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Switzerland

With inheritance and gift taxes, 7.6% VAT on commercial transactions and on the import of works of art, Switzerland is certainly no tax haven, but it does have the free ports, where art can stay in "fiscal limbo" indefinitely

In Switzerland, taxes are levied on a federal, cantonal and communal level. With a few exceptions, there are no specific rules applicable to cultural goods. For tax purposes, business transactions with cultural goods are treated like transactions with any other goods and valuables. Income generated from the sale of cultural goods held as actual or deemed business assets is subject to income tax for individuals and corporate income tax for companies, while non-professional sales by private individuals are in general treated as tax-free capital gain. Possession of cultural goods is subject to wealth tax for individuals and capital tax for companies; however, certain exceptions apply to the possession of cultural goods by private individuals and tax-exempt institutions.
A recurring issue in tax matters regarding cultural goods is the assessment of the market value of cultural goods, which value serves as the basis for wealth, inheritance and donation taxes.

With regard to VAT, certain privileges apply to the sale and import of works of art. While sales of works of art by the artists themselves are exempt from VAT and import taxes, sales by galleries, art dealers and auction houses are subject to VAT. In the latter cases, however, VAT may be limited to the commission, margin or premium of the gallery, art dealer or auction house. The general VAT and import tax rate of 7.6% applies also to transactions with cultural goods. An exception applies to books, which are subject to a reduced rate of 2.4%. The Swiss government is currently simplifying its VAT rules. Many of the numerous VAT exceptions and privileges may be abolished in the interest of an easier VAT regime. This may eliminate certain VAT privileges applicable in the field of art described below. In return, the overall VAT rate of 7.6% may be reduced to a rate as low as 6.2%. It is not yet clear, when and to what extent these modifications will be introduced.

WEALTH TAX

In principle, cultural goods owned by individuals are taxable assets subject to wealth tax on a cantonal level. The tax rates range between 0.1% and 1.0%. Cultural goods owned by legal entities are subject to capital tax, which ranges between approximately 0.05% and 0.1%.

Some cantons exclude household effects, including furniture, carpets, books, silverware, paintings and objects of personal use from wealth tax. In these cases, a question arises regarding the extent to which works of art can be considered to constitute household effects used for furnishing. There are no clear rules on determining whether a cultural object is a taxable asset or a tax-exempt furnishing item. In general, tax authorities base their discretionary decision on a variety of criteria, including the examination of whether the cultural object was acquired for the purpose of decoration and furnishing or as an investment, whether the object is used and placed in the owner's living quarters or kept in storage, and whether the object is covered by the owner's general household insurance or by a separate and specific art insurance. In addition, tax authorities look at the relation in value between a tax payer's works of art, on the one hand, and, on the other hand, his or her other assets. The higher the net worth of assets, the higher the tolerance for appropriate furnishing, including works of art.

Prior to the enactment of federal rules on tax harmonisation, the canton of Geneva explicitly excluded art collections from wealth tax. With this background, the Genevan tax administration tends to maintain a liberal view in treating cultural goods as household effects exempt from wealth (and inheritance) tax.

For wealth tax purposes, the value of cultural objects is determined on the basis of market value. In many cases, it is obviously difficult to establish market value. Tax authorities tend to rely on the declarations made by taxpayers. The authorities also use insurance value as a point of reference. Collectors must thus be aware that the values used for insurance purposes may be relevant in determining market value for wealth tax purposes.

INCOME TAX

With respect to income taxes, a relevant distinction must be drawn between income resulting from professional selling and dealing with cultural goods on the one side, and profits (capital gains) resulting from a private sales by a private individuals (collectors) on the other side. Capital gains resulting from non-professional sales of cultural goods by private individuals are usually tax free, provided that the sold cultural good was not held, or deemed to be held, as a business asset (see "Capital Gains Tax"). In contrast, income generated from professional trading in cultural goods is subject to income taxes on a federal and cantonal level.

Income tax rates depend on a taxpayer's overall income. Depending upon the tax domicile, the combined federal and cantonal tax rate ranges between 20% and 42%.

Sales by legal entities are subject to corporate income tax at rates of approximately 15% to 30%, depending on the domicile, unless the entity has been granted tax free status due to its recognised charitable purposes. In addition, tax privileges may be granted to companies with no relevant business activities in Switzerland, such as companies established for the sole purpose of holding and managing collections of cultural goods.

SALES TAX

In Switzerland there is no sales tax other than VAT (see "VAT").

CAPITAL GAINS TAX

For individuals, no income taxes are levied in Switzerland on capital gains realised on the sale of valuables, including cultural goods. Profits from the sale of privately owned cultural goods are therefore exempt from income tax, provided that the sale was not aimed at generating income on a professional basis.

