Transfer Pricing

Country Summary

Switzerland

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1. Introduction

Switcherland follows the OECD TP Guidelines without however mentioning them directly in its legislation.

2. Laws & Regulations

a) References to OECD/EU/Local Rules

There are no specific transfer pricing regulations. However, legal support for adjusting profits of a taxpayer is derived from the arm's length principle in Article 58 of the Federal Law on Direct Federal Tax and Article 24 of the Federal Law on the Harmonization of the Cantonal and Communal Taxes on a cantonal level. Furthermore, the Swiss Federal Tax Administration (SFTA) instructed the cantonal tax administrations in Circular Letter issued on 17 September 1997 that when taxing multinational enterprises, they should take into consideration the OECD Transfer Pricing Guidelines. Switzerland has agreed to apply the key aspects of the OECD Transfer Pricing Guidelines.

There are a number of circulars and circular letters that imply transfer pricing regulations, such as:

- Circular Letter No. 6 issued in June 1997, which regards hidden equity;
- Circular letter No.8 issued in December 2001, which regards the international profit allocation of principal companies;
- Circular Letter No. 4 issued in March 2004, which states that the remuneration for services performed by service companies should respect the arm's length principle by selecting an appropriate transfer pricing method and an arm's length margin of mark up.

On yearly basis, SFTA publishes a Circular letter regarding the interest rates for inter-company loans in Swiss Francs and a Circular letter regarding the interest rates for inter-company loans in foreign currencies. The interest rates vary per currency.

A draft legislation regarding corporate tax reform is in its final stages of parliamentary works. It is expected that the new legislation will be enacted in 2019/2020.

Implementation of BEPS-related documentation requirements

Switzerland implemented the Country-by-country reporting obligation in its legislation. The CbCR law entered into force on 1December 2017.

b) Definition of Related Party

There are no formal related party disclosure requirements. In general, the OECD definition regarding associated enterprise is applied. Therefore, a related party is considered to be a direct or indirect shareholder of (a) the Swiss company, (b) any other group company or (c) a third party fronting for them.

The Swiss Federal Supreme Court has in his jurisprudence clearly defined this expression. An entity is considered as a related party if primarily a commercial or secondarily a personal close relationship exists between the two entities. Therefore, a direct or indirect participation in the management, control or capital is not required. The crucial question is if the tested transaction was conducted only because of the associated relationship or not.

c) Nature of Transfer Pricing Documentation

In Swiss tax legislation, there are no particular references to TP. The arm's-length concept in Article 58 of the Federal Direct Tax Act on a federal level (14 December 1990), as well as Article 24 of the Federal Law on the Harmonization of Taxes on a cantonal and communal level, provide legal foundation for adjusting a taxpayer's taxable profits (14 December 1990).

In addition, on March 4, 1997, the SFTA published a circular letter urging cantonal tax administrations to examine cross-border intercompany transactions in accordance with the OECD Guidelines and the arm's-length principle.

The word "related party" is not defined in Swiss domestic law or regulations. According to the federal court's jurisprudence, two entities or individuals are considered connected if they have a business or close personal relationship. There is no requirement for direct or indirect participation in management, control, or capital. The most important consideration is whether the transaction was carried out only because of the close friendship or not.[1]

d) Tax Havens & Blacklists

On December 5th, 2017, Switzerland was added to EU's list of Tax Havens, because it enticed international investors by enabling firms and rich people to pay a low, lump-sum tax on money held in Swiss banks.

Swiss voters approved the Federal Act on Tax Reform and AVS Financing in a referendum on May 19th of this year (TRAF). This legislation made significant changes to the Swiss tax system by abolishing some favourable tax schemes and replaced them with new international-standard regulations. The Swiss are now in compliance with EU expectations thanks to this tax reform, which will take effect in 2020.[2]

e) Advance Pricing Agreement (APA)

Advance Pricing Agreements can be concluded with the Swiss tax authorities. Even though there are no specific formal procedures, tax rulings are a common practice in Switzerland. Also, SFTA participates in bilateral and multilateral APAs in accordance with Mutual Agreement provision in the applicable double tax treaty. APA is generally granted for 3to 7years but it may be subject to different negotiation.

f) Audit Practice

The risk that transfer pricing issues are scrutinized during an audit has increased (medium level of audit risk). Transfers of intangibles, services, intercompany financing or business restructuring are usually more scrutinized.

There is no specific TP audit in Switzerland so far. Transfer pricing can potentially be audited during the normal tax audit procedure.

The cantonal tax authorities are now more active regarding transfer pricing during a tax audit, in particular towards foreign companies showing a balance sheet loss. The FTA is also becoming more active toward foreign companies, in particular regarding WHT related to deemed dividend and Swiss value-added tax (VAT), when applicable.

