



Amendments to the Tax Act in Liechtenstein

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This CONFIDA Info provides an overview of the proposed amendments to the Tax Act (SteG), in particular, the introduction of specific anti-avoidance rules in connection with the tax exemption of dividends and capital gains from participations, the notional interest deduction, and the elimination of the asymmetric treatment of capital gains and losses from participations. The details of the bill are discussed in the Government's Report and Proposal (BuA) No. 35/2018.

Background of the Bill

The reason for amending the Tax Act was the EU Code of Conduct Group's review of the Liechtenstein tax law and administrative practice with regard to tax transparency, fair corporate taxation and implementation of the BEPS minimum standards. Those jurisdictions that are unwilling to adjust their tax regulations assessed as harmful have been blacklisted by the Economic and Financial Affairs Council (Ecofin). The gray list includes jurisdictions - Liechtenstein a. o. -, where deficits have been identified, but which have agreed to eliminate the deficiencies by the end of 2018.

Tax exemption of dividends and capital gains

In order to prevent tax avoidance, the tax exemption of dividends based on participations in legal entities shall be submitted to specific requirements as stipulated by the EU. Now, dividends from participations held as business assets of natural as well as legal persons shall not be exempt from income tax / profit tax, if (Art. 15 (2) (n) and Art. 48 (3) SteG-E [Tax Act Bill]):

- a) dividends from participations of 25% and more of the votes or capital can be deducted as expenses by the paying legal entity;

OR

- b) for participations:

1. the total gross revenue of the foreign taxable legal entity sustainably consists of more than 50% of passive income (except in the case of effective economic activity); and

2. the net profit of the foreign taxable legal entity is directly or indirectly subject to low taxation. Low taxation means:

- in the case of participations < 25%: income tax burden at a tax rate of less than 6.25% (50% of 12.5%);
- in the case participations ≥ 25%: effective income tax burden of less than 50% compared to a domestic case, determined in accordance with the provisions of the Liechtenstein Tax Act.

The new anti-avoidance provision is also applied analogously to distributions from foreign foundations, establishments structured similar to foundations and special asset dedications with personality, where the point of reference for the assessment of low taxation is the tax rate of less than 6.25% because of the absence of a specific participation quota. As far as dividends from participations are not tax-exempt due to the fulfillment of the above requirements, capital gains (realized and unrealized) as well as liquidation proceeds are also deemed not to be tax-free. The anti-avoidance provision is restricted to foreign legal persons, as the criterion of low taxation, per se, cannot be satisfied in purely domestic cases.

Passive income shall be understood as (Art. 48 (4) SteG-E):

- a) interests or other income from financial assets, royalties or other income from intellectual property and income from finance leases;
- b) dividends or distributions from foreign legal entities whose total gross revenue consists of more than 50% of low-taxed passive income pursuant to provision a (interests etc.) and insofar as such income was not realized in the course of an effective economic activity;

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- c) capital gains and unrealized appreciations of participations in foreign legal entities provided they meet the requirements set out in provision b.

In order to claim the tax exemption taxpayers will be required to prove that dividends, distributions, realized and unrealized capital gains are tax-free income. If proof is not provided, such income is deemed not to be tax-free and added to the taxable net income (Art. 48 (7) SteG-E).

Transitional periods are envisaged for the new provisions on the exemption of dividends and distributions. Thus, Art. 48 (3) (b) and (4) to (7) SteG-E shall be applied on dividends based on participations in foreign legal entities and on distributions from foreign asset structures for the first time from the tax year 2022, if the participations have been acquired before January 1, 2019, or beneficial interests have existed before January 1, 2019.

Notional Interest Deduction

Specific anti-avoidance provisions are added to the regulations on notional interest deduction. Basically, there are two tax avoidance issues that are addressed:

1. Double deduction (debt capital with the parent and equity with the subsidiary) (Art. 54 (4) SteG-E).

If participations are financed by debt capital, notional interest deduction can be claimed at the level of the subsidiary and deduction of debt capital interests at the level of the parent company. In order to prevent such double-dipping structures, a tax offset at the parent company shall be made in the future for participations in legal entities that can claim a deduction of equity interests but are financed with debt capital. The offset shall be made to the extent of the target yield of the debt financing, up to the maximum notional interest deduction claimed by the participation. The relevant debt financing is based on the deduction of own interests and debt-financed participations from the taxable equity. The tax-effective offset is calculated as follows:

	taxable equity
–	own interests
–	participations in legal persons, which claim notional interest deduction
=	subtotal (only relevant if negative balance)
x	4% target yield
=	tax-effective offset

