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Year End Tax Bulletin 2013

In this Bulletin

- Introduction
- The Netherlands
- Belgium
- Luxembourg
- Switzerland
- International developments

1. Introduction

This Year End Tax Bulletin summarizes the most significant tax developments in the Benelux and Switzerland in 2013 and highlights the main legislative changes announced for 2014. It also provides an insight into major international tax developments. The focus is on developments and changes with relevance for internationally operating enterprises. Given the general nature of this Year End Tax Bulletin, the information contained in this publication should not be regarded as a substitute of detailed legal advice. You are, however, most welcome to contact us if you would like to receive more information on any of the below topics.

2. The Netherlands

2.1 Main changes 2014: companies / corporate income tax

2.1.1 New Tax Arrangement for the Kingdom

On 12 December 2013, the Ministry of Finance announced that an agreement has been reached between the Netherlands and Curacao on a new bilateral arrangement for the avoidance of double taxation (the "**Arrangement**") and the application of the anti-abuse provision of article 35a in the current Tax Arrangement for the Kingdom ("**TAK**").

It is expected that the Arrangement will become effective as of 1 January 2015. During 2014, the Netherlands will not invoke article 35a of the current TAK with respect to the non-Dutch resident taxation rules, i.e. the applicable grandfathering period up until the year 2013 is extended with an additional year. For more detailed information we refer to our Tax Flash of 13 December 2013.

2.1.2 Codification partitioning doctrine in relation to the participation exemption

Subject to a number of conditions, income (dividends and capital gains) realized on an investment in a qualifying subsidiary is exempt from corporate income tax by virtue of the participation exemption regime. It may occur, however, that not all of the conditions are met uninterruptedly throughout the period that the parent company owns the shares in the subsidiary.

Supreme Court case law doctrine dictates that in those cases capital gains (or losses) realized by the parent company must be partitioned in a tax-exempt part (to which the participation exemption applies) and a taxable part (to which the participation exemption does not apply).

This partitioning doctrine will now be incorporated into law, with retroactive effect. The codification is caused by a verdict of the Supreme Court on 14 June 2013. In that case, litigated by Loyens & Loeff, the Supreme Court ruled that the partitioning doctrine does not apply if the change in the tax regime applicable to a participation is caused by a change in the law (as opposed to a change in facts or circumstances), unless the legislator explicitly provided for transitional rules.

Based on the legislative proposal, any income (both dividends and capital gains) from the participation originating from a period that the participation exemption did not apply will be taxed at the latest upon disposal of the participation. The legislative proposal includes that the partitioning doctrine also applies if the tax regime applicable to a participation changes as a result of a change in the law. For more detailed information we refer to our Tax Flashes of 14 June 2013 and 4 September 2013.

2.1.3 Base Erosion and Profit Shifting: national developments in the Netherlands

On 4 October 2013, the Dutch government issued a legislative proposal which would provide the Dutch tax authorities with a legal basis to spontaneously exchange information to tax treaty partners with respect to certain financing and licensing companies. A draft decree published on 18 October 2013 stipulates that group financing, licensing and/or leasing companies must confirm in their annual corporate income tax return they have satisfied the substance requirements as listed in the decree.

If a tax payer cannot confirm that all substance requirements are met, it should (i) indicate in the tax return which requirements are not met, (ii) provide all necessary information for the tax authorities to determine which of the substance requirements are met, and (iii) provide an overview of all interest, royalty and similar payments for which a reduction of (withholding) tax has or could be claimed under any tax treaty or EU Directive. This information will then be spontaneously provided by the Dutch tax authorities to the relevant treaty partner.

Also, in respect of holding companies the Dutch government announced that advance tax rulings will only be granted if the group of which a company forms part has sufficient nexus with the Netherlands, which is defined as ‘real presence’. Holding companies that satisfy the substance requirements for group financing, licensing and/or leasing companies are considered to have real presence in the Netherlands.

The rules are scheduled to apply as from 1 January 2014. For more detailed information we refer to our Tax Flashes of 30 August 2013 and 22 October 2013.

2.2 Main changes 2014: VAT, Real Estate Transfer Tax & Other

2.2.1 Abolition of deemed supply in case of self-producing goods by VAT exempt entrepreneurs

The application of self-produced goods by an entrepreneur performing exempt activities is currently deemed to be a supply of goods for VAT purposes. This deemed supply leads to an extra VAT burden in cases where certain costs of the production process are initially VAT exempt, such as personnel costs, non-building land, etc. In case the deemed supply applies, all costs of the production process, even if purchased without VAT, are taken into account when determining the VAT due. VAT on actual costs during the production process is deductible as a result whereof VAT is payable on the cost price of the self-produced goods. This deemed supply leads especially in the social-housing sector to a VAT burden.