3. Transfer Pricing Documentation

a) Level of Documentation

Swiss tax law does not have specific requirement in terms of documentation with the exception of the Country-by-country reporting obligation (please refer hereafter to the paragraph concerning the Country-by-country reporting obligation).

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[1] ey-worldwide-transfer-pricing-guide-10-september-2020 (2).pdf, p. 611.

[2] Why Switzerland is no longer on the EU's black list of tax havens (thelocal.ch)

The taxpayer must submit documentation (most often within 30 days) upon request from the tax authorities as part of the normal tax audit. According to article 126 FDTA and article 42 FHDT, the taxpayer should provide all necessary documents for properly assessing the taxable income.

In case of intercompany transactions, the taxpayer must be able to demonstrate that transfer prices applied are based on sound economic and commercial reasoning. There is no specific formal requirement but the taxpayer should prepare appropriate documentation depending on its structure and/or activities.

If the tax authorities do not request for further information, the taxpayer has no obligation to maintain TP documentation, although it is now highly recommended to prepare adequate documentation.

There is no formal requirement in terms of TP documentation in Switzerland then the documentation may be limited. The only requirement is that the documentation provided should respond sufficiently to the tax authorities' request. The Swiss practice is to refer to the OECD guidelines on Transfer Pricing and thus it is expected that intercompany transactions adhere to the arm's length principle.

Country-by-country reporting obligation

Switzerland signed the Multilateral Competent Authority Agreement on the Exchange of Country-by-Country (CbC) Reports and adopted the CbC reporting standards in its domestic legislation. The law and the ordinance regarding the CbC reporting entered into force as of 1 December 2017.

The obligation to prepare and file a CbC report will become mandatory for the first time from the tax year 2018 onwards. The first exchange between Switzerland and its partner states or countries that have signed the multilateral competent authority agreement (MCAA) will be mandatory from 2020 onwards.

To enable Swiss-based and only Swiss-based companies to meet with the generally expected earlier exchange of CbCR from the tax year 2016 onwards, the Ordinance and in particular the law foresees voluntary submission of CbCR for tax periods before 2018. These reports can be transmitted by the Federal Tax Administration (FTA) based on the MCAA on the Exchange of CbCR to partner states from 2018 onwards. The FTA published on its website the procedure to follow.

Content of Transfer Pricing documentation

There is no specific requirement in terms of content except for the fact that the taxpayer should provide appropriate documentation to support positions taken. The notion of "appropriate documentation" is not defined and varies on a case-by-case appreciation.

b) Industry Analysis

By identifying value drivers for the relevant industry, a first indication of the level of profitability common in the industry is being given.

c) Company Analysis

A description of the management structure of the local entity, a local organisation chart, and a description of the individuals to whom local management reports and the country(ies) in which such individuals maintain their principal offices.

A detailed description of the business and business strategy pursued by the local entity including an indication whether the local entity has been involved in or affected by business restructurings or intangibles transfers in the present or immediately past year and an explanation of those aspects of such transactions affecting the local entity.

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d) Functional Analysis

In conducting a functional analysis, an assessment is made of the significant activities and responsibilities that are performed by the related parties relevant to the Intercompany Transactions under review, the tangible and intangible assets that are employed and the risks that are borne in undertaking the business activities. Such an assessment is consistent with the recommendations that have been made in the OECD Guidelines at paragraph 1.51.

e) Choice of Transfer Pricing Method

The SFTA adheres to the OECD Guidelines for transfer pricing, and prefers the transactional methods over the profit-based methods. Circular Letter 4/2004 mentions that mark ups of service companies must be determined in accordance with the arm's length principle, on the basis of comparable uncontrolled transactions and with appropriate ranges of mark ups for any individual case. The Circular Letter also implicitly states that the cost-plus method is the most appropriate method for service companies to price their services. However, the cost-plus method is only exceptionally the appropriate method for financial services or management functions. A company that wishes to lower the mark up applied under the cost plus method for determining its taxable income has the burden to prove that the mark up is too high.

However, where facts and circumstances indicate, other methods of arriving at a profit on the services may be appropriate.

f) Economic Analysis – Benchmark Study

Swiss comparables are preferred but limited; therefore Pan-European benchmark searches are generally accepted by the Swiss tax authorities. The Amadeus database is generally applied.

g) Inter-company (IC) Legal Agreement

Although an Inter-company legal agreement formalizes the business and financial relationship between group entities, the legal agreements have a lower ranking since the OECD 2017 Guidelines made the ''conduct of parties'' the prevailing concept.

h) Financial Statements

Operations that are reflected in the taxpayer's statutory accounts and are compatible with Swiss business law are generally binding for Swiss tax reasons. As a result, the statutory accounts serve as the foundation for calculating taxable profit and, as a result, for tax assessment. Accounting follows taxation (the so-called "Massgeblichkeitsprinzip," which states that statutory accounts are determinative for tax reasons). Intercompany transactions that appear in the financial statements are so taxed as well.

