The Tax Disputes and Litigation Review

Second Edition

Editor
Simon Whitehead

Law Business Research

The Tax Disputes and Litigation Review

This article was first published in The Tax Disputes and Litigation Review, 2nd edition (published inFebruary 2014 – editor Simon Whitehead).

The Tax Disputes and Litigation Review

Second Edition

Editor
Simon Whitehead

Law Business Research Ltd

THE LAW REVIEWS

THE MERGERS AND ACQUISITIONS REVIEW

THE RESTRUCTURING REVIEW

THE PRIVATE COMPETITION ENFORCEMENT REVIEW

THE DISPUTE RESOLUTION REVIEW

THE EMPLOYMENT LAW REVIEW

THE PUBLIC COMPETITION ENFORCEMENT REVIEW

THE BANKING REGULATION REVIEW

THE INTERNATIONAL ARBITRATION REVIEW

THE MERGER CONTROL REVIEW

THE TECHNOLOGY, MEDIA AND
TELECOMMUNICATIONS REVIEW

THE INWARD INVESTMENT AND
INTERNATIONAL TAXATION REVIEW

THE CORPORATE GOVERNANCE REVIEW

THE CORPORATE IMMIGRATION REVIEW

THE INTERNATIONAL INVESTIGATIONS REVIEW

THE PROJECTS AND CONSTRUCTION REVIEW

THE INTERNATIONAL CAPITAL MARKETS REVIEW

THE REAL ESTATE LAW REVIEW

THE PRIVATE EQUITY REVIEW

THE ENERGY REGULATION AND MARKETS REVIEW

THE INTELLECTUAL PROPERTY REVIEW

THE ASSET MANAGEMENT REVIEW

THE PRIVATE WEALTH AND PRIVATE CLIENT REVIEW

THE MINING LAW REVIEW

THE EXECUTIVE REMUNERATION REVIEW

THE ANTI-BRIBERY AND ANTI-CORRUPTION REVIEW

THE CARTELS AND LENIENCY REVIEW

THE TAX DISPUTES AND LITIGATION REVIEW

THE LIFE SCIENCES LAW REVIEW

THE INSURANCE AND REINSURANCE LAW REVIEW

THE GOVERNMENT PROCUREMENT REVIEW

THE DOMINANCE AND MONOPOLIES REVIEW

THE AVIATION LAW REVIEW

THE FOREIGN INVESTMENT REGULATION REVIEW

THE ASSET TRACING AND RECOVERY REVIEW

THE INTERNATIONAL INSOLVENCY REVIEW

THE OIL AND GAS LAW REVIEW

THE FRANCHISE LAW REVIEW

www.TheLawReviews.co.uk

PUBLISHER
Gideon Roberton

BUSINESS DEVELOPMENT MANAGERS
Adam Sargent, Nick Barette

MARKETING MANAGERS
Katherine Jablonowska, Thomas Lee, James Spearing, Felicity Bown

PUBLISHING ASSISTANT
Lucy Brewer

MARKETING ASSISTANT
Chloe Mclauchlan

EDITORIAL ASSISTANT
Eve Ryle-Hodges

HEAD OF PRODUCTION
Adam Myers

PRODUCTION EDITOR
Robbie Kelly

SUBEDITOR
Jonathan Allen

MANAGING DIRECTOR
Richard Davey

Published in the United Kingdom
by Law Business Research Ltd, London
87 Lancaster Road, London, W11 1QQ, UK

www.TheLawReviews.co.uk

ISBN 978-1-907606-94-6

Printed in Great Britain by
Encompass Print Solutions, Derbyshire
Tel: 0844 2480 112

ACKNOWLEDGEMENTS

The publisher acknowledges and thanks the following law firms for their learned assistance throughout the preparation of this book:

