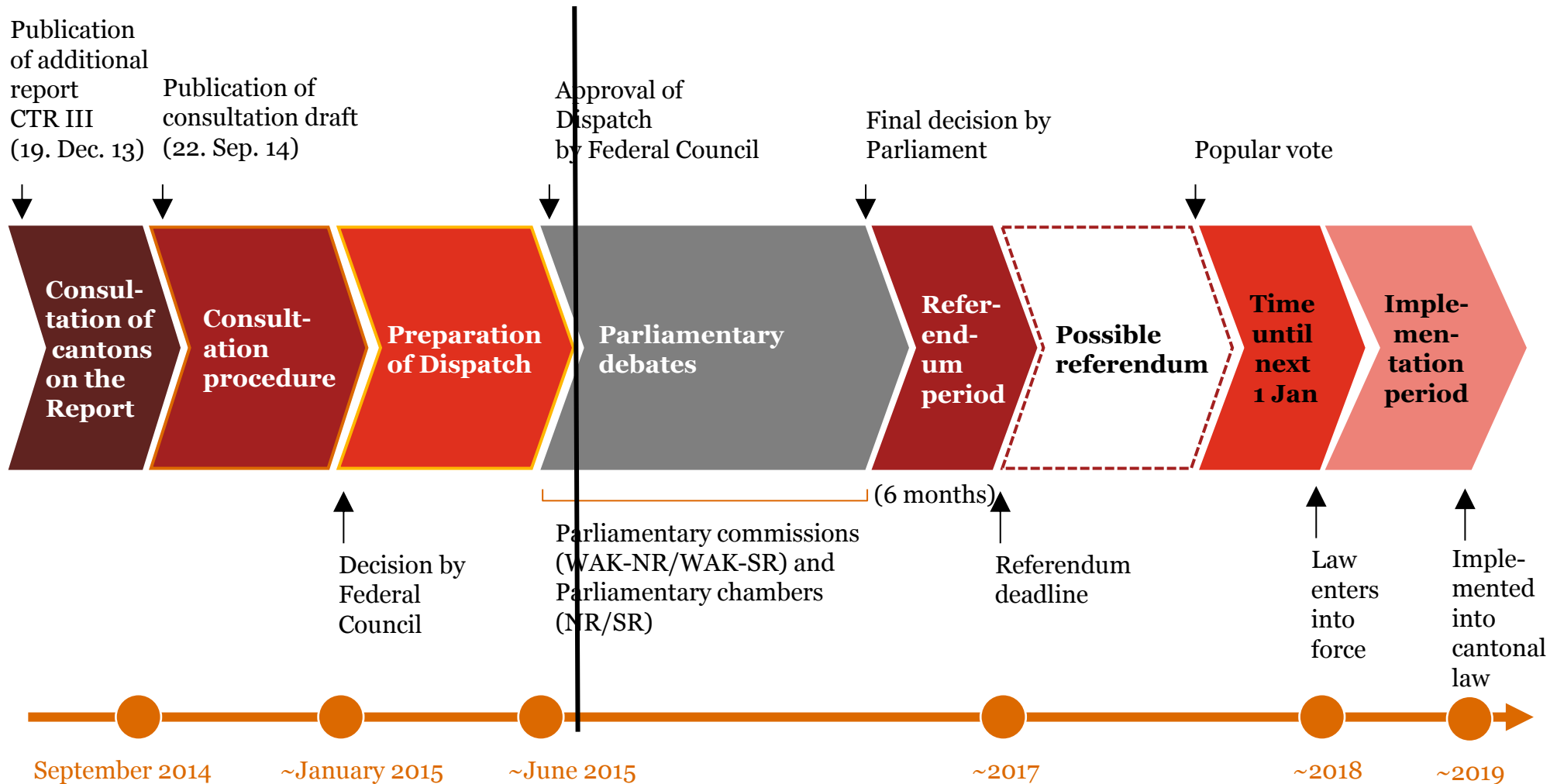
Measures considered but not included in reform package

- No introduction of Notional Interest Deduction (NID);
- No capital gains tax on privately held securities by individuals;
- No switch to direct participation exemption, and;
- No change of tax loss carry forward rules;
- No introduction of Tonnage Tax (due to lack of compatibility with constitution).

Next Steps

- The current corporate taxation rules and specifically the tax regimes that will be abolished have contributed to the success of Switzerland.
- The fact, that Switzerland has to eliminate these 30 year old rules has caused severe legal uncertainty. The proposed package is aimed at re-establishing certainty to the extent possible.
- Due to the Swiss political process it can be expected that the new reform measures will not come into effect before 2017 (Federal tax provision) and 2019 (Cantonal tax provisions).
- Implementation may be delayed depending on the speed the two Swiss Chambers will deal with the reform package and whether a referendum will be called making a public vote necessary.

Outlook/ political agenda



Q&A

Contacts

Dieter Wirth

Tax Partner

Birchstrasse 160

CH-8050 Zürich

Phone: +41 58 792 44 88

Mobile: +41 79 743 3886

Dieter.wirth@ch.pwc.com

This publication has been prepared for general guidance on matters of interest only, and does not constitute professional advice. You should not act upon the information contained in this publication without obtaining specific professional advice. No representation or warranty (express or implied) is given as to the accuracy or completeness of the information contained in this publication, and, to the extent permitted by law, PricewaterhouseCoopers AG, its members, employees and agents do not accept or assume any liability, responsibility or duty of care for any consequences of you or anyone else acting, or refraining to act, in reliance on the information contained in this publication or for any decision based on it.

© 2015 PwC. All rights reserved. In this document, “PwC” refers to PricewaterhouseCoopers AG which is a member firm of PricewaterhouseCoopers International Limited, each member firm of which is a separate legal entity.