In contrast, profit resulting from the sale of cultural goods by companies or professionals is subject to tax.

The distinction between non-taxable private sales and professional activities aimed at generating income is a matter of debate. Swiss case law has developed certain criteria, which include the following:

- The number of transactions within a certain period of time. Regular and recurring sales of privately owned cultural goods will be considered to constitute a professional activity aimed at generating income.
- The period of ownership prior to sale. A long period of ownership and possession of a cultural object prior to its sale is a criterion for upholding a private sale.
- A systematic approach and sophisticated sales strategies as well as the availability and use of specific business know-how indicate a professional nature of a sale.
- The use of borrowed capital in a sales transaction is a strong indication of the professional nature of a sale.
- The reinvestment of proceeds from a sale into objects of a similar kind is considered to be a criterion indicating a professional rather than a private sale.

VAT

For Swiss VAT purposes, cultural goods are treated like any other goods. With a few exceptions, the ordinary rules governing the supply of goods and of services are applicable. Individuals or companies selling, buying or lending cultural goods for a fee, such as art galleries, art and antiquity dealers, auction houses, etc. fall within the definition of taxpayer for VAT purposes, provided that their annual turnover exceeds SFr75,000.

The applicable VAT rate is currently 7.6%, except for the sale and distribution of books, which is subject to a reduced rate of 2.4%.

Creators of artistic works, such as painters, sculptors, writers, composers, movie directors, etc. are exempt from VAT on the sale and distribution of works created by them. This exception also applies to works by art photographers, but not to photographs taken by advertising and press photographers.

In the case of sales by art galleries acting as intermediaries for artists on a commission basis, VAT will not be levied on the entire amount of the gallery's sale price, but only on the gallery's commission.

In addition, art galleries and dealers in artworks, collectables and antiquities more than 100 years old may benefit from a so-called "margin-system", according to which VAT is levied on the difference between the purchase price paid by the gallery or art dealer when buying an object and the proceeds (resale price) received by the gallery or art dealer when reselling the object. A variation of the margin-system applies in situations in which a gallery or art dealer buys a multitude of art works (eg, an entire lot of works by the same artist) in one transaction. In this case, the gallery or art dealer may request that VAT

SWITZERLAND GETS TOUGH ON ILLICIT TRADING AND MONEY LAUNDERING

Switzerland has liberal legislation regarding the possession and transfer of cultural goods. In fact, there are no particular regulations regarding the possession of cultural goods. However, Switzerland recently signed the Unesco Convention on the Prevention of Illicit Import, Export and Transfer of Cultural Property and enacted a law on the international transfer of cultural goods (Swiss Federal Act on the International Transfer of Cultural Property). The new act introduced certain rules on due diligence for the art trade, collectors and museums.

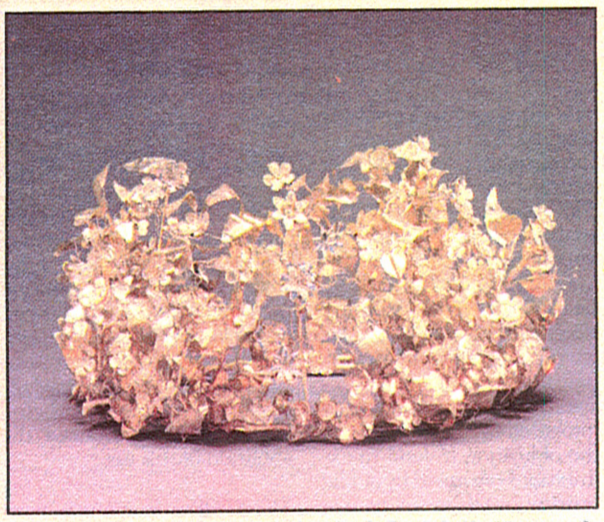
Art dealers must identify sellers (but not buyers) and keep certain records regarding the provenance and particulars of business transactions. As a rule, cultural property may only be transferred if the person effecting the transfer can safely assume, under the circumstances, that the object was neither stolen nor illegally excavated or imported. Persons selling, buying or transferring cultural objects must act with caution and must investigate any circumstances that raise doubts regarding the provenance of the cultural object.

There are no restrictions on the export of cultural goods owned by private individuals or legal entities. Export bans are limited to certain objects owned by the Swiss Confederation or by the Swiss cantons and registered in specific public registries. In contrast, reporting duties and restrictions apply to the import and transfer of cultural property.

The new act has also introduced rules on the repatriation of illegally exported cultural goods; these have not yet been tested and are applicable only under limited conditions.