As of 1 January 2014 this deemed supply will be abolished, and the application of self-produced goods will not be taxable with VAT. Subsequently, VAT on costs relating to the self-production is no longer deductible as far as the right to deduct input VAT is limited for the entrepreneur.

*2.2.2 Real Estate Transfer Tax (“***RETT***”) on interest in real estate entities without legal personality*

As of 1 January 2014 the levy of RETT changes on acquisitions of an interest in entities without legal personality that own real estate. Currently, due to case law, interests lower than 33.3% could be acquired in such entities without RETT if the entity has a capital divided in participations. As of 1 January 2014 acquiring an interest in such entity is taxed with RETT regardless of the volume of the interest acquired. Only in case the entity qualifies as a collective investment scheme or a fund for collective investment in shares as mentioned in the Act on Financial Supervision, an acquisition of an interest below 33.3% will not be taxed with RETT.

2.2.3 Changes to the tax on tap water

As of 1 January 2014 the tax rate regarding the ‘tax on tap water’ (“**TTW**”) will be increased from EUR 0.165 to EUR 0.330 per cubic meter. Moreover, as of 1 July 2014 the limit of 300 cubic meters per year will be abolished and a degressive rate will be introduced, meaning that as of that date TTW is also due on water consumption that exceeds 300 cubic meters per year. This measure will particularly affect companies that are large-scale consumers of tap water (e.g. companies in the chemical or food & beverage industry).

2.2.4 The Netherlands concludes FATCA agreement with the United States of America

On 18 December 2013, the United States of America (“**US**”) and the Netherlands signed an intergovernmental agreement (model 1A) (“**IGA**”) to implement the Foreign Account Tax Compliance Act (“**FATCA**”). FATCA obliges foreign financial institutions (“**FFIs**”) to report to the US Internal Revenue Service (“**IRS**”) information about financial accounts held by US taxpayers, or by foreign entities in which US taxpayers hold a substantial ownership interest (certain financial institutions may be exempt from the reporting requirement, such as qualifying Dutch pension funds). Failure to meet these reporting obligations would result in a 30% withholding tax on payments received by FFIs.

By concluding the IGA, the administrative burden for Dutch FFIs is expected to be reduced, since they do not have to sign separate agreements with the IRS, and report to the Dutch authorities, that in turn will inform the IRS. Pending Dutch parliamentary approval of the IGA, with the goal of having the IGA enter into force by 30 September 2015, Dutch FFIs are deemed compliant with FATCA and not subject to the withholding tax.

2.3 Main changes 2014: employment taxes

2.3.1. Employer tax extended

The 16% employer tax will be extended for another year. The tax will be due in 2014 on 2013 taxable employment income exceeding EUR 150,000 per employee. Employment income includes fixed and variable salary elements, such as a bonus, but it excludes inter alia severance payments. The 2013 excessive employment income will be deemed to be paid on 31 March 2014 and therefore the employer needs to pay the employer tax in April 2014. Because of the possible violation of EU law, several legal procedures have been started this year. Although the outcome of these procedures will also be of importance for the 2014 employer tax, a separate objection will need to be filed against the employer tax to be paid in 2014.

2.3.2. Tax deferral for severance payments abolished

As of 1 January 2014 the tax deferral for severance payments (“*stamrechtvrijstelling*”) will be abolished. Consequently, severance payments will become fully subject to taxes at the moment of payment. However, the deferral will remain applicable to entitlements existing on 31 December 2013. Under conditions, these existing entitlements can be paid out as a lump sum in 2014, in which case only 80% will be subject to taxation.

2.3.3 Pension

Since the legal pension age will be increased from 65 to 67 on 1 January 2014, the yearly accrual of pension rights changes. In view hereof, pension schemes must be adjusted before 2014.

2.3.4 Immigration law

- As of 1 January 2014, the conditions for obtaining a work permit for individuals from outside the EU/EEA and Switzerland will be more strict, e.g. with respect to the salary requirement (introduction of a salary requirement in line with the prevailing market rates for the position for which the permit will be granted) and the term of the permit (in principle only one year).
- Since 1 October 2013, wealthy foreign nationals may qualify for a temporary residence permit on certain strict conditions. The individual must inter alia invest at least EUR 1.25 million of capital in the Dutch trade and industry.

