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## Taxation of Charities in Switzerland

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### 1. IN GENERAL

In Switzerland, non-profit organizations are in principle subject to the ordinary taxes levied on the federal, cantonal and communal levels. The federal as well as the cantonal laws, however, exempt charitable organizations under certain requirements from taxation. In general, legal entities that pursue public or charitable purposes are exempt from direct taxation provided that their profit is exclusively and irrevocably dedicated to such purposes<sup>1</sup>. Special rules apply for VAT.

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<sup>1</sup> See for more details para. 2 below.

Under Swiss direct tax law, only *legal entities* may benefit from tax exemption<sup>2</sup>. Individuals and partnerships may not request tax exemption even if they pursue purposes identical to those of charities<sup>3</sup>. Although the most frequently used legal forms of charities are associations and foundations, tax exemption is not restricted to these forms<sup>4</sup>. However, charitable legal entities organized as public limited companies or co-operatives must statutorily renounce any distribution of profits to their shareholders<sup>5</sup>.

Further, the tax exemption for charities is *not* restricted to organizations having their statutory seat in Switzerland. Legal entities incorporated in another country that are organized similarly to Swiss legal entities may request tax exemption for their permanent establishment in Switzerland<sup>6</sup>.

## 2. INCOME TAXATION OF CHARITIES

### 2.1 Overview

Non-profit organizations are in principle subject to the ordinary corporate income tax on the federal, cantonal and communal levels as well as the ordinary capital tax on the cantonal and communal levels<sup>7</sup>. Legal entities that pursue charitable or public purposes, however, may apply for tax exemption. The requirements are stated in Article 56 (g) Federal Income Tax Act (FITA)<sup>8</sup> for the federal corporate tax and in Article 23 (1) (f) Federal Tax Harmonization Act (FTHA)<sup>9</sup> for the cantonal and communal corporate income and capital taxes<sup>10</sup>. Pursuant to Article 56 (g) FITA, legal entities may

<sup>2</sup> Reich M., Gemeinnützigkeit als Steuerbefreiungsgrund, Archiv für Schweizerisches Abgaberecht ASA 58 (1989/90), 465 et seq., 480.

<sup>3</sup> Kuster R., Steuerbefreiung von Institutionen mit öffentlichen Zwecken (Zürich: Schulthess Polygraphischer Verlag, 1998), 244.

<sup>4</sup> Kuster, Steuerbefreiung von Institutionen mit öffentlichen Zwecken, 209 f.

<sup>5</sup> Kreisschreiben Nr. 12 der Eidgenössischen Steuerverwaltung vom 8. Juli 1994, Steuerbefreiung juristischer Personen, die öffentliche oder gemeinnützige Zwecke (Art. 56 Bst. g DBG) oder Kultuszwecke (Art. 56 Bst. h DBG) verfolgen; Abzugsfähigkeit von Zuwendungen (Art. 33 Abs. 1 Bst. i. und Art. 59 Bst. c DBG), para. II (2) (a) („circular letter no. 12 of 8 July 1994“).

<sup>6</sup> Praxishinweise der Schweizerischen Steuerkonferenz zuhanden der Kantonalen Steuerverwaltungen vom 18. Januar 2008, Steuerbefreiung juristischer Personen, die öffentliche oder gemeinnützige Zwecke oder Kultuszwecke verfolgen, Abzugsfähigkeit von Zuwendungen, para. 5 (IV) („practical instructions to the cantonal tax administrations of 18 January 2008“).

<sup>7</sup> Kuster R., Die steuerliche Behandlung von Non-Profit-Organisationen, Schweizer Treuhänder ST 1993, 869 et seq. Associations and foundations, however, benefit from a reduced tax rate that generally amount to the half of the ordinary corporate income tax rate.

<sup>8</sup> Bundesgesetz vom 14. Dezember 1990 über die direkte Bundessteuer (DBG), SR 642.11.

<sup>9</sup> Bundesgesetz vom 14. Dezember 1990 über die Harmonisierung der direkten Steuern der Kantone und Gemeinden (StHG), SR 642.14.

<sup>10</sup> The Federal Tax Harmonization Act contains binding guidelines for the cantonal direct tax legislation. The requirements for tax exemption are thereby exhaustively stated in the FTHA that means that the cantons do not have any room of discretion.

request tax exemption (i) if they pursue charitable or public purposes and (ii) if their profits are exclusively and irrevocably dedicated to such purposes<sup>11</sup>.

## 2.2 Material conditions for tax exemption of non-profit organizations

### 2.2.1 Charitable purposes

According to the established jurisprudence of the Federal Supreme Court, the term “charitable purpose” contains two elements: First, the purpose needs to be of general interest to the community and second, it must constitute an interest of an altruistic nature.

A purpose is of *general interest* to the community if it serves the common welfare. The term “general interest” has a rather broad meaning and includes activities in charitable, humanitarian, health-promoting, ecological, educational, scientific and cultural areas<sup>12</sup>. The respective circular letter of the Federal Tax Administration mentions as examples social care, art and science, education, the promotion of human rights, the protection of the environment, homeland and animals, as well as development aid<sup>13</sup>. Not of general public interests are activities that merely have an entertaining character, and activities that only serve a limited number of beneficiaries such as the members of a family or an association. In order to qualify as general public interest, the charitable organizations’ activity must in principle be open to an unlimited circle of persons<sup>14</sup>.