However, where (i) charges are not commercially justified; (ii) income is not properly recorded as such; (iii) a systematic tax realization occurs (e.g. transfer of assets or activities abroad); or (iv) related parties do not deal with each other at arm's length conditions, the tax administration may take corrective measures and depart from the financial statements. Income tax adjustments, deemed dividend distributions, or presumed capital contributions may result as a result of this. Furthermore, if a substance-over-form investigation finds that the structure adopted does not match to economic reality, the tax authorities are entitled to alter taxable profits. They may thus ignore the legal form chosen by the parties for a particular transaction. The so-called "hidden profit distribution" concept has been used to build the required legislative framework that allows tax authorities to adjust taxable gains (or disguised profit distribution).[3]

[3] Document - Switzerland - Transfer Pricing & Intra-Group Financing - 2. Defining an Intra-Group Financing Policy - Tax Research Platform - IBFD, para 2.

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i) Production Process for TP Relevant Returns, Documents, Forms and Financials

In the chart below, the existence of the filing requirements with the details of which format is used, the latest filing date, notification requirement and its deadline, thresholds to be applied in case it exists, and the required languages are demonstrated. This information can be seen respectively for CIT, master file, local file, CbCR, local forms, annual accounts and segmented P&L documentations.

	Prepare or File?	**Format**	**Deadline**	**Notification Deadline***	**Threshold* (Yes/No)**	**Local Language (Yes/No)*(If "No", it can be filed in English)**
Corporate Income Tax	File	Swiss GAAP	June, 30th.	No	No	No
Master File	Prepare	OECD Guidelines	Upon request in APA and upon tax audit situation.	No	No	No
Local File	Prepare	OECD Guidelines	Upon request in APA and upon tax audit situation.	No	No	No
CbCR	File	OECD Guidelines	December, 31st.	Yes	Yes	No
Local form	N/A	N/A	N/A	N/A	N/A	N/A
Annual Accounts	File	Swiss GAAP	March, 31st.	No	No	No
Segmented P&L	N/A	N/A	N/A	N/A	N/A	N/A

* Switzerland has signed the MCAA agreement for the filing of CBCR

* Switzerland does not request as much and detailed information from smaller and less complex enterprises (SMEs included) than it does from large and complex enterprises.

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j) Mandatory Language

Documentation should be drafted in the official language of the cantonal authorities where the company is established. The official languages of Switzerland are: German, French, Romansh or Italian. English documentation may also be accepted, but it is expected that the documents have to be translated into the relevant official language, upon request.

k) Notification Requirement

Article 10(1) of the CbCR Act requires the reporting entity (and alone the reporting entity) to notify the FTA of its capacity as an ultimate parent entity or a surrogate parent entity, its trade name and seat, its unique business identification number (UID), and the date of its inception. Article 10(2) of the CbCR Act allows the Federal Council to mandate that each resident constituent entity also provide a notification. This notification requirement, on the other hand, will only be enacted if it is deemed required at a later date. There is no necessity for constituent entities to notify the CbCR Act once it becomes effective.

Article 10(4) of the CbCR Act requires that the notification be submitted no later than 90 days following the end of the reporting financial year. There is no necessity to renew this notification on an annual basis, thus a one-time notification is sufficient. If the reporting entity loses its ability to report, it must deregister with the FTA (CbCR Act, item 10(5)).[4]

l) Record Keeping

There are no specific transfer pricing regulations or rules dealing with record keeping. There are general and mandatory record keeping rules in the statutory accounting regulations, though.

m) Penalties and Interest Charges

There are no specific transfer pricing penalties, but general penalty rules apply. However, penalties are only imposed in case of fraud or negligence. Interest charges for late payment are due in case of adjustments.

As a non-arm's length transaction can be considered as a hidden distribution of profits, a transfer pricing adjustment can result in the payment of Swiss withholding tax of 35% or a gross-up to 54% (if not borne by the beneficiary). Nevertheless, the company may request for a total or partial refund based on the applicable double taxation agreement between Switzerland and the concerned foreign state.

[4] Document - Switzerland - Transfer Pricing - 13. Documentation Requirements - Tax Research Platform - IBFD, para. 13.2.4.