2.4 Developments in 2013: companies / corporate income tax

2.4.1 Dutch Supreme Court rules that Finnish investment fund is not entitled to a refund of Dutch dividend withholding tax

The 1965 Dividend Withholding Tax Act provides for refunds to both resident and non-resident entities that are not subject to profit tax. However, non-resident entities must also comply with the additional condition that they would not be subject to Dutch corporate income tax, if they would have been resident in the Netherlands. In November 2013 the Supreme Court ruled that a Finnish open-ended investment fund is not entitled to a refund since it would be subject to Dutch corporate income tax if it would have been a resident of the Netherlands. The investment fund argued that it was in an objectively comparable position as tax-exempt resident entities as it was exempt from tax in Finland. The Supreme Court, however, rejected this argument and held that the Netherland was not obliged to follow the tax exemption given to the investment fund by Finland. In this case, the Supreme Court overruled the Court of Appeal of Den Bosch that had ruled in March 2012 that the Finnish investment fund was entitled to a refund.

2.5 Developments in 2013: VAT

2.5.1 Supreme Court raises questions on funds investing in immovable property to the ECJ

On 1 November 2013 the Supreme Court referred to the European Court of Justice (“**ECJ**”) for a preliminary ruling on the application of the VAT exemption for the management of funds investing in immovable property. The Supreme Court wants to learn from the ECJ whether such property funds can be classified as collective investment funds for VAT purposes. If so, the management of those funds is VAT exempt. For the time being, the management of funds investing in whatever type of assets is VAT exempt in the Netherlands. The Supreme Court doubts however whether that exemption also applies to the management of funds that invest in other types of assets than securities and other liquid financial assets.

3. Belgium

3.1 Main changes 2014: companies / corporate income tax

3.1.1 Amendment to the calculation of the notional interest deduction

When determining the notional interest deduction (“**NID**”), a Belgian company with a permanent establishment in a tax treaty country should reduce the base amount (i.e. the company’s total equity) on which the NID is calculated by any positive difference between (i) the net book value of assets allocated to such foreign establishment and (ii) the liabilities allocated to such establishment.

The Antwerp Court of First Instance referred a question for a preliminary ruling to the ECJ on 24 June 2011 with respect to this reduction. On 4 July 2013, the ECJ issued its ruling in this case (*Argenta Spaarbank*, case C-350/11). It found that this limitation does constitute a restriction of the freedom of establishment as it may cause Belgian companies to refrain from pursuing their activities through a permanent establishment in a Member State other than Belgium. We refer to our Tax Newsflash of 4 July 2013 for more detailed information on this case.

The Belgian Government has now proposed to delete this limitation of the calculation basis of the NID. The correction would in the future occur at a later stage as the NID calculated on the higher calculation basis would be reduced, if it concerns a permanent establishment located in the EEA, with the lower amount of (i) the result of the foreign permanent establishment or real estate and (ii) the net asset value of the foreign permanent establishment or real estate multiplied by the NID rate. If it concerns a permanent establishment outside the EEA, the calculation basis would always be reduced with (ii).

3.2 Main changes 2014: withholding tax

3.2.1 Increase of liquidation withholding tax rate

The 10% liquidation withholding tax rate is to be increased to 25% as of 1 October 2014. A liquidation distribution with application of the 10% withholding rate remains, therefore, possible until 30 September 2014. The existing exemptions from the liquidation withholding tax are not affected (for example the EU Parent - Subsidiary Directive including the extension thereof to qualifying parent companies located in treaty countries).

Under a transitory regime the shareholders are allowed to distribute the taxed reserves as a dividend at a withholding tax rate of 10%, on the condition that they contribute the net proceeds into the share capital of the company before the last day of the financial year ending before or on 30 September 2014. Reserves incorporated in the capital and taxed at 10%, can thereafter be reimbursed free of withholding tax if distributed after 8 years (4 years for Small and Medium-sized Enterprises ("**SMEs**")). If the capitalized reserves are distributed earlier, withholding tax will be due at the following decreasing rates:

- 15% during the first 4 years (2 years for SMEs);
- 10% in the 5th and 6th year (3rd year for SMEs); and
- 5% in the 7th and 8th year (4th year for SMEs).

3.3 Main changes 2014: individual income tax

3.3.1 Reporting requirements

New reporting requirements have been introduced for founders/beneficiaries of foreign legal structures. For more detailed information we refer to our Tax Flash of 19 July 2013.

3.4 Main changes 2014: VAT

3.4.1 VAT on lawyers fees

Lawyers' fees, currently exempt from Belgian VAT, will become subject to 21% VAT as of 1 January 2014 provided that the services rendered are deemed located in Belgium for VAT purposes.

