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Implementation of Tax Proposal and AHV financing (TRAF) in Canton St. Gallen

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On 19 February 2019, the Council of the Canton of St. Gallen approved the XV Amendment to the Cantonal Tax Act by a large majority in its final vote. This includes the cantonal implementation of Tax Proposal 17 and Tax Proposal and AHV financing (TRAF). The 40-day referendum period is still running.

International acceptance of Swiss corporate taxation is intended to be achieved through the Tax Proposal and AHV financing ("TRAF", previously Tax Proposal 17). The changes will particularly affect the Federal Act on Direct Federal Tax (DBG) as well as the Tax Harmonization Act (StHG), and include the abolition of the cantonal tax status (privileged taxation as holding company, mixed company, domiciliary company) and the introduction of internationally recognized replacement measures.

The popular vote on the federal level will take place on 19 May 2019.

The legal effectiveness of the Amendment of the Cantonal Tax Act is subject to the legal effectiveness of the Federal Act on Tax Reform and AHV financing (TRAF) and will enter into force on 1 January 2020, if adopted in the referendum of 19 May 2019.

In particular, the reduction of the profit and capital tax rate for all companies domiciled in the Canton that have not benefited from any status will lead to a substantial reduction of their tax burden.

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

If you have any questions, please get in touch with your usual contact or one of the following tax proposal experts at PwC St. Gallen.

Amendment of capital tax

Ordinary capital tax rate of 0.2‰ (effective tax burden: 0.6 ‰) applies now for all legal entities. The taxable capital is subject to a reduction in proportion to qualifying participations, box-qualifying patents and intercompany-loans compared to total assets.

Partial taxation of dividends

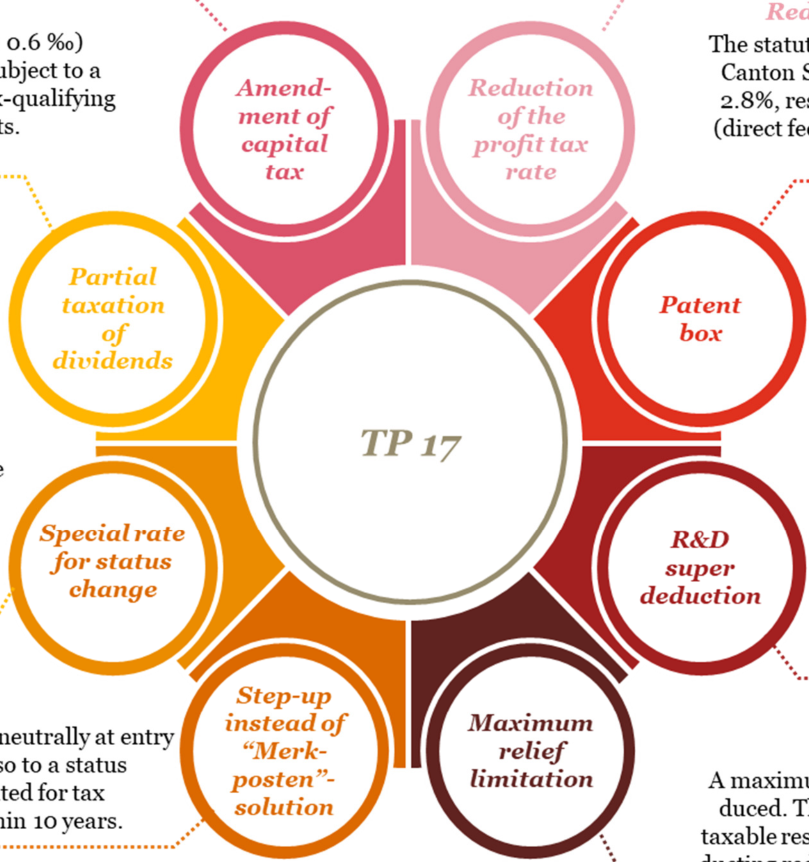
From the previous half-rate taxation of dividend income for individual shareholders at cantonal level, there will now be a switch to partial taxation of qualifying dividend income of 70%.

Special rate for status change

In case of status change from privileged (holding and domiciliary company) to ordinary taxation, the hidden reserves existing at the beginning of the implementation of this act, including the self-generated goodwill, will be taxed separately at the tax rate of 0.5% if realized within the next 5 years. This results in an effective tax burden of 1.49%.

Step-up instead of "Merkposten"-solution

Hidden reserves incl. goodwill can now be revealed tax-neutrally at entry into Swiss tax liability (in the Canton SG, this applies also to a status change of a mixed company) and subsequently depreciated for tax purposes. The revealed goodwill must be amortized within 10 years.



Reduction of the profit tax rate

The statutory corporate income tax rate in Canton SG will be reduced from 3.75% to 2.8%, resulting in an effective tax burden (direct federal tax and cantonal tax SG) of 14.5%.

Patent box

Net income from patents and similar rights is included in the calculation of taxable net income upon request in the ratio of qualifying research and development expenses to total research and development expenses per patent/similar right (nexus quotient) with a reduction of 50%.When the reduction is granted, the research and development expenses already taken into account in previous tax periods are added back to the taxable net profit and a taxed hidden reserve is created to this extent.

R&D super deduction

Research and development expenses incurred directly by the taxpayer or indirectly by third parties in the domestic market are eligible for a deduction of 140 % upon request.

Maximum relief

A maximum relief limitation of 40% is introduced. This ensures that at least 60% of the taxable result before offsetting losses and deducting reductions is always ordinarily taxed.

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