

PERMANENT ESTABLISHMENT IN SWITZERLAND: BRANCH OR SUBSIDIARY?

DEFINITION OF A PERMANENT ESTABLISHMENT

Art. 4 and 51 of the Swiss Federal Law on Direct Tax define a permanent establishment as being fixed places of business which are wholly or partially engaged in business activities of an enterprise or an independent profession. They include, in particular, branches, manufacturing plants, workshops, sales offices, permanent agencies, mines and other plants for the extraction of mineral resources and building or installation projects with a duration of at least 12 months.

The definition of a permanent establishment does, per leading opinion, not exclude preparatory or auxiliary activities. Also, a permanent establishment does not require the presence of human personnel. The Supreme Court has ruled, for instance, that vending machines, which distributed goods against payment at the place of location, must be characterized as permanent establishments. This case, however, was ruled for domestic circumstances and may have no impact in an international environment.

Switzerland's double taxation agreements generally follow the OECD Model Tax Convention regarding the definition of permanent establishments.

DEFINITION AND MAIN DIFFERENCES BETWEEN A BRANCH AND A SUBSIDIARY

A branch is an office or establishment through which a foreign company engages in business in Switzerland. The branch is dependent and generally does not have its own legal personality. The foreign company is therefore directly and fully liable for all undertakings of the Swiss branch.

A branch does not have the authority to act independently of its headquarters and its activities will therefore depend on the nature and strategy of the company. It will have to register with the commercial register and at least one of the branch managers must be resident in Switzerland. Registration of the branch will imply publication of certain data of the foreign company, see "Registration formalities".

A subsidiary is a corporate entity in its own right. It is formed under and governed by Swiss law. Its shareholder (parent company) has therefore no liability (other than providing the share capital) for the undertakings of the subsidiary. The subsidiary has its own corporate bodies, including a board of directors. Influence of the parent company is limited to its vote in the annual general assembly of shareholders, where it may also elect the members of the board. In effect the parent company will exercise management control, but there is a legal separation of the two entities.

A subsidiary is mainly advantageous considering liability issues, as for some aspects the members of the board are personally liable. Other than in a branch-situation, the members of the board have actual control or rather oversight over the local activities.

TAX AND ACCOUNTING OBLIGATIONS

A Swiss branch of a foreign company is tax liable as a permanent establishment. Tax liability is limited to locally attributable profit and capital. An annual tax declaration has to be completed and filed. Standard corporate tax rates apply. The international allocation of taxable profit and capital is usually performed directly and with

the help of local book-keeping and annual financial statements. Only as an exception taxable factors may be indirectly and proportionally split between the branch and its headquarters with auxiliary parameters, such as revenues or production factors.

A clear advantage of the branch is, that it is not considered a taxable entity for Swiss withholding tax. Therefore, profit can be repatriated to the headquarters without tax consequences.

A local subsidiary has the same accounting obligations as any Swiss corporation. It must perform proper accounting and provide annual financial statements including balance sheet, P&L statement and notes. Switzerland has no concept of group taxation for direct taxes. A legally independent subsidiary is tax liable for its own profit and capital. Tax liability extends to worldwide profit except for foreign branches and/or real estate. A tax declaration including the annual financial statement has to be prepared on a yearly basis, allowing the tax authorities to assess taxes.

Swiss VAT is independent of the legal form of a business. VAT-liability is given for any business with Swiss revenues exceeding CHF 100,000 p.a.

REGISTRATION FORMALITIES

To establish a branch it has to be entered into the commercial register. The following information and documents are required: name and statutory domicile of the headquarters, a certificate of incorporation or a certified extract from the commercial register for the headquarters, a certified copy of the articles of association, the amount of authorized and paid-in share capital and the minutes of the board meeting granting authority to establish a Swiss branch, designating its local managers.

All documents certified or notarized by foreign institutions require an apostille and a certified translation into the official language at the place of registration is required. Additionally the application must include the desired place of business and name for the branch (including name of headquarters, domicile of headquarters, the word "branch" and the place of business) as well as valid and notarized signatures by people authorized to sign either for the headquarter or the branch. All individuals to be nominated with signatory power for the branch must be identified by passport-copies.

A subsidiary is set up as an independent corporate body, either as a limited liability company or a stock corporation. For the formation to come into effect, they have to be entered into the local commercial register. The application must include the company name, its domicile and address and be accompanied by the notarized public deed of formation, the articles of association, a notice of acceptance for every elected member of the board, a waiver of audit (if applicable), minutes of the meeting of the board containing its establishment and the nomination of any signatories, a bank certificate for the deposit of the share capital and declarations under special law including the waiver of real estate acquisition by foreign-controlled corporations.

The application must be duly signed by at least one member of the board (if individual signatory power) and notarized. All documents certified or notarized by foreign institutions require an apostille and a certified translation into the official language at the place of registration is required. All individuals to be nominated with signatory power for the branch must be identified by passport-copies.

STANDARD LEGAL OBLIGATIONS AND FORMALITIES FOR A BRANCH

Once set up, a branch has very few standard legal obligations. First and foremost an annual tax declaration has to be filed and any down-payments or final taxes have to be paid within the applicable deadlines. If VAT-liable, either quarterly or semi-annual VAT declarations and payments have to be effected.