Schweizerische Eidgenossenschaft
Confédération suisse
Confederazione Svizzera
Confederaziun svizra

Swiss Confederation

Der Bundesrat
Le Conseil fédéral
Il Consiglio federale
The Federal Council

# Press background information

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# Withholding tax reform

### General

Withholding tax is levied primarily on interest and income from participation rights and collective investment schemes. With the current system, withholding tax is collected via companies (which pay dividends), Swiss banks (which pay interest), savings banks, corporations, cooperatives and providers of collective investment schemes. These withhold the corresponding tax amount from the dividends, interest and other taxable items they pay out and transfer it to the tax authorities. Swiss recipients of income are entitled to claim a refund of the withholding tax deducted in this way. Recipients resident abroad are not entitled to claim a refund in many cases or can claim only a partial refund. Generating average annual revenue of approximately CHF 5 billion, withholding tax is an important source of receipts for the Confederation.

### Stimulating the capital market and improving the safeguard purpose

It is currently necessary to reform withholding tax at the moment for the following reasons:

- Underdeveloped Swiss capital market: The capital market is the financial market for raising medium- and long-term capital and enables companies, households and the state to finance investments and other expenditure. The market for equity capital (e.g. equities of a company limited by shares) is distinct from that for debt capital (e.g. bonds). By international standards, Switzerland is relatively unappealing for the issuance of debt capital, which has unfavourable consequences for the country as a financial centre and business location. Given that withholding tax is currently collected irrespective of who the beneficiary of the taxable item is, institutional investors such as pension funds also have to pay the tax when they invest in Swiss securities. Even though investors are entitled to claim a withholding tax refund, Swiss securities are unappealing because of the associated administrative burden.

- Avoidance of withholding tax: Companies often issue their bonds abroad in order to avoid the disadvantages mentioned. As a result, groups have to bear the administrative burden of maintaining these structures and the associated creation of value added and jobs takes place abroad.

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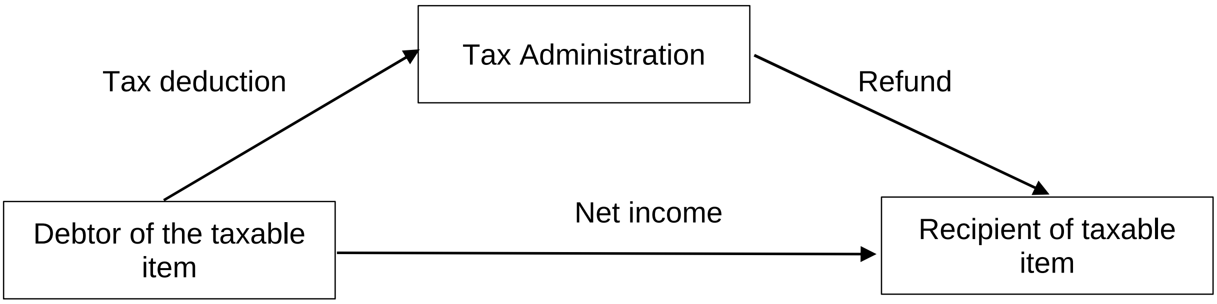
- Insufficient safeguard role: The foreign income of a Swiss beneficiary is not subject to the tax at present, although income tax does apply. Withholding tax as currently applied is unable to ensure the declaration of such income.

**From the debtor principle...**

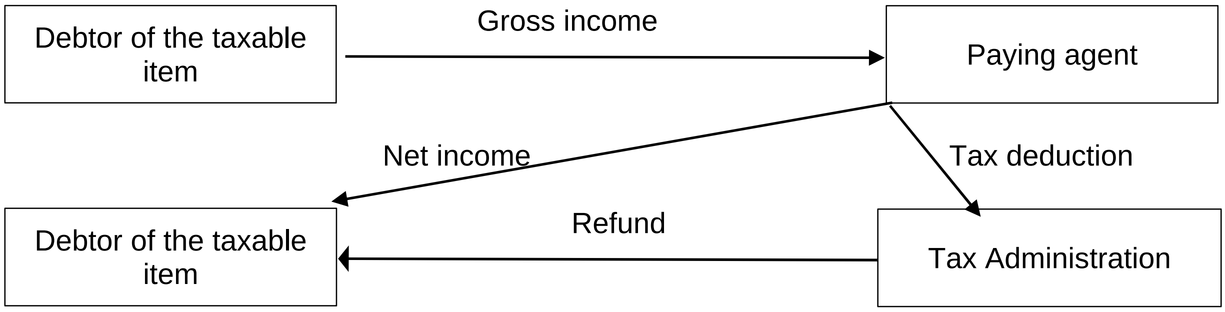
Withholding tax as currently applicable is collected in accordance with the debtor principle. When making a taxable payment, the debtor subtracts the tax amount from the payment irrespective of who the beneficiary is and transfers the corresponding amount to the FTA. The debtor thus transfers only the income minus the tax withheld, i.e. the net income, to the beneficiary. If beneficiaries who are Swiss residents correctly declare the taxable income for direct taxes, they are entitled to a refund. Foreign beneficiaries are possibly entitled to a refund on the basis of the double taxation agreement between Switzerland and the foreign country concerned.