3.5 Developments in 2013: companies / corporate income tax

This section concerns measures applicable as of assessment year 2014 (i.e. financial years ending on 31 December 2013 or in 2014 but at the latest on 30 December 2014)(“**AY 2014**”).

3.5.1 Fairness tax

Belgian companies (except small enterprises as defined in Article 15 of the Companies Code) and (proportionally) Belgian permanent establishments of foreign companies become subject to a so-called ‘fairness tax’ on their distributed dividends. The fairness tax is a separate assessment at a rate of 5.15% (5% + 3% crisis surcharge).

The tax is only applicable if, in a given taxable period, dividends are distributed by the company, and (part or all of) the taxable profit is offset against NID and/or carried forward tax losses.

The taxable base for the fairness tax for Belgian companies, is determined as follows. First, any positive difference between the gross dividends distributed during the taxable period and the taxable base that is effectively subject to the ordinary corporate income tax, is determined. The resulting positive difference is then reduced by the amount of any dividends that derive from previously (and at the latest during AY 2014) constituted taxed retained earnings (with application of the LIFO-method: last in, first out). The outcome of this calculation is limited to a fraction that expresses the proportion between the amount of both the NID and the carried forward losses, effectively deducted in the taxable year (the numerator), and the fiscal result of the taxable year (the denominator).

It is debatable whether the fairness tax complies with European law, specifically with the EU Parent-Subsidiary Directive. That is why the Government has notified the European Commission of this measure. In addition, it is questionable whether its application to branches is compatible with the tax treaties entered into by Belgium. Finally, the Council of State doubts whether there exists a valid justification for excluding small companies from the scope of application of the fairness tax. For more detailed information we refer to our Tax Flash of 19 July 2013.

3.5.2 Capital gains on shares

Capital gains realized on shares qualifying for the participation exemption regime are fully exempt from corporate income tax. For non-SMEs, such exempt capital gains are however subject to a separate taxation at the rate of 0.412%.

3.5.3 Notional interest deduction

The calculation base of the NID has been modified. Currently, shares held as portfolio investments, with an initial investment value of at least EUR 2.5 million, and held for at least 12 months, benefit twice:

- the dividend income benefits, under conditions, from the 95% dividend received deduction (“**DRD**”); and
- the value of the share portfolio investments does not reduce the calculation base of the NID (whereas this is the case for shares held as financial fixed assets).

These two benefits can no longer cumulate. The DRD regime ought to prevail. Only if the investment is not eligible for the DRD, the calculation base for the NID will not be reduced by the value of the shares held as portfolio investments.

3.5.4 Patent income deduction

Resident companies and Belgian permanent establishments of foreign companies may deduct 80% of the income from qualifying patents if – amongst other conditions – the patents have been developed or improved in a “research center”, i.e. a separate business department or branch of activities of the company. SMEs rarely have such separate research centers. To make the patent deduction more accessible for these companies, the Belgian legislator has abolished the requirement to develop or improve the patents in a separate research center for SMEs as of AY 2014. Note that at the same time the exemption of payment of the professional withholding tax on the wages of certain researchers is increased from 75% to 80% on wages received as of 1 July 2013.

3.6 Developments in 2013: investment companies

The present section only concerns regulated funds (i.e. SICAV, SICAF, SIC and Pricaf).

3.6.1 Taxation of investment income

The Belgian taxation of Belgian source dividends and interest when distributed to EU foreign funds has been held contrary to European law (ECJ, 25 October 2012, case C-387/11, *Commission vs. Belgium*) as resident funds receive a credit and/or are refunded for Belgian taxes. The request of the Belgian State to limit in time the consequences of the ECJ decision has been denied.

Further to this decision, the law has been modified (see below) and the Belgian Revenue has issued a circular and (not yet published) guidelines in respect of the principles governing the reimbursement requests, including, but not limited to,

- a limitation of the reimbursement procedure to foreign UCITS, although this limited scope was not part of the ECJ decision (i.e. other type of funds may consider filing a claim as well);

- statute of limitation for reimbursement requests of 5 years (i.e. 5 years as of 1 January of the year during which the withholding has been applied); and

- a list of the certificates required in order to grant the reimbursement.

While the aforementioned ECJ decision has condemned the tax treatment in the hands of the shareholders (through the withholding tax), the Belgian State has modified the tax regime of the Belgian funds in order to comply with this decision.

As of AY 2014, Belgian source dividends are taxed in the hands of the Belgian funds through a withholding tax (in principle: 25%) that cannot be credited anymore nor is reimbursable. Belgian funds are thus effectively taxed at a rate of 25% on Belgian source dividends they receive.