BAKER & MCKENZIE LLP

BOWMAN GILFILLAN

ECONOMIC LAWS PRACTICE

FLICK GOCKE SCHAUMBURG

GIDE LOYRETTE NOUEL

GREENWOODS & FREEHILLS

GTLAWYERS – GRISI E TANZILLI SOCIEDADE DE ADVOGADOS

HANNES SNELLMAN ATTORNEYS LTD

HERBERT SMITH FREEHILLS

HERGÜNER BILGEN ÖZEKE ATTORNEY PARTNERSHIP

HOCHE SOCIÉTÉ D'AVOCATS

JOSEPH HAGE AARONSON LLP

LOYENS & LOEFF

MAISTO E ASSOCIATI

MASON HAYES & CURRAN

MORAIS LEITÃO, GALVÃO TELES, SOARES DA SILVA & ASSOCIADOS, RL

MORRISON & FOERSTER LLP

NISHIMURA & ASAHI

OPF PARTNERS

PÉREZ BUSTAMANTE & PONCE, ABOGADOS

PWC LEGAL CIS B.V.

ROSCHIER ADVOKATBYRÅ

SCHELLENBERG WITTMER LTD

URÍA MENÉNDEZ

WARDYŃSKI & PARTNERS

CONTENTS

EDITOR'S PREFACE

The objective of this book is to provide tax professionals involved in disputes with revenue authorities in multiple jurisdictions with an outline of the principal issues arising in those jurisdictions. In this, the second edition, we have continued to concentrate on the key jurisdictions where disputes are likely to occur for multinational businesses.

Each chapter provides an overview of the procedural rules that govern tax appeals and highlights the pitfalls of which taxpayers need to be most aware. Aspects that are particularly relevant to multinationals, such as transfer pricing, are also considered. In particular, we have asked the authors to address an area where we have always found worrying and subtle variations in approach between courts in different jurisdictions, namely the differing ways in which double tax conventions can be interpreted and applied.

Perhaps it is merely a perception from a jurisdiction whose prime minister has publicly vilified a multinational for complying with the national tax laws, but tax avoidance seems to have become the new international evil. As such, this book provides an overview of each jurisdiction's anti-avoidance rules and any alternative mechanisms for resolving tax disputes, such as mediation, arbitration or restitution claims.

We have attempted to give readers a flavour of the tax litigation landscape in each jurisdiction. The authors have looked to the future and have summarised the policies and approaches of the revenue authorities regarding contentious matters, addressing important questions such as how long cases take and situations in which some form of settlement might be available.

We have been lucky to obtain contributions from the leading tax litigation practitioners in their jurisdictions. Many of the authors are members of the EU Tax Group, a collection of independent law firms, of which we are members, involved particularly in challenges to the compatibility of national tax laws with EU and EEA rights. We hope that you will find this book informative and useful.

Finally, I would like to acknowledge the hard work of my colleague Federico Cincotta in the editing and compilation of this book.

Simon Whitehead
Joseph Hage Aaronson LLP
London
February 2014

Chapter 23

SWITZERLAND

Harun Can and Pietro Sansonetti[1]

I INTRODUCTION

Implementing a new structure or transaction often incurs the risk of challenge by the tax authorities. In Switzerland, such risks are mostly addressed in a practical way by means of 'advance ruling requests' with the respective tax authorities. This has the advantage that the taxpayer, prior to a change of structure or prior to the completion of a transaction, can receive a written and binding answer from the tax authorities on the tax consequences of such structures or transactions within four to six weeks. Obtaining tax rulings in advance is therefore a very common way of reducing tax risks, and as a result disputes with the Swiss tax authorities arise to a lesser extent than in other OECD countries. Nevertheless, tax disputes do arise in Switzerland, whether regarding direct or indirect taxes.

To understand the Swiss tax dispute environment it is important to know how taxes are levied in Switzerland. The Swiss tax system mirrors Switzerland's federal structure. Switzerland has 26 cantons and approximately 2,600 municipalities. Based on Article 3 Federal Constitution, all cantons have the full right to levy taxes, except for those taxes exclusively assigned in the Constitution to the federal authorities. Consequently, Switzerland has a multilayered system of federal, cantonal and municipal taxes, in which tax disputes can arise on all levels and involve different authorities and courts.