Most importantly, the new act does not apply to all and any kind of artworks, but only to cultural objects of particular importance to archaeology, prehistory, history, literature, art or science. As a rule of thumb, the term "particular importance" implies cultural objects "worth exhibiting in a museum", or objects whose loss would constitute a loss for cultural heritage, as well as objects of particular interest to the general public.

In addition to the federal act, some cantons have enacted rules on the protection of their cultural property. These rules are applicable on a cantonal level, but are in practice of little relevance.



This funerary wreath, bought by the J. Paul Getty Museum in the 1990s, and claimed as an illicit export by the Greek government, passed through the Swiss market

When there is the suspicion that cultural goods and/or the proceeds of their sale might have illicit origins, the financial intermediaries, eg banks, are obliged to inform the Money Laundering Reporting Office Switzerland (MROS).

The Swiss government is analysing how to introduce the new version of the 40 OECD-FATF/Financial Action Task Force Recommendations 2003 concerning the extension to art dealers, auction houses, etc, of the same duty to prevent money laundering as the financial intermediaries.

Upon request of foreign judicial criminal authorities in favour of criminal proceedings regarding stolen goods, the Swiss criminal judicial authorities may seize cultural goods and order their restitution to the requesting foreign authorities.

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be assessed on the difference between the price paid for the lot and the aggregate proceeds resulting from the resale of individual pieces of the lot.

If cultural goods are sold by auction houses, VAT is usually levied only on the buyer's and seller's premium. However, in the event that an item is sold at auction on behalf of a Swiss dealer subject to VAT, VAT is charged on the final bid price plus the premium. If the item sold at auction has been imported, auction houses tend to charge the import tax/VAT to the buyer (see "Import and Export Taxes").

GIFT TAX

In most cantons, the rules and tax rates applicable to donations are similar, if not identical, to the rules and tax rates for inheritance taxes (see "Inheritance Tax").

The threshold of tax-free *de minimis* donations is usually low (around SFr10,000).

In principle, the tax is payable the recipient of the donation. However, there is a vicarious liability by the donor in cases where the tax cannot be levied on the recipient, eg, when a recipient is domiciled abroad.

For donations to tax-exempt institutions, see "Transfer to Cultural Institutions".

Regarding the determination of a donation's value (ie the valuation of the donated cultural object), the same rules apply as for wealth tax purposes.

INHERITANCE TAX

Inheritance taxes are levied by the cantons. Depending on the last residence of the deceased, the tax burden may vary considerably. A few cantons do not levy any inheritance tax at all (Schwyz) while the other cantons (except Basel, Neuchâtel, Solothurn, St Gallen, Thurgau) do not levy inheritance tax on direct descendants.

Frequently, the tax rate will depend on the degree of kinship between the deceased and the heirs. The rates are usually in the range of 0% to 53%.

In some cantons, furniture and household effects are partly or entirely exempt from inheritance tax. This raises similar issues regarding cultural objects as we have seen with wealth tax (see "Wealth Tax").

The valuation of cultural objects for purposes of inheritance tax is subject to the same rules as for wealth tax.

In the case of large art collections, the heirs are often forced to sell part of the collection to fund the inheritance tax.

Two cantons (Geneva and Jura) allow for the payment of inheritance taxes through donations to the canton of works of art of particular artistic, historic or scientific importance (so-called *dation en paiement*).

TRANSFERS TO CULTURAL INSTITUTIONS

Switzerland modified its legislation as of 1 January 2006 on donations to tax-exempt institutions. Donations to tax-exempt institutions may be deducted from income on a federal level. The deduction is limited to 20% of the taxable net income of individuals. Donations are not only deductible if made in cash, but also if made in kind (eg, the donation of works of art or of intellectual property rights or the rendering of services). The same rules of exemption apply to donations made to institutions that are only partly tax-exempt, ie; that engage both in charitable and non-charitable activities.

On a cantonal level similar rules apply. However, the cantons may adopt a higher or lower percentage of the allowable deductions than the 20% applicable on the federal level.

IMPORT AND EXPORT TAX

Pursuant to international agreements, such as the Unesco Lake Success Convention on the Import of Goods of an Educational, Scientific or Cultural Nature of 22 November 1950, Switzerland does not levy any customs duties on paintings, drawings and sculptures. Etchings and lithographs are exempt if they are numbered and produced by a non-mechanical method on the basis of plates etc created by the artist. For works of art which are not exempt, such as, for instance, unnumbered lithographs, the customs duties are generally modest, since they are calculated according to the weight of the object. If the artworks are imported by the artists themselves they are exempt from customs duties.