For systemic reasons, taxation according to the debtor principle means that only Swiss securities can be taxed, and not foreign ones.

**... to the paying agent principle**

With taxation according to the paying agent principle, the duty to collect tax lies with the institution that acts as paying agent. The debtor of the taxable item transfers the full income amount to the paying agent (typically a bank). The paying agent withholds the tax amount from the taxable item and passes on the tax by reducing the payment to the recipient accordingly. It then transfers the tax to the tax authority.




The paying agent knows who the recipient of the taxable item is and can therefore collect the tax in a differentiated manner. While tax collection is more complex, refunding is simpler because the tax is no longer collected in all cases. With the paying agent principle, not only is the income of Swiss debtors affected, but also that of foreign debtors if the taxable item is paid through a Swiss paying agent. The withholding tax base is extended in this respect.

For systemic reasons, taxation according to the paying agent principle means that no securities held through a foreign paying agent can be taxed.

**What will be taxed in the future?**

The changeover from the debtor principle to the paying agent principle will also bring about changes regarding what is taxed.

- In principle, taxation will apply to all taxable items paid to natural persons resident in Switzerland. If the investor is not an individual resident in Switzerland (e.g. a pension fund or foreign investor), tax will not be collected.

- The tax base will be extended relative to the currently applicable law, as not only will the income of Swiss debtors be affected, but also that of foreign debtors if the taxable item is paid through a Swiss paying agent. Withholding tax will thus be harmonised with income tax.

- At the same time, the reform will restrict the tax base, as securities will be subject to withholding tax only if the income on them is processed through a Swiss paying agent.

- The income from Swiss participation rights will continue to be taxed according to the debtor principle. There is no need for action in this area from a capital market view or in terms of withholding tax's safeguard role, and the corresponding receipts will still be ensured. The tax will thus continue to be collected irrespective of who the investor is. As has been the case up to now, whether and to what extent foreign investors are entitled to a withholding tax refund will depend on the provisions of the applicable double taxation agreement.

| **Items that will be subject to tax with the paying agent principle** | **Items that will be subject to tax with the debtor principle** |
|---|---|
| Bond yields | Income from Swiss participation rights |
| Income from client balances with banks and savings banks | Income from Swiss participation rights distributed or retained by Swiss collective investment schemes |
| Income from foreign participation rights (dividends) | Lottery winnings |
| Income from collective investment schemes (with the exception of Swiss participation rights) | |
| Income from structured products (with the exception of Swiss participation rights) | |
| Life insurance benefits | |

**Option of voluntary disclosure as an accompanying measure**

The changeover to the paying agent principle could cause persons resident in Switzerland to transfer their assets to a foreign paying agent in order to avoid tax. Such an incentive could exist as, even in the event of a full refund, the collection of withholding tax entails a liquidity shortage and a loss of interest due to the refund coming at a later stage.

The possibility of opting for voluntary disclosure instead of paying withholding tax should prevent switches to a foreign bank. Taxpayers who opt for disclosure in the future will not have to pay withholding tax and will also avoid the administrative burden of the refund procedure. With disclosure, they will not provide the tax authorities with any information other than that which they already provide when filing their tax return for income and wealth taxes. Consequently, voluntary disclosure does not represent an invasion of their financial privacy. As for the paying agent, voluntary disclosure is simpler in administrative terms than the payment of tax.

Given that the existing debtor principle will be maintained for Swiss dividends, the associated disclosure possibilities will also remain unchanged.