At the federal level, income taxes for corporations and individuals are imposed pursuant to the Federal Income Tax Act.[2] Each person is a separate taxpayer. In Switzerland, no consolidated income taxation is available for corporate taxpayers. Under the federal withholding tax law, the Swiss Confederation exclusively levies a withholding

1 Harun Can and Pietro Sansonetti are partners at Schellenberg Wittmer Ltd. The authors would like to thank Charles Goumaz at Schellenberg Wittmer Ltd for his valuable contribution to this article.

2 Loi fédérale du 14 décembre 1990 sur l'impôt fédéral direct, RS 642.11.

tax on defined passive income. This tax mainly affects dividends and certain types of interest payments. The federal stamp tax law foresees three types of stamp taxes: a stamp tax on the issuing or increase of Swiss shares; a turnover stamp tax on the purchase, sale or exchange of certain Swiss or foreign securities traded by registered securities dealers, whether acting on their own account or as intermediaries; and a stamp tax on insurance premiums. The federal VAT is a general use and consumption tax.

At the cantonal level, each canton has its own income tax act and basically is given wide authority to design its own tax system. The cantonal tax systems include in particular income and equity taxes, gift and inheritance taxes, and real estate capital gains and real estate transfer taxes. However, to harmonise the cantonal (and municipal) direct taxes, the Confederation has enacted a harmonisation statute, the Federal Tax Harmonisation Act,[3] which contains certain provisions according to which cantons have to adapt their own direct tax acts. However, the cantons are still free to set their own tax rates.

II COMMENCING DISPUTES

In the field of individual income taxes and corporate income taxes, as well as in the field of real estate capital gains tax and real estate transfer tax, disputes usually arise as a result of an assessment decision by the responsible tax commissioner regarding filed income tax returns, be they based on a full audit of the taxpayer or on a simple review of the tax return. Income tax declarations in Switzerland are always reviewed by a tax commissioner, who issues a formal decision after assessment. This is called a mixed assessment procedure. In the event that the taxpayer does not agree with such an assessment, he or she has the right to appeal against it to the assessment authority within 30 days under Article 132 et seq. of the Federal Income Tax Act and the corresponding cantonal provisions. If the appeal is directed against an assessment that is duly substantiated, the appeal may, with the consent of the appellant and the other petitioners, if any, be referred as an appeal to the cantonal tax appeals court based on Article 132(2) of the Federal Income Tax Act and the corresponding cantonal provisions.

As partnerships are treated as being transparent, no special treatment for partnerships exists.

In the field of VAT, withholding tax and stamp taxes, disputes usually arise as a result of a tax audit. Such indirect taxes are self-assessment taxes, for which the tax commissioner does not issue a tax assessment decision. Again, if the taxpayer does not agree to a tax audit decision, he or she can appeal within 30 days against such a decision to the assessment authority under Article 83 of the Federal VAT Act, Article 42 of the Federal Withholding Tax Act and Article 39 of the Federal Stamp Duty Act. The appeal will be continued, despite its withdrawal, if there are indications that the contested decision does not comply with the applicable provisions of the law. If the appeal is raised against a properly substantiated decision of the Federal Tax Authority regarding VAT, on application or with the consent of the objecting party the appeal must be forwarded

3 Loi fédérale du 14 décembre 1990 sur l'harmonisation des impôts directs des cantons et des communes, RS 642.14.

as an appeal to the Federal Administrative Court based on Article 83(4) of the Federal VAT Act. Usually each instance takes one to one-and-a-half years to make a decision, meaning that such proceedings can take four to five years until they are finally decided by the Federal Supreme Court.