2. Abusive Transactions (Art. 54 (5) SteG-E).

Further anti-avoidance provisions in connection with notional interest deduction may concern the following transactions with related parties:

- a) monetary assets and assets in kind from related parties, insofar as they are not already included in the assets not needed for business operations;
- b) acquisition of operations or sub-operations held by related companies;
- c) transfer of participations to or from related parties.

For claiming notional interest deduction, the taxpayer will have to prove that the transactions were not made for tax purposes, but for economic or otherwise considerable reasons. If the proof fails, such transactions are not taken into account in determining the notional interest deduction.

Treatment of capital losses from investments

The asymmetric tax treatment of capital gains and losses from participations in legal entities, which is assessed as being harmful, results from the fact that capital gains from participations are not taxed while capital losses are tax-deductible. According to the present bill (Art. 47 (3) (C^{bis}) SteG-E), realized and unrealized capital losses from participations in legal entities shall no longer be permitted to be deducted; i.e. they shall be added to the taxable income and charged with the income tax.

In this context, Art. 53 SteG, which governs depreciations and value adjustments regarding the permanent value reduction of participations, is deleted without replacement. Furthermore, Art. 52 (6) and (8) SteG (Restructurings) and Art. 58 (5) SteG (Group Taxation), which refer to Art. 53 SteG, are adjusted. In the area of depreciations and value adjustments regarding the permanent value reduction of participations as well as restructurings, transitional provisions must be observed. It should be noted here that there is no transitional provision envisaged for eliminating the asymmetric treatment of capital gains and losses from participations in legal persons.

Further Amendments

The following further amendments to the Tax Act are proposed:

1. Changes in the statutory assessment of limited taxpayers (Art. 23 (2) (a) and (c) SteG-E)

Under the current rules, limited taxpayers are automatically (ex officio) submitted to the statutory tax assessment by the Tax Administration, provided that the taxable domestic income exceeds CHF 150,000. If the domestic taxable income is less than CHF 150,000, a regular assessment is possible on request. Now, it is suggested to choose the domestic gross income as a point of reference and set this at CHF 200,000.

2. Collection of withholding tax from the taxpayer in exceptional cases (Art. 27 (4) SteG-E)

Collecting the withholding tax is basically the responsibility of the party liable for the payment. In practice, however, there are cases in which the withholding tax cannot or cannot be collected entirely by the party liable for the payment. For example, in the case of persons working in Liechtenstein for foreign employers or cross-border commuters from Switzerland who become tax-liable in Liechtenstein due to the exceeding of the 45-day limit, or upon presentation of a DTA certificate the party liable for the payment has trusted in. In such cases, the Tax Administration shall collect the withholding tax directly from the recipient of the payment.

3. Commercial law provisions for the relevant annual financial statement (Art. 47 (1) SteG-E)

So far it has been possible to prepare the annual financial statement according to international accounting standards (IFRS). It is proposed that annual financial statements compliant with international standards pursuant to Art. 1139 PGR shall be excluded for the assessment of the income tax.

4. Reporting requirement regarding capital transfers (Art. 96 SteG-E)

The tax return shall specify:

- donations > CHF 10,000 (as is the case now);
- inheritances and bequests > CHF 10,000 (not only foreign, but also domestic);
- contributions from foundations, establishments structured similar to foundations or special asset dedications (new).

Consequently, donations, inheritances and legacies as well as contributions from home and abroad shall be subject to the reporting requirement.

5. Joint liability of bodies (Article 111 (3) (b) SteG-E)

The current provision concerning the liability of the bodies of legal persons when they move their domicile outside the EEA / CH (without liquidation) shall be extended to include the transfer of the place of effective management of legal persons and special asset dedications without personality.

Entry into force and applicability

The Liechtenstein Parliament will probably deal with the current bill at First Reading in June and at Second Reading after the summer break so that the amended Tax Act is expected to enter into force as of 1 January 2019. The proposed amendments to the Tax Act will be applicable for the first time for the tax year 2019 or 2022.

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