Whether a certain purpose is of general interest to the community depends on the relevant public opinion of the particular time. According to the Federal Supreme Court’s jurisprudence, the legal-ethical principles as stated in the Swiss Constitution and the Swiss legislation may serve as guidance in determining whether an activity may be regarded as being in the general public interest. The term “general interest” nevertheless underlies a broad range of interpretation<sup>15</sup> which may, in Switzerland, lead to diverging results in the cantons. In an effort to counteract such divergences, the Swiss Tax Conference, an association of all cantonal tax administrations, published practical instructions for the cantonal tax administrations in order to reach

<sup>11</sup> In addition, Article 56 (h) FITA and Article 23 (1) (g) FTFA exempt legal entities from corporate income and capital taxes that pursue religious purposes provided that the profits are exclusively and irrevocably dedicated to such purposes.

<sup>12</sup> Circular letter no. 12, para II (3) (a).

<sup>13</sup> Circular letter no. 12, para II (3) (a).

<sup>14</sup> *Locher P.*, Kommentar zum DBG, Bundesgesetz über die direkte Bundessteuer, II. Teil, Art. 49-102 DBG (Therwil/Basel: Verlag für Recht und Gesellschaft, 2004), Art. 56 n. 87. The question whether the circle of beneficiaries is in principle open to everyone may be difficult to answer. The limitation of the organization’s purpose to the inhabitants of a certain community may not hinder its tax exemption if the community has several thousand inhabitants. If, however, the community only has one hundred inhabitants, the restriction may be a hindrance. The practical instructions published by the Swiss Tax Conference give the following example: A privately-held day nursery that only accepts children of a certain city district, or – in the case of a smaller community – of the community, does not fulfill the requirement of an open circle of beneficiaries. The day nursery must in principle be open for any child living in the region (practical instructions to the cantonal tax administrations of 18 January 2008, para. 4 (II) (E)).

<sup>15</sup> *Kuster*, Steuerbefreiung von Institutionen mit öffentlichen Zwecken, 200.

harmonization among the cantons<sup>16</sup>. For instance, the instructions set forth that private schools promote basic and further education and are thus of general public interest, however in order to be granted tax exemption they must act in a selfless way and may not be profit-oriented. The same principles apply to nursery schools or retirement and nursing homes. Youth organizations are considered to pursue a purpose of general public interest if their activities have mainly an educational and not only an entertaining character<sup>17</sup>. That distinction, however, may be rather difficult to draw.

As a second criterion, the organization's purpose must be of an *altruistic nature*. In practice, this second criterion raises many more questions than the first. This requirement implies the making of certain "sacrifices" that may consist of either financial sacrifices in the form of sponsors' donations to support the institution's purpose or personal sacrifices in the form of services rendered to the charitable organization without remuneration<sup>18</sup>. It is thereby irrelevant whether such sacrifices are made by the members or/and employees of the institution or even by third parties, as long as the altruistic performances are of considerable importance in relation to the institution's overall financial basis<sup>19</sup>.

The requirement of an altruistic nature of the organization's activity excludes from tax exemption any organizations that mainly pursue *self-serving purposes*<sup>20</sup>. For that reason, any association or institution pursuing objectives that are primarily in the interest of its members does not qualify for tax exemption. Such self-serving organizations include for example professional organizations representing the interests of a certain profession, as well as organizations that assemble members with similar interests, including sport, literature and debate clubs. The same principles apply to political parties and institutions whose activities, even if they fulfill an important task within a democratic system, are presumed to be of personal and economic interest primarily to their members and therefore lacking the character of disinterestedness<sup>21</sup>.

With regard to sport organizations, however, an exception is so far being made for international sport associations that are incorporated in Switzerland like the Union of European Football Associations (UEFA)<sup>22</sup> or the Fédération Internationale de Football Association (FIFA)<sup>23</sup>. These institutions have, upon instructions of the Federal Council, been declared tax exempted by the Federal Tax Administration on the grounds that international sport is contributing to international understanding and peace-building and

<sup>16</sup> Practical instructions to the cantonal tax administrations of 18 January 2008.

<sup>17</sup> Practical instructions to the cantonal tax administrations of 18 January 2008, para.9 (II).

<sup>18</sup> *Kuster*, Steuerbefreiung von Institutionen mit öffentlichen Zwecken, 203 et seq.; *Locher*, Kommentar zum DBG, Art. 56 n. 88.

<sup>19</sup> *Reich*, Gemeinnützigkeit als Steuerbefreiungsgrund, ASA 58 (1989/90), 465 et seq., 472.

<sup>20</sup> *Locher*, Kommentar zum DBG, Art. 56 n. 89; *Greter M.*, Art. 56 n. 31 et seq., in: Zweifel M./Athanas P. (eds.), Kommentar zum Schweizerischen Steuerrecht, I/2a, Bundesgesetz über die direkte Bundessteuer (DBG), Art. 1-82 (Basel/Genf/München: Hebling Lichtenhahn, 2008).