The following points are often raised in the context of tax assessments and tax decisions resulting from, for example, a tax audit.

i Amendments to tax returns after the filing

In principle, taxpayers can correct their tax returns after the filing, as long as no final tax assessment decision has been issued by a tax commissioner. This includes necessary balance sheet corrections, but in most cases not balance sheet amendments. Income tax assessments are usually issued within one to three years of the filing of the tax return.

ii Discretionary assessment in the event that no tax return is filed in time

If the taxpayer has, notwithstanding a warning notice, failed to file the tax return before the due date, or if the tax factors cannot be determined beyond doubt due to the absence of reliable documentation, the tax commissioner issues a discretionary assessment, taking into account empirical figures, changes in wealth and the living expenses of the taxpayer.

iii Alternative methods for reviewing decisions by the tax authorities

If, during an assessment or an audit, the taxpayer was not aware of materially incorrect facts, he or she can claim that the authorities have made a manifest error of assessment based on such facts. Such a claim is made with a petition for revision. A petition for revision by the taxpayer is only admitted if significant facts or decisive proof are discovered; or if the assessing or deciding authority failed to consider significant facts or decisive evidentiary proof that was or should have been known to it, if it otherwise violated important procedural principles, or if a crime or offence influenced the assessment or decision. Revision, however, is precluded if the reason for revision could have been asserted earlier in the ordinary proceeding (see Article 147 et seq. of the Federal Income Tax Act and the corresponding cantonal provisions).

In principle, the taxpayer can also appeal against the behaviour of an official, but this is rarely the case. Such an appeal is first decided by the tax authorities themselves, and can then be appealed against at the next instance.

iv Relevant time periods for commencing a dispute

In most cases, the taxpayer has 30 days to appeal against an assessment or decision of the tax authorities or a previous instance starting from the day following the date of notification of the assessment or decision. A petition for revision must be filed within 90 days after recovery of the revision ground, but not later than 10 years after notification of the assessment or decision. The first instance usually takes from one to one-and-a-half years to issue a decision.

Disclosure regime

On 1 January 2010 the Federal Act on the Simplification of Additional Tax Assessments in Succession Matters and the introduction of a tax amnesty for voluntary disclosures

came into force in Switzerland for the purposes of federal income tax and harmonised cantonal taxes. The purpose of this Act, on the basis of which the Federal Income Tax Act and the cantonal tax acts were modified, was to encourage taxpayers (individuals and businesses) to report hitherto undisclosed elements of wealth, income, capital or profits.

The waiver of penalties in exchange for a voluntary disclosure is a type of individual tax amnesty in the sense that it allows a taxpayer to choose the time of its application. However, since a taxpayer can qualify only once in its lifetime, it is not a 'general amnesty', requiring a taxpayer to act within the deadlines set by the amnesty law, as was the case with the 1969 amnesty. For both the simplified additional tax assessments in succession cases and voluntary disclosures, there is no criminal prosecution and hence no penalties. However, additional tax assessments and default interest will remain due, although for different periods.

The difference in treatment between the simplified additional tax assessments in succession cases (recovery of the three years prior to death) and voluntary disclosure (recovery of the 10 years prior to declaration), however, may deter some taxpayers, particularly the elderly, from regularising their tax situation, leaving their heirs with the task of doing so.

On 1 January 2010 a fully revised Federal VAT Act entered into force. This VAT Act includes a disclosure provision on the basis of which a taxpayer reporting him- or herself for an offence under the VAT Act before it comes to the attention of the competent authority will not be prosecuted, provided he or she assists the authority in a reasonable manner in establishing the VAT payable or refundable, and makes a serious effort to pay the VAT.

Release of information from the tax authorities

On the basis of Article 29(2) of the Federal Constitution, all taxpayers, within certain time and factual limits, have the right to see their tax files, which are kept by the tax authorities. Access to the files of other persons is possible in a few cantons only, and is limited to the taxable factors.

