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NEWSLETTER

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New accounting legislation as tax catalyst

Dear Ladies and Gentlemen,

In this newsletter, the amended accounting legislation will be analysed from a tax point of view. The full article about this topic was published in a professional journal in March 2014 (the complete reference will be given at the end of this article).

95% of tax decisions are at the expense of the taxpayer, 90% in case of the Federal Supreme Court. This is not due to a formally or materially poor initial position of the taxpayer, it is an inherent failing in the system of tax proceedings and the fiscal court proceedings. All public sector professionals at administrations and courts are public sector employees and thus, basically, have the state's interest at heart. The new accounting legislation will not make great inroads into this basic situation, and despite all noble claims of fiscal neutrality, it will cause all levies to go up.

According to Code of Obligations 958, accounting should represent the financial situation of a company in such a way that third parties can make a fair judgement. Thus "fair presentation" becomes the new fundamental standard. Building hidden reserves is no longer possible.

In contrast to this stand all written materials and the message all stressing again and again that the introduction of the new accounting legislation should ensure fiscal neutrality.

A few preferential rights in tax proceedings exist, which reduce profits significantly: hidden reserves on stocks, del credere, and immediate write-offs, to name just the most important. These cannot be reconciled with the principle of "true and fair view."

Thus the starting position is as follows: As previous accounting legislation was more open, fiscal accounting regulations could be applied to balance sheet and profit and loss account, with the framework set up by the tax authorities as a matter of course. According to the new law, however, the very same fiscal accounting regulations can, strictly speaking, not be applied anymore – but the tax authorities are still entitled to accept them. At first glance it looks likely all manifestations of fiscal neutrality will be implemented. To what extent these are actually implemented in the future is open to debate – it is only the fiscal appetite of the public sector than can supply an answer.

When it comes to stocks, calculated according to accounting regulations and various methods (FiFo, LiFo, etc.) tax authorities allow the taking of a third as hidden reserves on stock. As an example: stocks with a market value of CHF 9m can be entered into the balance sheet at CHF 6m. Cost of goods can be raised by CHF 3m – a pleasant preferential right of tax practice. Should it not be possible to build them up in the first year, these hidden reserves can be established gradually over the years. It is obvious that this reduces tax before profit considerably, but this also means a reduction of profits in the actual balance of trade and thus does not correspond with "fair presentation" anymore.

In practice, tax authorities are granting flat del credere on debtors: 5% on (domestic) debtors, 10% on foreign debtors and 15% on foreign debtors with foreign currencies involved, with specific regulations varying from canton to canton. More often than not these flat depreciations are granted on the net amount loaned, after deduction of loans effectively at risk. This constitutes another case of building up hidden reserves that does not correspond with a "true and fair view".

Another obstacle in tax legislation on the way to "fair presentation" is the balancing (capitalisation) of services that have not been billed yet. So far, SMEs in the services sector have rarely added this provision to the balance sheet. It is and has been the custom to add up all debtors that have been billed during the financial year. A balance position for "work commenced" was unusual. Fiscally neutral entries require individual advice. Artax Fide Consult AG has developed its own approach.

As the dilemma between fiscal neutrality and "fair presentation" has been demonstrated, the question arises as to how approaches in line with accounting regulations can be applied to achieve the desired fiscal neutrality which has been guaranteed in relevant written material.

Approach One: Anyone intending to claim previous preferential rights and thus deviating from the accounting regulations under the new accounting legislation needs, if they want to correctly implement it, to show this in the appendix. This would almost implicitly allow a profit adjustment in the tax statement; however, it is a necessary consequence of correctly implementing regulations.

The second approach lies with dual accounting: a balance sheet is created according to both tax law regulations and regulations of accounting legislation, in particular without hidden reserves – a radical solution, but nonetheless authentic.

You find the full article "Das neue Rechnungslegunsrecht als Steuerkatalysator" (in German) by clicking on this link.
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Kind regards
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