<sup>21</sup> Federal Supreme Court Decision of 2 April 2009, 2C\_77/2007; *Locher*, Kommentar zum DBG, Art. 56 n. 87; *Greter*, Art. 56 n. 40.

<sup>22</sup> UEFA has its seat in Nyon (Canton of Vaud).

<sup>23</sup> FIFA has its seat in Zurich.

is reinforcing positive messages such as fair play and the fight against racism and discrimination as well as the promotion of social and cultural integration<sup>24</sup>. The Federal Supreme Court, however, recently questioned the legality of the tax exemption of these international organizations<sup>25</sup>. The decision concerned the Swiss Equestrian Federation that requested tax exemption and asserted equal treatment to the exempted international organizations. The Federal Supreme Court ruled that even though the Swiss Equestrian Federation pursues certain purposes that are in the public interest such as the promotion of young athletes, the main purpose of the federation was to promote and support the interests of its members. The Federal Supreme Court thus denied an altruistic-natured purpose. With regard to the international sport organizations, the Federal Supreme Court invited the federal and cantonal tax administrations to reexamine their practices<sup>26</sup>.

The requirement of an altruistic-natured purpose for tax exemption also excludes any organizations that mainly pursue *business purposes*<sup>27</sup>. Business purposes are pursued whenever a legal entity participates in the market, whether as a competitor or a monopolist, with the intention of making profit and by charging market prices<sup>28</sup>. In cases where a non-profit organization operates as a valid competitor in the market, any tax exemption in its favor would constitute an unjustified improvement of its market position and infringe the principle of neutrality in competition<sup>29</sup>. In such cases, even if the organization's profit is exclusively and irrevocably dedicated to a charitable purpose, the organization will not be granted tax exemption. An exception applies only in situations where the business activity has merely an auxiliary character<sup>30</sup>. Further, it is possible to apply for a partial tax exemption if the organization keeps strictly separated books for its charitable activities and its profit oriented activities<sup>31</sup>.

According to the Swiss legislator, tax exemption is not limited to charitable organizations that carry out their activities within the boundaries of Switzerland, but includes *worldwide activities*, provided that the organization's purpose fulfills the requirements of general interest and altruistic nature<sup>32</sup>. In this context, the term "general interest" is considered from a Swiss perspective. Thereby, any foreign activities embodying the solidarity of Switzerland with the entire world are regarded as being in the general public interest of Switzerland<sup>33</sup>.

<sup>24</sup> Rundschreiben der Eidgenössischen Steuerverwaltung vom 12. Dezember 2008 über die Steuerbefreiung von internationalen Sportverbänden; Swiss Federal Council in its reply of 5 December 2008 to the Interpellation 08.3511 of 24 September 2008 by National Councillor Louis Schelbert.

<sup>25</sup> Federal Supreme Court Decision of 28 December 2010, 2C\_383/2010, Archiv für Schweizerisches Abgaberecht ASA 80 (2010/11), 207 et seq.

<sup>26</sup> Federal Supreme Court Decision of 28 December 2010, para 3.4, 2C\_383/2010, Archiv für Schweizerisches Abgaberecht ASA 80 (2010/11), 207 et seq.

<sup>27</sup> *Locher*, Kommentar zum DBG, Art. 56 n. 89.

<sup>28</sup> Circular letter no. 12 of 8 July 1994, para.II (3) (b).

<sup>29</sup> *Reich*, Gemeinnützigkeit als Steuerbefreiungsgrund, ASA 58 (1989/90), 465 et seq., 490.

<sup>30</sup> See for more details para. 2.2.3 below.

<sup>31</sup> See for more details para. 2.2.4 below.

<sup>32</sup> *Locher*, Kommentar zum DBG, Art. 56 n. 86.

<sup>33</sup> Practical instructions to the cantonal tax administration of 18 January 2008, para.5 (III).

Proof that the organization actually pursues a charitable purpose abroad must be established by adequate means<sup>34</sup>. Because of an inherent lack of control, purely foreign-based activities are for practical reasons still judged with a certain reserve by the cantonal tax administrations<sup>35</sup>. The practical instructions to the cantonal tax administrations require, among other measures, the monitoring of the annual financial statements and the financial transactions performed by and in favor of the institution, as well as a permanent control of the actual activity performed in order to verify that the conditions of tax exemption remain fulfilled<sup>36</sup>. Furthermore, the statutory bodies of the institutions are required to be constituted of trustworthy individuals of either Swiss nationality or at least with domicile in Switzerland<sup>37</sup>.

## 2.2.2 Public purposes (excursus)

In Switzerland, organizations pursuing public interests may be tax-exempted under the same requirements as organizations pursuing charitable interests. In contrast to charitable purposes, public purposes do not require any sacrifices to be made in favor of the community. However, business activities are still not allowed. Such organization must further fulfill a public service mission or pursue objectives that are inherently in the interest of the specific community.

## 2.2.3 Auxiliary business purposes

The prohibition for charitable organizations to carry out business activities is not always incompatible with its tax exemption<sup>38</sup>. Exceptions are approved if the principle of fair and neutral competition is not at stake. As a first example, auxiliary operations are regularly permitted for practical reasons, as long as they serve to support the charitable purpose, are clearly subordinated to the organization's non-profit purpose, and are of minor importance for the institution's budget<sup>39</sup>. Secondly, a business activity may also be permissible if it is indispensable for the realization of the organization's purpose, for instance in the case of training workshops linked to educational centers or facilities for mentally or physically disabled people<sup>40</sup>. Even in such cases, however, the business activity must be only a means to an end and constitute an element of minor importance

<sup>34</sup> Circular letter no. 12 of 8 July 1994, 3.