3.6.2 Modification of withholding taxes

The withholding tax rate is fixed at 25%, with a reduced rate of 15% only available for residential REITs, i.e. REITs investing at least 80% of their net asset in residential real estate located in the EEA.

At the same time, a uniform withholding tax exemption regime applies on dividends distributed by Belgian retail and institutional investment companies to non-residents: a full exemption is granted except for Belgian source dividends redistributed to non-residents.

The Belgian implementation of the EU Savings Directive is extended to all investment funds and companies with capitalization shares that invest directly or indirectly more than 25% in receivables, while in the past the principles of the EU Savings Directive were only applicable to UCITS.

3.7 Developments in 2013: withholding taxes

3.7.1 Reduced rates for new shares issued by SMEs

Reduced rates apply to dividend distributions in respect of new (non-preference) shares issued from 1 July 2013 onwards by SMEs in return for a cash contribution. For such dividends the following withholding tax rates apply:

- 25% on dividends distributed in the first 2 years after the shares were issued;
- 20% on dividends distributed out of the profit allocation of the second accounting year following the accounting year of the contribution; and
- 15% for dividends distributed out of the profit allocation of the third (or any subsequent) financial year following the accounting year of the contribution.

Various transitional measures apply as well as specific anti-abuse provisions.

4. Luxembourg

4.1 Main changes 2014: companies / corporate income tax

4.1.1 Plans of the new Luxembourg government

On 4 December 2013 the new Luxembourg government was installed. The new government’s program contains several tax measures, aimed at keeping Luxembourg an attractive location for international business activities, especially for headquarters of international groups.

The tax measures aim to further improve Luxembourg’s tax regime in terms of coherence with international standards (general substance rules, codification of transfer pricing principles in line with OECD guidelines, improvement of the procedural framework for advance tax confirmation, etc), to introduce new tax regimes (notional interest deduction) and to improve existing ones (IP regime, participation exemption).

It is not yet clear when these measures will be implemented. For more detailed information we refer to our Tax Flash of 5 December 2013.

4.1.2 Envisaged changes in exit tax rules

According to Luxembourg tax law currently in force, the migration of a Luxembourg company out of Luxembourg implies in general the taxation of unrealized gains and the payment of corporate income tax (no automatic deferral of the “exit tax” upon migration). These provisions are not in line with the outcome of the ECJ case National Grid Indus (see our Tax Flash of 29 November 2011 for details on this case).

In light of this ECJ case, on 15 March 2013 a proposal of law was submitted to Parliament amending, among others, the tax provisions regarding exit taxation by introducing the possibility for a Luxembourg company to opt for a deferred payment of exit taxation on unrealized gains where the Luxembourg company migrates to a State of the EEA, if the continued ownership of the assets is duly demonstrated. The deferral will not be subject to other conditions (such as guarantees, interest payments or pre-approval from tax authorities).

4.2 Developments in 2013: companies / corporate income tax

4.2.1 Corporate income tax – debt waivers

On 7 February 2013, the Administrative Court of Luxembourg (the “**Court**”) rendered its decision on the tax qualification of a partial shareholder debt waiver including a clause of “better fortune”, overruling a judgment from the Administrative Tribunal that held that a shareholder debt waiver is a taxable event.

The Court in essence concluded that a debt waiver made by a shareholder does qualify as a hidden capital contribution, even if it contains a better fortune clause. The Court did not decide on the value of the hidden contribution, but it deferred this matter to the tax authorities. For more detailed information we refer to our Newsflash of 15 February 2013.

4.3 Developments in 2013: investment companies

4.3.1 Corporate income tax aspects

On 12 July 2013 the Luxembourg law implementing the AIFM Directive (“**AIFM Law**”) was approved by Parliament, which includes changes in the area of taxation. This section will focus on the changes in relation with corporate income taxation.

Introduction of the Special Limited Partnership (SLP)

The AIFM Law introduced a new type of partnership, the SLP (*Société en Commandite Spéciale*). The SLPs will resemble the LPs (*Sociétés en Commandite Simples*) but will have no legal personality. SLPs (as long as they are not regulated by the UCI Law, the SIF Law, the SICAR Law and the ASSEP and SEPCAV Law) will not be required to publish annual accounts. In addition, the AIFM Law introduced a modernized legal framework for LPs, more adapted for investment structures.

Full tax neutrality

(S)LPs are tax transparent for corporate income tax purposes, but not for the municipal business tax. In the absence of a real business, however, (S)LPs are fully tax neutral (i.e. no municipal business tax) where the Luxembourg general partner does not hold at least 5% of the (S)LP interest.

