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Implementation of Tax Reform and AHV Financing in the canton of Lucerne

International acceptance of Swiss corporate taxation is intended to be achieved through the Tax Reform and AHV Financing Package (TRAF). The changes will particularly affect the Federal Act on Direct Federal Tax ("DBG") and Tax Harmonization Act (StHG), and include the abolition of the cantonal tax status (privileged taxation as holding company, mixed company, domicile company) and the introduction of internationally recognised replacement measures.

At the federal level, the National Council and the Council of States have debated the proposal, and the aligned position was finally voted on by both chambers on 28 September 2018. On 31 August 2018, the Lucerne cantonal government presented the planned implementation of TRAF in the canton of Lucerne.

By halving the corporate income tax rate in 2012, the canton of Lucerne had already significantly mitigated the implications of the TRAF. The canton's tax law revision 2020 generally only implements a minimal number of the replacement measures offered by the STAF. Nevertheless, even after the STAF's entry into force, Lucerne will be able to stay in the group of the most economically attractive business locations in Switzerland.

The replacement measures the canton of Lucerne is implementing feature a patent box with maximum relief of 10 %, adoption of capital tax and attractive transitional rules in the transition period from 2020 until 2024 (alternatively until 2029). All of the measures are to become effective as of 1 January 2020.

The following page provides an overview of the most important planned legislative changes with their effects on corporate taxation in Lucerne.

If you have any questions, please contact your usual contact at PwC or one of the following TRAF experts at PwC Lucerne.

Overview of the most important planned legislative changes with their effects on corporate taxation in Lucerne

Reduction of capital tax base

For all legal entities, a uniform capital tax rate of 0.5% applies (multiplied by tax units of the municipality). Equity shares attributable to qualifying participations, patents and Group receivables are taxed at a fixed capital tax of 0.01%.

Patent box

The proportion of income from patents and similar rights, which is based on the qualifying research and development expenses (R&D) of the taxable person, is included in the calculation of taxable net income with a relief of 10%. One-time entry fee upon first time entry into the patent box (i.e. taxable add-back to taxable profit) to the extent of the past R&D costs before entry into the patent box. To the extent of the taxable add-back, a taxed hidden reserve has to be made/declared.

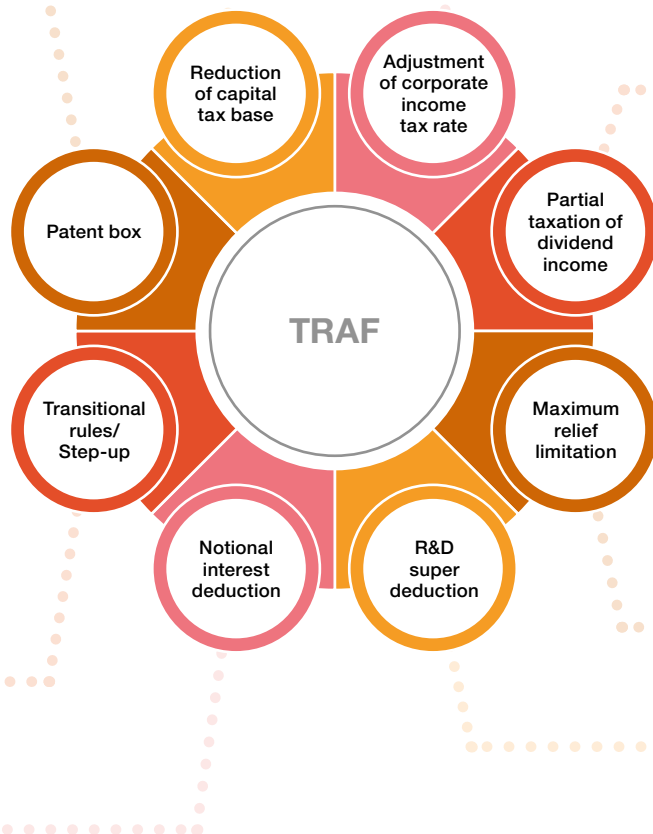
Transitional rules / Step-up

The realisation of hidden reserves and self-generated goodwill of companies which were previously taxed under a privileged regime will be taxed separately at a rate of 0.4% (multiplied by tax units of the municipality) for a limited period of 5 years.

Alternatively, based on current practice, a voluntary disclosure and subsequent depreciation of hidden reserves (current law step-up) for a limited period of up to 10 years remains available until the TRAF enters into force.

Notional interest deduction (NID)

A notional interest deduction on excess equity will **not** be introduced in the canton of Lucerne.



Adjustment of corporate income tax rate

The cantonal Council of Lucerne rejects the government's proposed increase in the income tax rate from 1.5% to 1.6% per unit. Thus, the effective tax burden (direct federal tax and cantonal tax for the municipality of Lucerne) is expected to remain unchanged at **12.3%**.

Partial taxation of dividend income

If individuals hold participations of more than 10% as business assets, the dividends will be considered only partially (i.e. 50%) for the assessment of the tax base. If individuals hold participations of more than 10% as private assets, the dividends will be considered only partially (i.e. 60%) for the assessment of the tax base.

Maximum relief limitation

The cantons are obliged to introduce a limitation for the relief from all TRAF measures combined. In order to remain competitive, the canton of Lucerne has set the respective limitation at 70% in the case of a current law step-up, which is the highest permissible rate. In other words, a quota of only 30% of the taxable income will remain ordinarily taxed. Where no step-up occurs, maximum relief lies at 20%.

R&D super deduction

A R&D super deduction will **not** be introduced in the canton of Lucerne.