<sup>35</sup> *Frei W.*, Die Steuerbefreiungspraxis in der Zürcher Steuerpraxis, Zürcher Steuerpraxis ZStP 1993, 1 et seq., 9; *Locher*, Kommentar zum DBG, Art. 56 n. 86; *Koller T.*, Gemeinnützigkeits- und Spendenrecht in der Schweiz, in: Walz/von Auer/von Hippel (eds.), Spenden- und Gemeinnützigkeitsrecht in Europa (Tübingen: Mohr Siebeck, 2007), 441 et seq., 475.

<sup>36</sup> Practical instructions to the cantonal tax administrations of 18 January 2008, para.5 (V) (A).

<sup>37</sup> Practical instructions to the cantonal tax administrations of 18 January 2008, para.5 (V) (A).

<sup>38</sup> *Greter*, Art. 56 n. 33, in: Zweifel/Athanas, Kommentar zum Schweizerischen Steuerrecht, I/2a.

<sup>39</sup> *Kuster*, Steuerbefreiung von Institutionen mit öffentlichen Zwecken, 207. The practical instructions to the cantonal tax administrations of 18 January 2008 mention in para. 3 (IV) the example of a nursing home that additionally runs a cafeteria.

<sup>40</sup> *Kuster*, Steuerbefreiung von Institutionen mit öffentlichen Zwecken, 207.

within the altruistic purpose of the organization<sup>41</sup>. If these requirements are met, the income deriving from such auxiliary business activities is also exempted from tax.

The same applies to the acquisition and administration of a significant capital share in a company: Investments of this kind do not necessarily hinder tax exemption provided that the interest in the company is subordinated to the charitable purpose and no management functions are performed<sup>42</sup>. Even capital shares of more than 50% may be permitted as long as any direct influence on the board of the company is excluded, i.e. the charitable organization is not allowed to exercise any voting rights<sup>43</sup>. This requires in particular clear organizational and personal separation of the management of the non-profit organization on the one hand and the company's management on the other<sup>44</sup>. Any profits realized by the controlled company must, in addition, be substantially devoted to the charitable institution<sup>45</sup>.

If, on the contrary, the business activities or investments do not qualify as activities clearly subordinated to the charitable purpose, any income deriving from these undertakings is not exempted but remains subject to income tax.

#### **2.2.4 Partial tax exemption**

The requirement that a tax-exempted charitable organization may not pursue any profit-oriented activities does not *per se* prevent a charitable organization from carrying out a business. In such cases, i.e. if the business activities do not have only an auxiliary character, tax exemption is however restricted to the charitable purpose and the organization is obliged to keep strictly separated books for its charitable and profit-oriented purposes<sup>46</sup>. Further, a partial tax exemption will only be granted if the organization fulfills several formal conditions with regard to its separated accounting<sup>47</sup>.

#### **2.2.5 Irrevocable and exclusive dedication of the profit**

The funds of a tax-exempted charitable organization must exclusively and irrevocably be dedicated to the charitable purpose as set forth in its statutes. Accordingly, any distribution of profit to members of the institution or persons related to them must statutorily be excluded. Moreover, members of the charitable organization, i.e. the members of the board or the foundation council, are expected to act on a voluntary basis. Their work for the charitable organization must not be remunerated. According to common practice, however, adequate compensation for any expenses, including cash expenses, in connection with the activity for the organization as well as adequate remuneration for exceptional performances of individual members are considered

<sup>41</sup> *Locher*, Kommentar zum DBG, Art. 56 n. 91.

<sup>42</sup> *Greter*, Art. 56 n. 34, in: Zweifel/Athanas, Kommentar zum Schweizerischen Steuerrecht, I/2a.

<sup>43</sup> Circular letter no. 12 of 8 July 1994, para 3 (c).

<sup>44</sup> Circular letter no. 12 of 8 July 1994, para 3 (c).

<sup>45</sup> *Greter*, Art. 56 n. 34, in: Zweifel/Athanas, Kommentar zum Schweizerischen Steuerrecht, I/2a; Circular letter no. 12 of 8 July 1994, para. 3 (c).

<sup>46</sup> Circular letter no. 12 of 8 July 1994; *Locher*, Kommentar zum DBG, Art. 56 n. 83.

<sup>47</sup> Practical instructions to the cantonal tax administrations of 18 January 2008, para 11.

permissible<sup>48</sup>. Any compensation exceeding the adequate amount can, on the other hand, be considered as distribution of profit and as such compromise the organization's tax exemption<sup>49</sup>.

The requirement of exclusive dedication of the profit to the charitable purpose also comprises any liquidation proceeds. The organization's statute must irrevocably state that the liquidation proceeds must not be distributed to the members of the organization, but must be transferred to another tax-exempted organization that pursues similar purposes<sup>50</sup>.