While there are generally no custom duties levied on the import of cultural goods, such imports are subject to import taxes/VAT at a rate of 7.6% (2.4% for books). Two exceptions apply: no taxes are levied on works of art and collection items imported for the purpose of public display. Also, no taxes are levied on imports by or on behalf of painters and sculptors with respect to works of art created by them.

It is relevant to note that, with respect to import taxes, the scope of the exception for artists is much narrower than the VAT exception granted to artists for domestic sales. While the VAT exception on an artist's domestic sales is broad in scope and applies to all kinds of artistic creators and their works (see above, under "VAT"), the exception for the purpose of import tax applies only to painters and sculptors with respect to the import of their "personally created works of art". The exception applies to works where colour is put on a base, including hand-coloured photographs, collages, multiple prints, serigraphs, lithographs, etc. if these are signed and the number of copies is limited, as well as to any form of plastic art, but not to photographic art, video art or computer-generated art and not to functional items created by artisans.

In cases of import for sales or commission purposes, the tax is assessed on the basis of the sales price or the commission. In all other cases, the tax is determined on the object's market value.

Objects intended to remain in Switzerland for a limited period only (temporary import) may be imported tax free and exempt from VAT under a so-called "free pass". Some sort of collateral (bank guarantee, bond) may be required, except in the case of temporary imports by museums. The same rules apply if a work of art is to be imported for sale, and if the sale is uncertain. If a work of art is imported under a free pass, the VAT and customs duties become due only after the sale has been effected or if the duration of the free pass has expired without the object having left Switzerland.

There are no export taxes for the export of cultural goods.

DROIT DE SUITE

There is no droit de suite (artists' resale charge) in Switzerland. However, the Swiss Copyright Act is currently under revision. There is considerable pressure from royalty collecting agencies supporting the introduction of resale charges on works of art by living artists and by deceased artists until 70 years after their death. The charges would be levied on sales in the secondary market, ie, upon reselling art works after the first sale by the artist or gallery. In its recent draft bill to parliament, the Swiss government did not include droit de suite. It is likely that parliament will decide the matter during 2006/2007.

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This article is intended only to give a general overview. For detailed information, consult your professional adviser.

The most inaccessible museum in the world

In terms of taxation, free ports are limbo. There are free ports in every corner of the globe, though none arouses such curiosity as the one in Geneva.

Referred to by some as "the largest museum in the world", for many art experts, dealers and collectors this is often the only place in Switzerland they know.

Its importance should however be kept perspective: it is not even the only free port in Switzerland, and indeed the more discreet free port in Zurich is preferred by some. And the no less than 15 others in Switzerland include those in Basel and Chiasso.

The history of the Geneva free port dates back to 1850, when customs barriers were of great importance and duties extremely high. For this reason, the Federal Council—the tutelary authority of Switzerland—granted the canton of Geneva the right to its own free port.

It is based on a very simple principle: economic goods are placed within brackets, so to speak, so far as Customs are concerned. This means that goods can remain "in transit" for any length of time between two Customs areas without any duties being payable on them. For example, a painting from New York can remain in Swiss territory in a free-trade area without tax being paid on it, and can then be officially imported into Switzerland or forwarded to any country in the EU, or, indeed, any other geographical area.

This can be extremely convenient during negotiations in which the seller does not know at the outset where his work of art will eventually end up.

The free port of Geneva is physically located in two different places: one near the airport, the other close by the city in the Praille district.

The two areas of the free port are enormous—over 140,000 sq.m.—and their turnover, derived almost solely from rental fees, amounts to over SFr20 million per year.

Surprisingly, these facilities are used only to a limited extent by the art world, occupying 13% of the surface area. Jewellers account for another 3%, which is proportionately a huge amount, considering the small size of their objects. Carpets take up only 1% of the total, a very modest figure if one bears in mind that at the time of the Shah almost the entire production of Persian carpets passed through Geneva. Another surprise is that two million bottles of wine transit through the free port.

The famous Geneva free port breeds fantasies about what marvels of great art it may contain

The great majority of items in the warehouses are, in fact, more prosaic commercial goods such as cars, computers, furniture and chemical products.

Another important aspect is that, for reasons of convenience, the free-port premises are divided into a part controlled by Customs and a part that is normally accessible to all for goods that have already had clearance.

Just in case anyone thinks this is a law-less no man's land, Swiss Federation officials, the Customs and the cantonal police may not only check everyone at the entry and exit points to the free port, but can also access all premises under Customs control.

Stolen works of art therefore do not find a haven within the free port and, since Switzerland is about to implement the 1970 Unesco Convention, the local authorities will be able to investigate the true provenance of works of art without having to wait for for them to be officially imported into Switzerland.

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