For more detailed information we refer to our Newsflash of 10 July 2013.

4.3.2 New rules on carried interest

Until recently, Luxembourg did not have clear rules on the taxation of carried interest. However, rules for the taxation of carried interest arrangements have now been introduced by the AIFM Law. The AIFM Law introduces a beneficial tax regime for certain types of carried interest (*l'intéressement aux plus-values*). It distinguishes between two categories of carried interest earned by the employees of an Alternative Investment Fund Manager ("**AIFM**"): (i) general carried interest (based on an incentive right not attached to a share or unit); and (ii) carried interest attached to a share or unit in the Alternative Investment Fund ("**AIF**") held by an employee of its AIFM.

The income on the first type of carried interest arrangement is taxed at the progressive income tax rate of 43.6%, although under conditions a reduced rate (corresponding to 25% of the personal income tax rate) applies for AIF employees who migrate to Luxembourg.

Capital gains and dividends on the second type of carried interest realized are subject to the same progressive income tax rate. However, with respect to capital gains it should be noted that if the gain is realised after a period of six months it is not subject to taxation, unless the carried interest represents a substantial (generally meaning a direct or indirect interest of more than 10% of the AIF's capital) stake in a tax-opaque AIF. For more detailed information we refer to our Newsflash of 10 July 2013.

4.4 Developments in 2013: individual income tax

4.4.1 Luxembourg impatriate tax regime

As of 1 January 2013, modifications to the impatriate regime entered into force. Expatriation-linked benefits (e.g. moving costs, housing expenses, tax equalisation expenses, etc.) are tax exempt under certain limits and conditions. It applies for a maximum period of six years.

4.4.2 Envisaged rules for individuals migrating to Luxembourg

On 22 July 2013, a bill of law introduced a new step-up in basis for individuals who become Luxembourg residents concerning a substantial shareholding (i.e. an interest of more than 10%) as well as convertible debt instruments (if the taxpayer has a substantial shareholding in the entity that has issued the debt instrument). For more detailed information we refer to our Newsflash of 29 July 2013.

4.4.3 Bill introducing a new wealth management vehicle in Luxembourg

On 22 July 2013, a bill of law introduced a new wealth management vehicle in the form of a private foundation (the "**Family Foundation**"), an orphan entity without shareholders or members.

Main features are that the Family Foundation is an entity subject to income tax at the standard corporate income tax rate, but benefits from an exemption for dividends, interest and capital gains on securities and is also exempt from the Luxembourg annual net wealth tax. Payments made by the Family Foundation to non-resident beneficiaries are not subject to withholding taxes and should not be taxable in Luxembourg. For more detailed information we refer to our Newsflash of 29 July 2013.

4.5 Developments in 2013: VAT

4.5.1 Amendments to the 2013 Luxembourg VAT law

Three major amendments have been made to the Luxembourg VAT law in 2013:

- in order to implement article 4 of the EU Directive 2008/8/EC, the place of taxation of long term hiring of means of transport to non-taxable persons has been modified. These services are now taxable in the country where the lessee is established or has its domicile. Given that no reverse-charge mechanism is available in this situation, the supplier is likely required to register for VAT purposes in the lessee's country, if not already the case;

- the Luxembourg VAT invoicing and compliance rules have been amended in order to implement Directive 2010/45/EU: it should in particular be noted that the Luxembourg VAT law now conditions the deduction of a VAT input to the possession of a VAT compliant invoice; and

- the Luxembourg VAT exemption for fund management has been extended in order to exempt fund management services provided to AIFs, as defined in the AIFM Law: it should be noted that all AIFs benefit from this VAT exemption, whether regulated or not.

5. Switzerland

5.1 Main changes 2014: companies / corporate income tax

5.1.1 Swiss Corporate Tax Reform III

Since several years there is a dispute going on between the EU and Switzerland about the Swiss cantonal tax privileges, such as the holding and mixed company regime. The EU is of the view that these beneficial Swiss tax regimes are not in compliance with the EU's code of conduct for taxation of companies.

During 2012, the EU put even more pressure on Switzerland by threatening to put Switzerland on a black list of tax havens. As a result thereof, Switzerland recommenced their Corporate Tax Reform III ("**CTR III**") which originated from 2008. On 19 December 2013, the final report on CTR III was issued, in which Switzerland recognizes that the special cantonal regimes have to be abolished or amended in the near future. However, the report made clear that Switzerland wants to remain an attractive business location and that in order to remain attractive certain amendments in the Swiss tax system are needed.