The requirement of irrevocable and exclusive dedication of the organization's profits to the charitable purposes does not however prevent the organization from paying market-compatible salaries to their employees, provided that the employees are not themselves members of the organization. Furthermore, the payment of interests for loans or other capital borrowed from a third party is also permitted, provided that the lender has no economic connection to the institution as such.

The tax-exempted charity is not obliged to directly use its funds. Rather, it is principally entitled to forward its funds to other tax-exempted charitable organizations, even if they are situated abroad<sup>51</sup>. This is for instance the case of the organization "Swiss Solidarity" (Schweizerische Glückskette), a tax-exempted charitable institution that transmits all of its funds to other aid organizations situated in Switzerland or abroad. This practice is accepted by most cantons, even though a high standard of proof applies with regard to the charitable purpose of the foreign organization receiving funds from the Swiss tax-exempted organization. The foreign charitable organization must in principle fulfill the requirements for tax exemption according to Swiss tax law. The cantonal tax administrations may further require a certificate proving that the foreign organization is tax-exempted at its place of residence<sup>52</sup>.

### **2.3 Formal conditions for tax exemption of charities**

The formal procedure for applying for tax exemption in Switzerland is rather simple. The charity must submit its request for tax exemption to the competent cantonal tax authority. This application includes the request for exemption from federal as well as cantonal and communal corporate income taxation. The application documentation must include a signed copy of the organization's statutes and rules, the protocol of the founder's meeting as well as a description of the organization's activities and projects. Once the request is accepted, the tax exemption is generally not restricted to a certain period of time<sup>53</sup>. However, if the organization mainly carries out its charitable activities

<sup>48</sup> Practical instructions to the cantonal tax administrations of 18 January 2008, para 10.

<sup>49</sup> *Koller, Gemeinnützigkeits- und Spendenrecht in der Schweiz*, in: Walz/von Auer/von Hippel (eds.), *Spenden- und Gemeinnützigkeitsrecht in Europa*, 441 et seq., 460.

<sup>50</sup> *Locher, Kommentar zum DBG*, Art. 56 n. 84.

<sup>51</sup> *Koller, Gemeinnützigkeits- und Spendenrecht in der Schweiz*, in: Walz/von Auer/von Hippel (eds.), *Spenden- und Gemeinnützigkeitsrecht in Europa*, 441 et seq., 461.

<sup>52</sup> Practical instructions to the cantonal tax administrations of 18 January 2008, para 5 (I) (B).

<sup>53</sup> *Koller, Gemeinnützigkeits- und Spendenrecht in der Schweiz*, in: Walz/von Auer/von Hippel (eds.), *Spenden- und Gemeinnützigkeitsrecht in Europa*, 441 et seq., 476.

abroad, the competent cantonal tax authority may grant a limited tax exemption only<sup>54</sup>. The tax-exempted organization is further obliged to immediately report any changes of its factual situation, statute or activities to the tax authority. The tax authority is furthermore entitled to request for the organization's annual reports as well as annual financial statements, and may at any time require additional information<sup>55</sup>. How often and on what occasions such inspections are to be carried out depends on the concrete circumstances and practices of the cantonal tax authorities and differs considerably from canton to canton<sup>56</sup>.

## 2.4 Tax treatment of donors or contributors

Voluntary contributions made by individuals or legal entities to tax-exempted charities having their seat in Switzerland are deductible from the taxable income of the respective fiscal year as long as the total of all contributions does not exceed 20% of the contributor's net income and, in the case of individual donors and contributors, amounts to at least CHF 100.- per fiscal year<sup>57</sup>. The contributions may be made either in the form of cash or in any other asset of economic value, including all movable and immovable property as well as capital assets and industrial rights<sup>58</sup>. On the other hand, any service in the form of work performance rendered in favor of the charity is non-deductible. Any conversion of work performance with a hypothetical hourly wage and its subsequent deduction from the taxable income is thus excluded<sup>59</sup>. Further, only voluntary contributions are deductible. Contributions in the form of statutory membership fees or any other contribution to which the legal entity is entitled do not qualify as voluntary contributions according to the practice of the Federal Tax Administration<sup>60</sup>.

Only contributions made to a legal entity which benefits from tax exemption for pursuing charitable or public interests in the sense of Article 56 (g) FITA can be deducted. The legal entity must not necessarily be established before the contribution is made. Contributions made on the occasion of the establishment of a legal entity can also be deducted from the contributor's taxable income, provided that the legal entity,

<sup>54</sup> Practical instructions to the cantonal tax administrations of 18 January 2008, para.5 (V) (A).

<sup>55</sup> *Koller*, Gemeinnützigkeits- und Spendenrecht in der Schweiz, in: Walz/von Auer/von Hippel (eds.), Spenden- und Gemeinnützigkeitsrecht in Europa, 441 et seq., 475.

<sup>56</sup> *Koller*, Gemeinnützigkeits- und Spendenrecht in der Schweiz, in: Walz/von Auer/von Hippel (eds.), Spenden- und Gemeinnützigkeitsrecht in Europa, 441 et seq., 476.

<sup>57</sup> For individuals: Article 33a FITA and Article 9 (2) (I) FTHA. For legal entities: Art. 59 (1) (c) FITA and 25 (1) (c) FTHA.

