PESTALOZZI
ATTORNEYS AT LAW

What is the latest news on the Swiss withholding tax on interest?

16.07.2019

Switzerland is planning to exempt certain groups of investors from the withholding tax on interest from bonds (including certain syndicated loans).

Specifically, investors residing outside Switzerland as well as investors residing in Switzerland in the form of a body corporate are to be exempt from withholding tax on interest on bonds. The planned changes may also facilitate loan syndication and should already be taken into consideration today in loan agreements.

Key takeaways

- **Loan agreements with Swiss borrowers typically limit the possibilities for syndication. Normally, it is stipulated that there must be no more than 10 non-bank creditors (Swiss 10 Non-Bank Rule). Otherwise, the loan is re-characterized as a bond, and withholding tax on interest is triggered. With regard to the pending work of the Swiss government to abolish withholding tax on interest for certain groups of investors, lenders must ensure that the contractual syndication restrictions are worded flexibly enough so that they no longer take effect if they are no longer needed due to the abolishing of withholding tax on interest.**
- **Companies in Switzerland who issue bonds on the capital market must monitor the further development. With a redesign of the Swiss interest withholding tax law, foreign issuance vehicles may no longer be needed for future bond issues, and it may be possible to simplify treasury structures.**

In what cases does Switzerland levy withholding tax on interest?

In contrast to other countries, Switzerland generally does not levy withholding tax on interest. Switzerland only levies withholding tax on interest in certain cases:

Pestalozzi Rechtsanwälte AG
Feldeggstrasse 4
CH-8008 Zürich
T +41 44 217 91 11
zrh@pestalozzilaw.com

Pestalozzi Avocats SA
Cours de Rive 13
CH-1204 Genève
T +41 22 999 96 00
gva@pestalozzilaw.com

pestalozzilaw.com

- from bonds issued by issuers in Switzerland;
- from credit balances at banks in Switzerland;
- from loan receivables of creditors outside Switzerland against borrowers in Switzerland, which are secured by security interests in Swiss real property.

Another situation that may result in Swiss withholding tax in connection with interest are the up-/cross-stream debt instruments between affiliated companies, where the agreed rate of interest is not at arm's length. In these cases, however, it is not a withholding tax on interest that is levied but rather a dividend withholding tax on a deemed dividend distribution that is levied.

Is loan interest subject to Swiss withholding tax?

Interest on loans is not generally subject to Swiss withholding tax (provided the rate of interest is at arm's length, and the loan is not secured by security interests in Swiss real property).

By way of exception, interest on loans is subject to Swiss withholding tax:

- if a bank in Switzerland owes interest to a creditor who is not a bank; or
- if the loan is re-characterized as a "bond" according to the Swiss tax authorities' practice ("bond-like" instrument, according to the so-called Swiss 10/20 Non-Bank Rules).

The Swiss 10/20 Non-Bank Rules are relevant, in particular, if a loan is syndicated. For the purposes of Swiss tax law, a loan is deemed a "bond" such that Swiss withholding tax is levied on the interest as soon as there are more than 10 creditors under the same debt instrument who are not banks (Swiss 10 Non-Bank Rule). Also, a loan is deemed a "bond" for the purposes of Swiss tax law if the Swiss debtor has more than 20 relevant creditors in total who are not banks (Swiss 20 Non-Bank Rule). There are exceptions for intra-group creditors.

How can an investor get relief from Swiss withholding tax on interest?

An investor resident outside Switzerland can obtain relief from Swiss withholding tax on interest only on the basis of the provisions of a double taxation agreement.

Please note, regarding Swiss withholding tax on interest from bonds, treaty relief is granted only in the form of a tax refund at a later date. In other words, there is no treaty relief at source for bond interest.

Investors in Switzerland, which generally also includes Swiss permanent establishments of companies residing outside Switzerland, may be granted full relief from withholding tax on interest under Swiss domestic tax law.

How do Swiss companies issue bonds?

On the international capital market, bonds can usually be placed only under the usual conditions if the interest is not subject to deduction of tax at source. This market environment is the reason why Swiss groups often look for ways to avoid issuing bonds except through a group company outside Switzerland. Categories and conditions have developed in the practice of the Swiss tax authorities regarding when any such issue abroad is recognized for tax purposes (hence not subject to Swiss withholding tax on interest).

What changes are envisaged regarding Swiss withholding tax on interest from bonds?

The Swiss government would like to reach a point where companies can issue bonds in Switzerland without being disadvantaged on the international capital market because of a withholding tax on interest. Fewer foreign issues and more issues in Switzerland should exist so that the added value and jobs associated with this issuing of bonds remain in Switzerland.

Following this train of thought, we see that the Swiss government is currently working on a proposal to change the law on withholding tax on interest income. In particular, it is envisaged that interest paid to investors outside Switzerland will no longer be subject to withholding tax. A corresponding consultation draft bill is expected for autumn 2019.

The planned changes may also facilitate loan syndication. Under the Swiss 10/20 Non-Bank Rules, a loan is re-characterized as a bond depending on the number of creditors involved that are not banks. To the extent that interest on bonds is no longer subject to any withholding tax, a re-characterization of a loan as a bond will no longer have any implications for withholding tax on interest.

What changes are envisaged regarding Swiss securities transfer tax?

The implications for Swiss securities transfer tax remain unaffected.

Even after changing the law on withholding tax on interest income, constellations are still conceivable in which the transfer of receivables from a syndicated credit facility re-characterized as a bond would be subject to Swiss securities transfer tax. Swiss securities transfer tax can even apply if there is no Swiss borrower under the syndicated credit facility.

Ludivine Boisard

Partner
Attorney at law

Pestalozzi Attorneys at Law Ltd
Cours de Rive 13
1204 Geneva
Switzerland
T +41 22 999 96 44
ludivine.boisard@pestalozzilaw.com

Remo Keller

Partner
Swiss Certified Tax Expert

Pestalozzi Attorneys at Law Ltd
Feldeggstrasse 4
8008 Zurich
Switzerland
T +41 44 217 92 78
remo.keller@pestalozzilaw.com

Jonas Sigrist

Partner
Attorney at law, Swiss Certified Tax Expert
Head of Tax Practice Group

Pestalozzi Attorneys at Law Ltd
Feldeggstrasse 4
8008 Zurich
Switzerland
T +41 44 217 93 26
jonas.sigrist@pestalozzilaw.com

Silvia Zimmermann

Senior Counsel
Attorney at law, Dr. iur., LL.M.

Pestalozzi Attorneys at Law Ltd
Feldeggstrasse 4
8008 Zurich
Switzerland
T +41 44 217 92 48
silvia.zimmermann@pestalozzilaw.com