Hence, in the report a mixture of measures is proposed to secure and even improve the attractiveness of Switzerland such as:

- introduction of new EU/OECD compatible regimes for the taxation of mobile activities (e.g. license box, notional interest deduction);
- reduction of cantonal corporate income tax rates; and
- amendments and/or abolition of certain tax charges, which have a negative impact on the attractiveness of Switzerland (e.g., issuance stamp tax on equity, cantonal capital tax, amendment of participation exemption).

The above proposals will be further developed and should result in a consultation procedure on CTR III which is expected to start by summer 2014. However, due to the Swiss political and legal system, the implementation of the proposals will probably take between five to seven years. During this phase the old regimes should remain effective. It might even be possible that some new regimes may be introduced earlier (e.g. license box) and would exist next to the old regimes.

5.1.2 New rules on executive pay and corporate governance for listed Swiss companies

On 3 March 2013, Swiss voters voted in favor of an initiative “against excessive pay” by council of states member Thomas Minder (the ‘Minder Initiative’). As a result thereof, the Federal Council issued a final ordinance implementing the Minder Initiative, as well as its explanatory report on 20 November 2013 (the ‘**Ordinance**’). The Ordinance will enter into effect on 1 January 2014 and will be valid until the Swiss Federal Parliament will enact upcoming implementing legislation.

The Ordinance is only applicable to joint stock companies governed by the Swiss code of obligations whose shares are listed on a stock exchange in Switzerland or abroad. Therefore, companies that only have bonds or participation certificates listed are not in scope of the Ordinance.

The key implications of the Ordinance can be summarized as follows:

- as of 1 January 2014 certain remunerations are prohibited, which include severance payments, payments in advance and commissions for acquisitions or transfer of enterprises (exceptions exist when such payments arise as a matter of law);
- as of the 2015 general meeting, all of the covered companies are required to specify in their articles of association the approach to binding shareholder voting on compensation approval compensation for the board of directors, advisory board and executive board. The articles of association must therefore include that: (i) the general meeting votes annually but separately on the aggregate compensation for the board of directors, advisory board and executive board; and (ii) the latter vote has a binding effect; and
- as for financial years starting on or after 1 January 2014, compensations paid during the financial year should be disclosed in a separate compensation report. Such compensation report must be reviewed by the auditors and disclosed to the shareholders in the same manner as the audit report on the annual financial statements.

5.2 Developments in 2013: companies / corporate income tax

5.2.1 Swiss Federal Supreme Court rules on place of effective management

On 16 May 2013 the Federal Supreme Court ruled in a case regarding the definition of the place of effective management in the context of an offshore finance company. The Federal Supreme Court ruled that the effective place of management of the offshore company was located in Switzerland and not in Guernsey.

In the case at hand, an offshore finance company organized as a Limited was registered in Guernsey and funded by its parent company in the canton of Zug. The offshore company solely provided loans to affiliated (group) companies. The Federal Supreme Court ruled that the Limited (i) had only a limited function; (ii) performed solely administrative activities exclusively for its parent company in Zug; and (iii) had only a limited infrastructure available. The fact that more than half of the board members were Guernsey residents and that the location of board meetings and general assemblies took place in Guernsey did not alter the decision of the Federal Supreme Court.

What became clear is that the Federal Supreme Court requires "functionally adequate" substance as a decisive criterion to determine the effective place of management. According to the Supreme Court, the place of effective management is where the operating business management within the purpose of the company takes place, including were daily business decisions, are made.

5.2.2 Switzerland – Hong Kong tax treaty in force

Hong Kong and Switzerland have signed a new double tax convention on 11 October 2011. During 2013, the tax convention became effective for Switzerland per 1 January and for Hong Kong per 1 April. Most interesting feature of this new convention is that for companies with direct shareholdings of at least 10% and pension funds, dividends should not be taxed with dividend withholding tax.

5.2.3 New Switzerland – China tax treaty signed

China and Switzerland have signed a new double tax convention on 25 September 2013. For companies with direct shareholdings of at least 25%, dividends will be taxed at maximum 5% dividend withholding tax (previously 10%). Corporate shareholders that do not qualify for the 5% treaty rate may still benefit from a reduced rate of 10%. Withholding tax on royalties may not exceed a rate of 9% (previously 10%). Furthermore, no Chinese business tax or VAT will be due on international transport services provided by Swiss shipping companies and airlines.

6. International developments

6.1 Companies / corporate income tax

6.1.1 Base Erosion and Profit Shifting: OECD

Recently tax avoidance and in particular base erosion and profit shifting ("**BEPS**") are hotly debated subjects in both national and international politics. This has led to a number of proposals and action plans by international organizations and national governments.

