Virtual Case Experience Corporate Tax

Model Work Task 3

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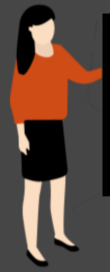
Step 1 - Ms. Bumblebee’s questions

1. From an economic point of view, how can FlyByU Group optimise its IP situation?



Considering economics of scope and scale it is usually not ideal, if multiple entities in the same country within a group own, develop, maintain, enhance, protect and exploit IP rights, as this likely leads to duplications, inefficiencies and increased administrative efforts. It could make sense to centralise all the groups IP rights within one group company.

2. How could FlyByU Group centralise its IP, and how could such transactions be structured in a tax-efficient manner?

In principle such transaction could be structured as a sale of the IP rights from one Swiss entity to the other or the two IP entities could be merged whereas the absorbed entity will transfer all its assets and liabilities to the surviving entity.

The Swiss tax law, in our case Art. 61 DFTA and § 67 TA ZH, allows a tax neutral transfer of hidden reserves between two entities provided that: (i) the assets are transferred at (tax) book value and the transferred assets remain subject to taxation in Switzerland.

Pursuant to Art. 61 para. 1 lit. c DFTA and § 67 para. 1 lit. c TA ZH the assets and liabilities of QuickShip AG could be transferred tax neutrally to FlyByU IP AG for corporate income tax purposes by means of a merger provided that (i) the assets and liabilities are transferred at (tax) book value and (ii) the assets and liabilities remain subject to taxation in Switzerland. Both conditions can be fulfilled in the case at hand. Moreover, the surviving entity FlyByU IP AG can use the tax loss carry forwards of QuickShip AG in line with Art. 67 para. 1 DFTA and § 70 TA ZH.

Step 1 - Ms. Bumblebee's questions

Pursuant to Art. 5 para. 1 lit. a federal act on withholding tax (WHTA) and Art. 6 para. 1 lit a^{bis} federal act on stamp duties (SDA) the reorganisation exemption also applies for Swiss withholding tax and issuance stamp duty purposes.
Pursuant to Art. 61 para. 3 DFTA and § 67 para. 3 TA ZH also only the IP as operating non-current assets could also be transferred tax neutrally to FlyByU IP AG, e.g. by means of a sale provided that (i) the assets and liabilities are transferred at (tax) book value and (ii) the assets and liabilities remain subject to taxation in Switzerland. Both conditions can be fulfilled in the case at hand. However, there results a blocking period of five years on the transferred assets (i.e. the IP) as well as on the acquiring and selling company pursuant to Art. 61 para. 4 DFTA and § 67 para. 4 TA ZH. A transfer of operating non-current asset does not have an impact on the tax loss carry forwards of QuickShip AG. In case the company does not generate any further profits, the tax loss carry forwards will expire and cannot be utilised anymore (Art. 67 para. 1 DFTA and § 70 TA ZH).

Pursuant to Art. 5 para. 1 lit. a WHTA and Art. 6 para. 1 lit a^{bis} SDA the reorganisation exemption also applies for Swiss withholding tax and issuance stamp duty.

Accordingly, it would make sense to centralise the IP by means of a sister merger to avoid a blocking period of five years and to maintain maximum flexibility for future reorganisations (Note that a subsequent tax neutral reorganisation does not harm an existing blocking period)
Circular letter number 5 "Reorganisations", cipher 4.1.2.2.4, published by the Swiss federal tax administration on 1 June 2004.

3. Could the planned centralisation of IP have any implications on indirect partial liquidation? Furthermore, what could be done in general to mitigate tax risks, if there are any?

As outlined in the prior case, an indirect partial liquidation can in general only be triggered, if non-operating assets are distributed from the acquired company to the acquiring company. In case of a sister merger, the indirect partial liquidation should not be triggered, since all the assets and liabilities of the absorbed entity will be transferred to the surviving entity and therefore remain at the same level. Also, in case of a sale of the IP an indirect partial liquidation should not be triggered as it is – based on the prevailing doctrine – not a transfer of non-operating assets.

As mentioned before, due to the indemnity clause in the share purchase agreement, FlyByU Holding AG would have to indemnify Mr. Seagull in case an indirect partial liquidation is triggered. Considering the risk in the amount of more than CHF 1m, FlyByU Group could obtain a ruling with the Zurich cantonal tax authorities to obtain an in-advance clearance that the envisaged steps do not trigger an indirect partial liquidation.

Step 2 - Combination of the holding activities

Combination of the holding activities

You

To Dominik Bischof

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Hi Dominik,

I researched around the topic.

Since the abolishment of the holding company regime as a result of the Swiss Tax Reform (STAF) as per 1 January 2020 it is in general possible from a Swiss tax perspective that one company performs holding as well as other business activities (e.g. IP management).