III THE COURTS AND TRIBUNALS

In the field of individual income tax and corporate income tax, appeals against disputed assessments can first be made to the same authority that issued the assessment (i.e., the cantonal tax authorities). In most cases, a special department of the relevant cantonal tax authority issues a first decision in collaboration with the responsible tax commissioner. In the event that the authority makes a decision in line with its assessment decision, a further appeal can be made to the first instance administrative court for the purpose of federal income tax, cantonal and municipal income and equity taxes, real estate capital gains tax and real estate transfer tax. Decisions issued by the specialised, independent and impartial judges of the first instance administrative court are subject to appeal at the cantonal second instance administrative court as final cantonal instance.

In addition, in the event that the final cantonal court decision does not satisfy the parties, an appeal to the Federal Supreme Court in Lausanne might be possible.

In certain matters, an appeal to the European Court of Human Rights can also be considered by the taxpayer. In the case of *JB v. Switzerland*,[4] the European Court of Human Rights confirmed a Swiss taxpayer's right to remain silent and his or her privilege against self-incrimination, which are generally recognised international standards that, according to Article 6(1) of the European Human Rights Convention, are central to a fair procedure. JB was requested on several occasions to submit documents he had concerning companies in which he had made investments, and was fined four times for not complying with these requests. The documents might have resulted in JB being charged with the offence of tax evasion.

In the field of VAT, withholding tax and stamp duties, appeals against disputed federal authority decisions can first be made to the same authority. In the event that the VAT authorities make a decision in line with the assessment decision, a further appeal can be made to the Federal Administrative Court in St Gallen. Furthermore, in the event that the Federal Administrative Court decision does not satisfy the parties, an appeal to the Federal Supreme Court in Lausanne might be possible.

Tax disputes are resolved in all instances. However, experience shows that the cases brought by taxpayers to the Federal Supreme Court in recent years were not very frequently successful at this level.

IV PENALTIES AND REMEDIES

In Switzerland a distinction is made between the negligent failure to carry out procedural duties, tax evasion and tax fraud.

Negligent failure to carry out procedural duties (e.g., where the taxpayer fails to file a tax declaration or does not comply with a certification or informational duty) is sanctioned with a penalty. For income and equity taxes the penalty is limited to 10,000 Swiss francs. For the other taxes, different limits exist. Negligent failure to carry out procedural duties is dealt with by the tax authorities. The decision of the tax authorities can be contested with an appeal.

Tax evasion (i.e., where taxpayer causes an assessment to be wrongfully omitted or a final assessment to be incomplete) is sanctioned with a penalty that is up to three times the sum evaded (up to five times the sum in the case of VAT). Tax evasion is dealt with by the tax authorities rather than criminal prosecutors. This means that such alleged evasion can be contested in the same way that an appeal can be made against an income tax assessment.

The penalty for a complete evasion of income taxes is, as a rule, equal to the amount of evaded taxes. In the case of simple negligence, the penalty may be reduced to one-third, whereas in cases of serious fault, the fine may be tripled (Article 175(2) of the Federal Income Tax Act and the corresponding cantonal tax provisions). The penalty for an attempted evasion of income taxes is two-thirds of the amount that would have been determined in the case of a completed tax evasion (Article 176(2) of the Federal Income

4 No. 31827/96.

Tax Act and the corresponding cantonal tax provisions). Incitement, aiding and abetting and collaboration are punished, too.

Tax fraud is a qualified form of tax evasion and requires, for direct taxes, the use of falsified documents, whereas for indirect taxes, qualified tax swindling, which can include the use of falsified documents, is sufficient. Committing tax fraud can lead to a fine and imprisonment, as well as an entry in the criminal record of a person. Therefore, tax fraud is subject to criminal prosecution.

A completed fraud regarding income taxes can be punished with imprisonment or a fine of up to 30,000 Swiss francs. The punishment for tax evasion is not included (Article 186(2) with Article 175 of the Federal Income Tax Act and the corresponding cantonal tax provisions).

