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New ruling regarding joint and several tax liability of directors

The Swiss Federal Supreme Court ("SFSC") recently made a new ruling regarding the joint and several liability of members of the board of directors in case of a factual liquidation of a company (BGer 2C_607/2017 of 10 December 2018). In the following, we will discuss the key message of the decision and its impact on the Swiss corporate tax system.

1. Underlying facts

On 25 March 2004, X bought all shares of B SA from A. At the time of the share deal, B SA owned 15 properties in the Geneva area which constituted its sole assets. Between 25 March and 20 October 2004 X was director of B SA and in his corporate capacity sold 13 of the 15 properties of B SA in this period. On 20 October 2004, X resigned as director of B SA and was deleted from the commercial register.

In 2005, the cantonal tax authority of Geneva assessed the tax liability of B SA for the business year 2003 and started legal actions relating to tax evasion for the business years 2000 – 2004 against the company. In 2007, B SA was not able to comply with its tax liabilities and filed for bankruptcy. Since B SA had no funds at the time of the liquidation in 2009, the cantonal tax authorities of Geneva held X jointly liable

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for the tax liabilities of B SA for the business years 2003 – 2007 according to art. 55 Swiss Federal Direct Income Tax Act ("FDIT"). Furthermore, the cantonal tax authorities ruled that X had caused a factual liquidation of B SA in 2004 because he sold 13 of the 15 properties that B SA owned and held him responsible for the factual liquidation gain. X appealed against this ruling at the Cour de Justice of Geneva, however without success and subsequently brought his matter before the SFSC.

2. Findings of the SFSC

At the outset, the SFSC confirmed its jurisprudence that already the sale of the major assets (though not all) of a company can lead to a factual liquidation, notwithstanding that the company still owns minor assets. Hence, the SFSC ruled that the sale of 13 of the 15 properties of B SA in 2004 had led to a factual liquidation of B SA.

As a next step, the SFSC assessed whether the provision on the joint and several liability under the FDIT could also be applied analogously to a factual liquidation under Art. 15 of the Federal Withholding Tax Act ("WTA"). The SFSC came to the conclusion that both provisions were applicable to a factual liquidation since a liquidation of a company can take place independently of its actual registration in the commercial register. If the law were only applicable to a formal liquidation this could lead to an outflow of the equity from the company and to an undesired limitation of the joint and several liability of the members of the board. With this clarification, the SFSC confirmed the unanimous Swiss legal doctrine on this matter.

Finally, the SFSC determined the application in time of the joint and several liability in connection with a factual liquidation. It determined that the legislator did not provide for a time limitation for the joint and several liability of members of the board. Hence, a member of the board who newly joins the board of a company could be held unlimitedly liable retroactively for earlier liabilities of a company if art. 55 FDIT is applicable. However, this unlimited liability does not apply to debts of a company incurred after the resignation of a member of the board. According to the SFSC, the liability for such future debts could only be affirmed if such rule had its basis in primary legislation (i.e. based on a formal act of parliament). In addition, the SFSC considered that a member of the board could attempt to disprove his liability by demonstrating that the board member implemented all reasonable measures in order to prevent the occurrence of a liability.

3. Conclusion

The ruling of the SFSC demonstrates that the threshold to qualify a sale of substantial assets of a company as a factual liquidation is rather low. As a consequence, the evaluation of tax risks of a substantial transaction such as the sale of real estate should always also include the review of this risk factor. This aspect is even more pertinent given the SFSC's finding confirming the unlimited joint and several liability with retroactive effect for members of the board.

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