<sup>58</sup> *Zigerlig R./Jud G.*, Art. 33a n. 4, in: Zweifel M./Athanas P. (eds.), Kommentar zum Schweizerischen Steuerrecht, I/2a, Bundesgesetz über die direkte Bundessteuer (DBG), Art. 1-82 (Basel/Genf/München: Hebling Lichtenhahn, 2008).

<sup>59</sup> *Zigerlig/Jud*, Art. 33a n. 4, in: Zweifel/Athanas, Kommentar zum Schweizerischen Steuerrecht, I/2a.

<sup>60</sup> Circular letter no. 12 of 8 July 1994, para. IV. According to the Swiss doctrine, however, membership fees of tax exempted institutions that exclusively serve purposes of public benefit should qualify as voluntary contributions and therefore be deductible from the taxable income: *Zigerlig/Jud*, Art. 33a n. 9, in: Zweifel/Athanas, Kommentar zum Schweizerischen Steuerrecht, I/2a.

after its establishment, is granted tax exemption<sup>61</sup>. Deductible contributions can also be made to institutions that only benefit from a partial tax exemption, however the fact that the contribution is exclusively used for the charitable purpose must be proven accordingly<sup>62</sup>. It is further incumbent upon the contributor to specifically make sure that the contribution exclusively serves the charitable purpose, whether by explicit instruction upon payment or by directly transferring the contribution to the account specifically set up for the charitable purpose<sup>63</sup>.

Finally, as indicated in the clear wording of the legal provisions, only contributions made to exempted legal entities having their seats in Switzerland are deductible from the taxable income. Contributions made to charities with seats abroad cannot be deducted. This restriction has been subject to criticism among Swiss scholars<sup>64</sup>. Namely, it is requested that the deductibility of contributions should be extended at least to those contributions made to foreign legal entities with tax-exempted permanent establishments in Switzerland<sup>65</sup>. Furthermore, it is maintained that contributions should be deductible if they are made to international organizations of which Switzerland is a member, even if their seats are not in Switzerland<sup>66</sup>.

Since Switzerland is not a member of the EU and since the free movement of capital is not part of the bilateral agreements between Switzerland and the EU, the ECJ jurisprudence on the deductibility of contributions made to foreign legal entities pursuing a non-profit purpose<sup>67</sup> is not binding for Switzerland. Considering the clear wording of the legal text, a change in legislation would be necessary in order to extend the deductibility to contributions made to charities with seats abroad. So far, however, no such attempt has been made.

### 3. VALUE ADDED TAXATION OF CHARITIES

Swiss VAT law generally follows the EU directive. According to Article 10 (1) Federal Law on Value Added Tax ("VATA")<sup>68</sup>, any person, irrespective of its legal form, objectives and intention to make a profit is liable for VAT if that person carries on a

<sup>61</sup> *Locher*, Kommentar zum DBG, Art. 33 n. 85; *Zigerlig/Jud*, Art. 33a n. 8, in: Zweifel/Athanas, Kommentar zum Schweizerischen Steuerrecht, I/2a.

<sup>62</sup> *Zigerlig/Jud*, Art. 33a n. 5, in: Zweifel/Athanas, Kommentar zum Schweizerischen Steuerrecht, I/2a.

<sup>63</sup> *Kuster*, Steuerbefreiung von Institutionen mit öffentlichen Zwecken, 289.

<sup>64</sup> *Koller T./Sennhauser N.*, Das EuGH-Urteil Persche aus der Sicht von Drittstaaten, insbesondere der Schweiz, in: Martinek/Rawert/Weitemeyer (eds.), Festschrift für Dieter Reuter zum 70. Geburtstag am 16. Oktober 2010 (Berlin: de Gruyter, 2010), 1061 et seq., 1082.

<sup>65</sup> *Zigerlig/Jud*, Art. 33a n. 5, in: Zweifel/Athanas, Kommentar zum Schweizerischen Steuerrecht, I/2a.

<sup>66</sup> *Richner F./Frei W./Kaufmann St./Meuter H.U.*, Handkommentar zum DBG (Zürich: Verlag Zürcher Steuerrecht, 2009), Art. 33a n. 9.

<sup>67</sup> ECJ, C-318/07, 27. January 2009, Hein Persche v. Finanzamt Lüdenscheid, ECR 2009, I-359.

<sup>68</sup> Bundesgesetz vom 12. Juni 2009 über die Mehrwertsteuer (Mehrwertsteuergesetz), SR 641.20.

business and is not exempt from tax liability. Generally exempted are persons who within one year generate on Swiss territory a turnover from taxable supplies of less than CHF 100'000. Charitable organizations as well as non-profit, voluntarily-run sporting or cultural associations are exempted if they generate on Swiss territory a turnover from taxable supplies of less than CHF 150'000 unless they waive exemption from tax liability. The term "charitable organization" is defined as a charity that fulfills the requirements of Article 56 (g) FITA<sup>69</sup>; in other words, the requirements as already described for an exemption from corporate income tax also apply to VAT. From a formal perspective, there is no special VAT procedure for being granted the status of a charitable organization. The tax exemption granted by the competent cantonal authorities for the federal corporate income tax is also accepted for VAT.