V TAX CLAIMS

i Recovering overpaid tax

As regards income tax, overpaid taxes are refunded or set off against other tax liabilities due to the respective authorities upon request, or in the event that the taxpayer is finally assessed for the relevant income tax period and a too-high portion of provisional taxes has been paid. After a final assessment, a refund can be claimed, or in certain cases a set-off against another tax period can be requested. The Swiss authorities usually do not have to be reminded in this regard, and we are not aware of any cases where a refund of overpaid taxes has been disputed.

As regards VAT, a too-high declaration of output VAT might be reclaimed, but this depends on the case, as VAT that is wrongly stated in an invoice to a third party can only be reclaimed if new invoices are issued and acknowledged by the customer.

ii Challenging administrative decisions

It is possible to challenge an administrative decision of the tax authorities on grounds such as it being contrary to legitimate expectation or to constitutional authority. Under very specific conditions, a right to equal treatment may even be claimed.

iii Claimants

In principle, only the taxpayer itself can make an appeal. Depending on the kind of tax, the instance and the specified circumstances, appeals may also be lodged by a community, by another tax authority (e.g., in cases of inter-cantonal double taxation), and in certain cases even by a third private person that succeeds in demonstrating a justified interest in the outcome of the case.

As regards VAT, only the VAT-liable person that lodged the VAT return can make a claim against the VAT authorities. Based on civil law, a customer that was charged with an unlawful amount of VAT by the VAT-liable person has to claim such VAT from the supplier following the civil law procedures. For the purpose of withholding tax, the liable person is not the same as the one that, under domestic or treaty law, may have a right to a partial or full refund of the withholding tax. Regarding liability to pay withholding tax, the considerations outlined above apply, whereas any person applying for a refund upon receipt of a decision can make a claim against the authorities.

VI COSTS

In the event that the taxpayer succeeds in litigation, part of the cost may be recovered from the state, but in most cases approximately 30 per cent to 50 per cent of the costs are not reimbursed even if the taxpayer succeeds.

As regards the costs of the tax authorities, in most cases no such costs are charged to the taxpayer in dispute with the tax authorities (e.g., those appeals that are dealt with by the authority issuing the assessment or decision). However, the court charges costs in the event that the taxpayer does not succeed, or if his or her culpable behaviour caused or significantly delayed or impeded the procedure.

The costs of special investigative measures (e.g., examination of books or expert opinions) can, according to Article 183(4) of the Federal Income Tax Act and the corresponding cantonal provisions, be charged to the taxpayer, or another party who is involved in a tax evasion or tax fraud procedure and who is punished for a tax offence. These costs can also be charged to him or her when the investigation is discontinued if his or her culpable behaviour caused, or significantly delayed or impeded, the criminal investigation.

VII ALTERNATIVE DISPUTE RESOLUTION

The relationship between the various Swiss tax authorities and the taxpayers is usually good, and binding agreements (i.e., tax rulings between the tax authorities and the taxpayer) can be obtained on most questions regarding Swiss tax law. Therefore, it is very common to contact the tax authorities before the implementation of a new structure, or the signing or closing of a transaction, and to have the tax consequences of the structure or transaction confirmed in a written ruling.

Advance rulings legally bind the authorities provided all of the following conditions are met:

a the facts precisely described in the ruling are also implemented;
b the authorities signing the ruling are competent to issue the ruling;
c the tax law on which the ruling was based has not changed;
d the taxpayer has, on the basis of the tax ruling, taken measures that cannot be changed without incurring a financial loss; and
e it was not clear to the taxpayer or the tax adviser that the ruling answer is against clear provisions in the relevant tax act.

Tax rulings are in principle valid for an indefinite period, and only come to an end in the case of (informal) termination by the taxpayer (e.g., because of a change of facts) or the formal termination by the tax authority (e.g., because of a change in practice or a change of law). The termination by the tax authority is in most cases granted with a grandfathering period.

VIII ANTI-AVOIDANCE

Switzerland does not have any general anti-avoidance legislation. An anti-avoidance provision does exist, but only for the purpose of the refund of Swiss withholding tax.