In principle, a tax neutral merger of QuickShip AG and FlyByU IP AG into FlyByU Holding AG would be possible as well (two upstream mergers) or alternatively the two sister entities QuickShip AG and FlyByU IP AG could in a first step be merged followed by a downstream merger of FlyByU Holding AG into FlyByU IP AG (the surviving entity after the first step). After these two steps FlyByU IP AG would be the surviving entity. Pursuant to Art. 61 DFTA and § 67 TA ZH in this case a tax neutral merger would be feasible as well, provided that: (i) the assets are transferred at (tax) book value and the transferred assets remain subject to taxation in Switzerland. Both conditions can be fulfilled in the case at hand. Considering that FlyByU Holding AG is the listed ultimate holding company of the group the two upstream mergers would probably be easier to implement. Furthermore, Ms. Bumblebee should consider that FlyByU Holding AG, as a listed company, is subject to more extensive disclosure obligations than its subsidiaries. In the case at hand it might not be recommendable to transfer the IP activities to FlyByU Holding AG as the group's IP is an important success factor of the group and provides it with a competitive advantage.

However, in case QuickShip AG will be absorbed by FlyByU Holding AG or vice versa within five years after the acquisition the indirect partial liquidation will be triggered and FlyByU Holding AG would have to indemnify Mr. Seagull, which would result in additional costs of more than CHF 1m. Hence, the advantages of such a combination needs to be thoroughly assessed and it needs to exceed the one-off costs.

Let me know your thoughts. Does it help to answer to Ms. Bumblebee?

Kind regards,

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Step 3 - Tax assessment

Follow up – Tax assessment

You

To Dominik Bischof

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Hi Dominik,

Of course, Mr. Beagle can factually issue a tax assessment disregarding the tax ruling with the Zurich tax authorities. However, by doing so, he is breaching the principle of protection of trust, i.e. he makes the Zurich tax authority act contradictory (“*venire contra factum proprium*”). Even tax rulings, which were approved by the tax authorities in contradiction to the administrative practice or which include a wrong confirmation of tax consequences, can become legally binding.

As in the case at hand FlyByU IP AG has a legally binding (correct) tax ruling in place, it is possible to have the tax assessment corrected. In order to do so, FlyByU AG must first file a written objection with the Zurich cantonal tax authorities, within 30 days after receipt of the tax assessment (Art. 132 DFTA and § 140 TA ZH). Since this is a statutory deadline, it cannot be extended. If FlyByU IP AG misses this deadline, the tax assessment becomes final (it enters into “formal legal force”). In case an objection is filed after the deadline of 30 days the tax authorities only have to consider it in very limited cases (so-called request on restoration of the missed deadline, cf. Art. 133 III DFTA und § 15 Tax Ordinance Zurich (TO ZH). As a last option, FlyByU IP AG could try to apply for a voluntary reconsideration. However, the chances of success are very limited in this case, since it is only an informal legal remedy. If this fails as well, the tax assessment can theoretically only be overturned by means of a revision (i.e. an exceptional legal action), which – in case of negligence – is not available. Therefore, once the 30 days deadline is expired, it becomes very difficult to amend a tax assessment, even if it is clearly not correct.

Cf. notification on the formal procedure for tax rulings in the area of direct federal tax, withholding tax and stamp duties as published by the Swiss federal tax administration on 29 April 2019.

Kind regards,

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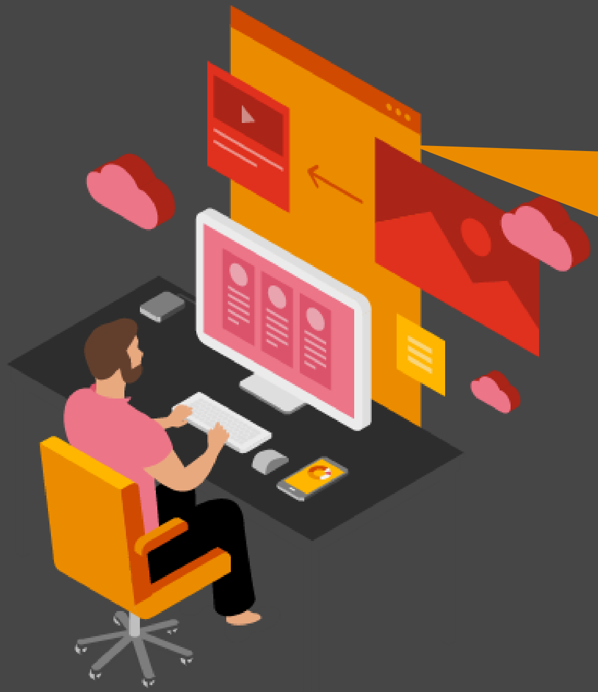
Step 4 - Tax returns



FlyByU IP AG should declare an additional deduction for its research and development expenses pursuant to § 65a TA ZH and analyse whether the application of a patent box for the patented IP (ApiFly Software) would result in a more favorable result (§ 64a and § 64b TA ZH), in particular considering the buy-in into the patent box regime.