Very similar to the Article 132 VAT directive, Article 21 (2) VATA exempts several transactions from VAT, namely<sup>70</sup>:

- supplies that are made by social assistance and social security institutions, supplies by charitable nursing and home aid organizations and by retirement and nursing homes (Article 21 (2) (8) VATA);
- supplies related to child and youth care by institutions specially fitted for the purpose (Article 21 (2) (9) VATA);
- supplies closely related to cultural and educational development of young people by charitable youth exchange organizations (Article 21 (2) (10) VATA);
- the provision of staff by religious or philosophical non-profit institutions for purposes of treating the sick, social assistance and social security, child and youth care, and education and training, as well as for religious and charitable purposes and for the common good (Article 21 (2) (12) VATA);
- supplies that non-profit institutions with political, trade union, economic, religious, patriotic, philosophical, philanthropic, ecological, sporting, cultural or civic objectives provide to their members against a contribution laid down in statutes or regulations (Article 21 (2) (13) VATA); and
- publicity services, which charitable organizations provide for the benefit of third parties or third parties for the benefit of charitable organizations (Art. 21 (2) (27) VATA).

Exempted supplies do not count for the calculation of the taxable turnover, and, further, they do not entitle for input tax deduction. A charitable organization may thus choose to voluntarily opt for taxation of its exempted supplies<sup>71</sup>. According to a strongly criticized practice of the Federal Tax Administration, however, a charitable organization that decides to opt for taxation is only allowed to deduct its input taxation if it carries out a business. A person carries out a business if that person independently performs a

<sup>69</sup> Article 3 (j) VATA.

<sup>70</sup> MWST-Branchen-Info 22, Hilfsorganisationen, sozialtätige und karitative Einrichtungen, Januar 2010, para. 2 et seq. („sector information 22“).

<sup>71</sup> According to Article 22 (2) VATA, a few exempted supplies are excluded from option. Supplies that are specifically provided by charities are however not excluded from option.

professional or commercial activity with the aim of sustainably earning income from supplies<sup>72</sup>. In most situations these requirements are not fulfilled by a charity.

Donations do not qualify as taxable turnover<sup>73</sup>. According to Article 3 (i) VATA, the term “donation” means a voluntary contribution with the intention of enriching the recipient without expectation of a reward in the sense of VAT. A contribution also qualifies as a donation if the contribution is mentioned once or on several occasions in a publication in neutral form, even if the name or the logo of the donor is used. Contributions by passive members and by patrons to associations or to charitable organizations are equivalent to donations.

No donation is given, however, if the contributor expects a consideration of any kind from the non-profit organization. The Federal Supreme Court recently had to decide on the contribution made by patrons to the non-profit foundation Swiss Air Rescue (REGA). By registering as patron and making an annual contribution of at least CHF 30 for an individual and CHF 70 for a family, a patron will in the case of rescue not be charged with any fees. The Federal Supreme Court decided that the patrons’ contributions are not made without consideration and do not qualify as donations. Even though the financial support of the charitable organization may be the principal motivation for most of the patrons and even though a patron does not acquire an enforceable right to be rescued by the REGA, the Federal Supreme Court argued that the fact that the REGA promises in its published “Conditions of Patronage” a cost waiver for certain rescue services to its patrons does qualify the contributions as taxable supplies in the sense of the VATA<sup>74</sup>.

Further, according to Article 33 (1) VATA, donations do not result in a restriction of the input tax deduction. Thus, if a non-profit organization makes non-exempted and exempted supplies and additionally receives donations, the amount of the donations is not taken into account for calculating the input tax correction.

Cross-border supplies of goods of Swiss non-profit organizations are exempted from VAT, provided that the Swiss non-profit organization follows the required export formalities<sup>75</sup>. Cross-border services of Swiss non-profit organizations are in principle exempted as well, provided that the recipient of the service has its place of business abroad. Additionally, Article 8 (2) (g) states that in the case of services in the area of international development, cooperation and humanitarian help, the place for supply of the service is deemed to be the place where the service is destined.

#### **4. INHERITANCE, ESTATE AND GIFT TAXATION OF CHARITIES**

Legacies and gifts made to non-profit organizations may be subject to inheritance and gift taxation. In Switzerland, inheritance, estate and gift taxes exclusively underlie cantonal tax law. Concerning the exemption of charities from inheritance, estate and gift taxes, most cantonal laws either refer directly to the provisions on the exemption

<sup>72</sup> Article 10 (1) (a) VATA.

<sup>73</sup> Article 18 (2) (d) VATA.

<sup>74</sup> Federal Supreme Court Decision of 24 October 2011, 2C\_202/2011.

<sup>75</sup> Article 23 (2) VATA; sector information 22, para. 5.

from income taxation<sup>76</sup> or use terms identical to those used in the provisions on the exemption of income taxation<sup>77</sup>. Accordingly, the requirements for exemption from inheritance and gift taxes are in principal identical to those for the exemption from income taxation<sup>78</sup>. If the non-profit organization is entitled to claim exemption from income tax on the federal and cantonal levels, in most cases it is thus equally exempted from any inheritance and gift taxes on the cantonal level.