Under Swiss tax law, fraudulent tax evasion (e.g., evading the full assessment of a tax that is legally due) is a criminal offence.

In contrast, and on the basis of various court cases,[5] a general anti-avoidance rule, in principle applicable to all Swiss taxes, classes tax avoidance as:

a an artificial arrangement or an artificial series of arrangements that have been put into place for the essential purpose of avoiding taxation;
b there are no valid business reason for such arrangements; and
c the arrangements lead to a substantial tax saving.

If the tax authorities come to the conclusion that the requirements of tax avoidance are all present, they have the right to treat the arrangements made by the taxpayer for tax purposes based on their economic substance.

IX DOUBLE TAXATION TREATIES

In a recent case of a cross-border transaction between related parties, the Federal Supreme Court ruled that, in the event that a Swiss entity is finally assessed for a tax period, a secondary adjustment (i.e., an additional payment of the Swiss entity due to a primary adjustment in the state of the contracting party) relating to this tax period is to be characterised as a hidden dividend distribution made by the Swiss entity to the foreign recipient of the payment and triggering Swiss withholding tax at the ordinary rate of 35 per cent.[6] Currently, the only way to obtain a withholding tax-free secondary adjustment is to refer to a mutual agreement procedure. In a mutual agreement procedure, the Federal Tax Authority may agree not to levy the withholding tax. Payments between related parties other than from a subsidiary to its foreign parent may constitute a tax risk.

Aside from a provision on the exchange of information in accordance with the OECD standard, in many of its recently revised treaties, Switzerland has also included an arbitration clause in accordance with the OECD standard.

X AREAS OF FOCUS

In recent years, the Swiss tax authorities have more frequently questioned tax-planning structures that involve Swiss quoted companies and that try to reduce their tax rate by using offshore tax structures.

In a 2006 case, the Federal Supreme Court disregarded for the purpose of taxes an offshore company.[7] The offshore company was managed from the office of a Swiss

5 For example, see the decision of the Federal Supreme Court in Case 138 II 239.

6 See Federal Supreme Court Case 110 Ib 127.

7 See Federal Supreme Court decision of 30 January 2006, reference 2A.145/2005.

company that was held by the same shareholder. Not only did the employees work for both companies, but the same IT was also used to keep books, which were in Swiss francs. In addition, the bank accounts were cross-pledged by both companies.

Because of the very close tie between the offshore and the Swiss company, the Federal Supreme Court came to the conclusion that the structure was a case of tax evasion and added the offshore company's taxable income to the Swiss company. This was the first time that the Federal Supreme Court disregarded a company and allocated the taxable factors not to the shareholder, but to another company.

This decision has been strongly criticised, as it was not clear whether the Federal Supreme Court introduced a *de facto* controlled foreign corporation regime without any legal basis. It was further criticised that the Federal Supreme Court based its decision on the general anti-avoidance rule, which should only be applied as the *ultima ratio*.

XI OUTLOOK AND CONCLUSIONS

A revision of the tax law as regards criminal offences is currently being prepared, in particular with the aim of updating and standardising the existing provisions. Furthermore, tax authority investigations are more frequently being challenged on the issue of the guarantee of human rights in the area of Swiss tax law.

Recently there has been a trend among the bigger cantons in Switzerland to open more criminal procedures against taxpayers; this had previously occurred to a lesser extent.

For example, in one case, a Swiss branch of a German company was threatened with a tax penalty of between 1.1 million and 10 million Swiss francs. The German company was part of a listed group in the course of a worldwide business reorganisation, and had also contributed all the assets and liabilities of its Swiss branch to a fully owned Swiss subsidiary. As a result, the transferred goodwill was recorded in the books of the receiving Swiss subsidiary at fair market value. The tax return of the Swiss branch was prepared by the local adviser of the branch, who was not involved in the bookkeeping or auditing of the Swiss subsidiary. The branch accounts that were enclosed with the income tax return did not show the realisation of profit resulting from the contribution; nor was such profit declared in the income tax return form of the branch itself – a clear mistake.