The OECD presented its ambitious Action Plan on BEPS, as requested by the G20, on 19 July 2013. The Action Plan includes actions that may impact domestic law provisions, tax treaties and transfer pricing rules, and the relationship between tax authorities and taxpayers. It aims to assist governments to address the concerns arising from double non-taxation and low taxation associated to tax planning within a two-year period. The Action Plan has three main pillars: (i) establishing international coherence of corporate income taxation, (ii) restoring the full effects and benefits of international standards, and (iii) ensuring transparency while promoting increased certainty and predictability. For more detailed information we refer to our Tax Flash of 19 July 2013.

6.1.2 Base Erosion and Profit Shifting: amendments to the Parent Subsidiary Directive

As part of its Action Plan against tax fraud and tax evasion (we refer to our Tax Flash of 6 December 2012), the European Commission issued a proposal (the "**Proposal**") on 25 November 2013 to amend the Parent Subsidiary Directive (2011/96/EU; "**Directive**"). The Proposal includes two main amendments to the Directive.

The first entails that Member States shall withdraw the benefit of the Directive in case of an "artificial arrangement" (or an "artificial series of arrangements") which has been put into place for the essential purpose of obtaining an improper tax advantage under the Directive and which defeats the object, spirit and purpose of the tax provisions invoked. A transaction is considered as "artificial" if it does not reflect "economic reality". The Proposal lists the specific elements that Member States should analyze to determine the artificiality of arrangements.

Secondly, the obligation of the Member States to exempt profits derived by a parent company (or its permanent establishment) from a subsidiary company is limited to cases in which the profit distributions have not been deducted by the subsidiary. The purpose of the Proposal is to deny the exemption granted by the Directive to parent companies which have made use of hybrid loan instruments, i.e. instruments providing for payments that are considered deductible interest in the Member State of the subsidiary and exempt dividend in the Member State of the parent company.

If the Proposal is approved by the Council of the European Union, Member States are expected to implement the amended Directive into their domestic law by 31 December 2014. For more detailed information we refer to our Tax Flash of 25 November 2013.

6.2 VAT

6.2.1 Employer can deduct input VAT on costs for pension administration and investment management in separate fund

According to the ECJ, based on its ruling of 18 July 2013 in the PPG-case, input VAT on costs made by a separate pension fund for the administration and investment management can be deducted by the employer if the employer has the right to deduct input VAT regarding general costs. In the case that came before the ECJ the tax inspector had rejected the input VAT deduction by the employer, arguing that the costs were made on services that were not rendered to the employer but to the separate pension fund. The ECJ ruled however that such costs are general costs of an employer and as such the employer, if entitled to VAT deduction on general costs, can deduct the input VAT. In the same case the ECJ repeated its consideration from the Wheels-case (7 March 2013) that pension funds executing a defined benefit pension scheme cannot be regarded as special investment funds. As a consequence the management of such funds can not apply the VAT exemption.

6.2.2 ECJ rules that non-VAT entrepreneurs can be part of a VAT group (Commission v Ireland and others)

On 9 April 2013 and 25 April 2013, the ECJ delivered its judgments in a number of infringement proceedings that the European Commission had started against various Member States (Ireland, the Netherland, Finland, the UK, Denmark and the Czech Republic). According to the European Commission, these Member States incorrectly allowed non-VAT entrepreneurs to be part of a VAT group. Based on a literal interpretation of Article 11 of the EU VAT Directive, the ECJ ruled that non-VAT entrepreneurs may, in principle, also form part of a VAT group. Moreover, the ECJ ruled that the context and objective of Article 11 of the EU VAT Directive do not lead to a different conclusion. The ECJ, therefore, concluded that non-VAT entrepreneurs may form part of a VAT group if the customary requirements of financial, organizational and economic links are met. We further refer to our VAT Newsflash of 26 April 2013.

6.2.3 ECJ rules that turnover of foreign permanent establishment does not influence the pro rata of the head office (Le Crédit Lyonnais)

On 12 September 2013, the ECJ ruled in the case *Le Crédit Lyonnais* on the question whether or not turnover of a foreign permanent establishment has to be taken into account when calculating the pro rata of the head office. According to the ECJ, the provisions of the EU VAT Directive have to be interpreted as not permitting a head office to take the turnover of its permanent establishments in other Member States into account for determining the pro rata. In this regard, the ECJ ruled that it does not matter whether the permanents establishments are located inside or outside the EU. We further refer to our EU Tax Alert of October 2013 (edition 122).

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