Concerning formal requirements, cantonal laws generally oblige any donee to declare any receipt of gifts to the tax administration within a certain period of time. Whether this applies to tax-exempted institutions as well depends on the respective cantonal regulations. Whereas some cantons provide for the tax-exempted institution's duty to categorically declare the receipt of any gifts<sup>79</sup>, others refrain from requiring such formalities from institutions that already benefit from tax exemption<sup>80</sup>. In the case of inheritance, generally no formal actions by the non-profit organization are required since the authorities usually act ex-officio. However, some cantons nevertheless require an additional declaration from the part of the heirs.

Specific rules exist in the context of trust arrangements. In Switzerland as in most other civil law countries, the concept of trust is not known. On July 1, 2007, Switzerland ratified the Hague Convention on the Law Applicable to Trusts and on their Recognition. Nevertheless, foreign trusts still do not constitute legal entities in Switzerland and therefore cannot be exempted from tax for pursuing purposes of charitable interests. Instead, wills, gifts and transfers of assets to and from trusts are taxed depending on the type of trust and trust arrangement, and underlie the specific cantonal and federal provisions on the treatment of trusts. In order to provide at least some degree of uniformity in the taxation of trust arrangements, the Swiss Tax Conference and the Federal Tax Administration have issued circulars<sup>81</sup> on the taxation of trusts for income tax purposes.

According to these circulars, due to its lack of legal personality the trust itself can never be subject to tax<sup>82</sup>. For the same reason, trusts cannot qualify as non-profit organizations within the meaning of the respective tax provisions. Likewise, the trustee and/or the protector are subject neither to taxation on the trust's assets nor on the

<sup>76</sup> This is the case, for instance, for the cantons of Zurich (§ 10 lit. f of the Inheritance and Gift Tax Act), Bern (Art. 6 (1) of the Inheritance and Gift Tax Act), and Basel (§ 120 lit. b of the Inheritance and Gift Tax Act).

<sup>77</sup> For instance in the canton of Geneva (Art. 6 (1) of the Inheritance Tax Act and Art. 28( 1) of the Registration Fee Act).

<sup>78</sup> *Koller*, Gemeinnützigkeits- und Spendenrecht in der Schweiz, in: Walz/von Auer/von Hippel (eds.), Spenden- und Gemeinnützigkeitsrecht in Europa, 441 et seq., 451.

<sup>79</sup> For instance in the canton of Berne.

<sup>80</sup> For instance in the canton of Zurich.

<sup>81</sup> Kreisschreiben Nr. 30 der Schweizerischen Steuerkonferenz zur Besteuerung von Trusts vom 22. August 2007; Kreisschreiben Nr. 20 der Eidgenössischen Steuerverwaltung über die Besteuerung von Trusts.

<sup>82</sup> Kreisschreiben Nr. 30 der Schweizerischen Steuerkonferenz zur Besteuerung von Trusts vom 22. August 2007, 7.

income deriving from the trust<sup>83</sup>. Rather, the circulars provide for taxation of either the settlor or the beneficiary of the trust, depending on the type of trust arrangement. Since tax exemption for corporate income and capital taxes on the one hand and inheritance and gift taxes on the other hand may only be requested by legal entities, trusts or their settlors or beneficiaries respectively who normally are individuals may not be granted tax exemption.

## 5. OTHER TAXES

All cantons levy a real estate capital gains tax and most of the cantons levy a real estate transfer tax and a real estate tax. Regarding the real estate capital gains tax, many cantons do not provide for an exemption of non-profit organizations<sup>84</sup>. Regarding real estate transfer taxes, on the other hand, tax exemption of non-profit organizations is principally known. In many cantons, however, the possibility of tax exemption is tied to the condition that the respective real estate is destined to be used for the charitable purpose<sup>85</sup>. The real estate itself is taxed only in some of the cantons with a real estate property tax<sup>86</sup>. Of these cantons, only a few foresee the possibility of tax exemption if the real estate is destined to serve the charitable purpose<sup>87</sup>.

Non-profit organizations that fulfill the requirements of tax exemption from federal corporate income tax are in principle exempted from issuance stamp<sup>88</sup>. Likewise, any goods donated to an exempted non-profit organization are customs-free, provided that the donated goods are appropriate in relation to the organization's purpose<sup>89</sup>. Vehicle taxes as well as excise taxes such as taxation of mineral oil, beer, alcohol or tobacco, to the contrary, do not specifically foresee exemptions for non-profit organizations.

Zurich, January 2012

<sup>83</sup> Kreisschreiben Nr. 30 der Schweizerischen Steuerkonferenz zur Besteuerung von Trusts vom 22. August 2007, 7.

<sup>84</sup> For instance the cantons of Zurich, Berne and Basel.

<sup>85</sup> For instance in the cantons of Berne, Basel and Geneva.

<sup>86</sup> For instance Berne, Lucerne, Geneva, St. Gallen and Ticino.

<sup>87</sup> For instance the cantons of Lucerne and Ticino.

<sup>88</sup> Art. 6 (1) (a) of the Federal Act on Stamp Duties (Bundesgesetz vom 27. Juni 1973 über die Stempelabgaben, SR 641.10)

<sup>89</sup> Art. 17 Customs Ordinance (Zollverordnung vom 1. November 2006, SR 631.01).