As a result of a subsequent tax audit performed by the tax authorities, the transferred goodwill was added to the taxable profit of the branch and was made subject to federal, cantonal and municipal income taxes. Six months later, the same tax authorities announced the initiation of an administrative penalty procedure against the branch because of suspicions of an attempt to evade tax according to Article 175 et seq. of the Federal Income Tax Act and the corresponding cantonal tax provision.

An attempt to evade tax can be punished with a penalty that, depending on the circumstances, can range from two-ninths to double the potentially evaded tax. In this case the federal, cantonal and municipal income tax was around 5 million francs, suggesting a penalty range of between 1.1 million and 10 million Swiss francs (as mentioned above).

This case clearly shows that the Swiss tax authorities have become less reluctant to initiate tax evasion or tax fraud proceedings against taxpayers. Ten years ago, such a case would not have led to a penalty proceeding. As the Swiss tax authorities continue to hire special teams for penalty proceedings more frequently, it can be expected that taxpayers will have to defend themselves more and more vigorously against such penalty proceedings.

Appendix 1

ABOUT THE AUTHORS

HARUN CAN

Schellenberg Wittmer Ltd

Harun Can is a partner in Schellenberg Wittmer's taxation group in Zurich. He specialises in Swiss and international tax planning for multinational corporations and private equity funds, and has special knowledge regarding the relocation of their managers to Switzerland. In addition, Harun Can has broad experience in real estate transactions and special expertise in value added tax law, and is the founder and chair of the 'mwst netzwerk zh', a network of Swiss VAT specialists.

Harun Can studied law at the University of St Gallen, graduating in 1994 (*lic iur* HSG). He was admitted to the Bar in 1997 and qualified as a Swiss certified tax expert in 2000. He obtained a Master of Laws at the London School of Economics (LLM tax 2001), and in 2005 became a Swiss VAT expert.

Harun Can publishes on a range of tax issues and is active in various think tanks. He lectures regularly at seminars sponsored by Swiss tax and law societies. He is fluent in English, French and German.

PIETRO SANSONETTI

Schellenberg Wittmer Ltd

Pietro Sansonetti is a partner in Schellenberg Wittmer's taxation group in Geneva. He specialises in domestic and international corporate tax matters, with a focus on complex situations requiring discussions with tax authorities. He also advises individuals – especially in partnerships – and private clients on tax issues and assisting clients in enforcement matters, including international exchange of information.

Pietro Sansonetti is the head of the Geneva taxation group at Schellenberg Wittmer, and is currently a member of the firm's management committee.

Pietro Sansonetti was admitted to the Bar in Switzerland in 1985 after graduating from the University of Geneva, where he obtained a law degree in 1982. He became a Swiss certified tax expert in 1990 while working as a tax manager with Arthur Andersen.

Pietro Sansonetti was the director of tax affairs (chief tax officer) at the Geneva Tax Authority before joining Schellenberg Wittmer as a partner in 1999. In addition, he was the chair of the Swiss examination commission for tax experts until 2006. He regularly publishes on a range of tax and legal issues, and is active in various think tanks in the field of tax policy, legislation and practice.

Pietro Sansonetti lectures regularly at international and Swiss seminars sponsored by the IFA, and various Swiss tax and law societies. He is a member of the faculty of the Executive Master of Advanced Studies in International Taxation at the University of Neuchâtel. He is fluent in English, French, German and Italian.

SCHELLENBERG WITTMER LTD

Löwenstrasse 19
PO Box 1876
8021 Zurich
Switzerland
Tel: +41 44 215 5252
Fax: +41 44 215 5200
harun.can@swlegal.ch

15bis, rue des Alpes
PO Box 2088
1211 Geneva 1
Switzerland
Tel: +41 22 707 8000
Fax: +41 22 707 8001
pietro.sansonetti@swlegal.ch

www.swlegal.ch