

Taxation of Trusts, Foundations and Similar Arrangements in a Global Setting

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CHAPTER 11

Wealth Taxes and Wealth Planning: The Role of Foundations

Peter Hongler & Subiksha Thirumamany

1 INTRODUCTION

The following chapter aims to provide an overview of the treatment of foundations for wealth tax purposes. A particular goal is to demonstrate whether wealth tax systems are able to cope with the challenges raised by using foundations as tax planning instruments. While general observations are made without tying the discussion to a specific jurisdiction, the primary focus is on legal practice in our home country, Switzerland—for reasons set out below.

As it is well known, Switzerland is one of the very few countries with a more or less comprehensive wealth tax regime. Moreover, Switzerland has a highly developed philanthropy sector and is of global importance for international charitable organizations.¹ This status is attributed not only to its liberal legislation but also to its favorable tax framework.² While foundations are in general subject to privileged corporate income taxation, charitable foundations are even tax-exempt.³ At the same time, however, the institution of a family foundation to support family members is considered unpopular in Switzerland, as the law imposes rather strict restrictions. Switzerland even knows a ban on pure family maintenance foundations.⁴

1. For an overview, see *Der Schweizer Stiftungsreport 7* (Julia Jakob, ed., 2023), Center for Philanthropy Studies (CEPS), University of Basel, <https://www.swissfoundations.ch/publikationen/der-schweizer-stiftungsreport-2023/> (accessed July 5, 2024).

2. See *supra* Chapter 6.

3. CH: Art. 59 lit. g Federal Act on Direct Federal Taxation (Bundesgesetz über die direkte Bundessteuer (DBG; SR 642.11)).

4. Already criticized at the time by Michael Hamm and Stefanie Peters, *Die schweizerische Familienstiftung: ein Auslaufmodell?* *successio* 250 et seq., 256 (2008); see also Andrea Opel and

This provides an interesting legal framework to discuss to what extent foundations undermine the proper functioning of a wealth tax regime.

2 STRUCTURE

The chapter is structured as follows: We begin with a brief example to highlight the issues raised in relation to wealth taxation and foundations (section 3). Next, we provide a concise overview of the Swiss tax system, with a particular emphasis on the wealth tax (section 4). In this section, we explain the structure of a wealth tax system and conduct a comparative international analysis. Following this, we present the Swiss legal framework governing foundations, distinguishing between domestic and foreign foundations (section 5). The discussion then moves to the various tax consequences in relation to foundations (section 6). Building on these fundamentals, we explore wealth tax planning strategies in Switzerland, focusing specifically on the role of foundations (section 7). Finally, we will assess whether wealth tax systems should enable the transfer of assets into a non-taxable cloud, e.g., to a foundation, and provide our conclusions.

3 AN EXAMPLE TO START

Every tax system needs to deal with the question of who is taxed on what items of income and if there is a wealth tax, who pays the wealth tax on a specific asset items. With regard to wealth taxation, it is crucial for the tax system to determine the point at which a transfer of ownership occurs for tax purposes. Concerning foundations, this means the following steps on a timeline need to be regulated:

- (1) Person A transfers an asset item (e.g., shares) to the foundation B.
- (2) Foundation B holds the asset for a few years.
- (3) Foundation B transfers the same asset to the recipient C.

Wealth taxes are in general only levied on individuals. Therefore, it could happen that for a period of time (especially during [2] above), the assets are not allocated to anyone (i.e., they remain in a cloud) although they were and will sooner or later be held by individuals.

This example demonstrates that foundations can create a challenge for wealth tax systems as they might undermine the effective taxation of wealth by creating a cloud for an intermediate transfer of wealth. As we will see throughout the chapter, this is particularly true for family and private foundations, i.e., foundations, *inter alia*, used for transferring assets from one generation to the next.

Stefan Oesterhelt, *Zukunft für die Schweizer Familienstiftung: Anpassungsbedarf in zivilrechtlicher und steuerrechtlicher Hinsicht*, 118 SJZ 955, 963 (2022); Sherin Kneifl, *Familienstiftung soll modernisiert werden und eine Alternative zum Schweizer Trust bieten*, 120 SJZ 89, 89 (2024).

4 FUNDAMENTALS OF A WEALTH TAXATION

4.1 The Swiss Tax System

Before discussing the Swiss wealth tax in more detail, it is essential to understand the structure of the Swiss tax system. Switzerland as a federal state is known for its decentralized and federal structure and consists of twenty-six cantons and around 2,131 municipalities. This federal structure means that taxes are levied at three levels: the federal, cantonal, and municipal level.

When it comes to the tax authority across the different levels, the Federal Constitution stipulates that the cantons (and thus also the municipalities) are sovereign in all areas unless their sovereignty is explicitly restricted by the Federal Constitution.⁵ Consequently, each canton has the autonomy to establish its own tax laws and rates. Municipalities can impose taxes based on the tax sovereignty derived and delegated by the cantons.

However, not every tax is levied at three levels. The value-added tax and withholding tax on income from movable assets are, for instance, levied exclusively at the federal level, while income tax is imposed at federal, cantonal and municipal levels. The wealth tax is only levied at cantonal and municipal level.⁶

Despite these differences, income and wealth tax overlap in terms of tax liability, as they are based on the same underlying rules. This ensures a consistent assessment and taxation of both income and wealth across all levels of government. Furthermore, the Swiss Federal Constitution contains a harmonization provision for direct taxes in the sense that the federation shall establish principles to ensure consistency in areas such as tax liability, tax objects and the tax period, procedural law, and laws regarding tax offenses.⁷ The alignment of several tax principles not only reinforces the coherence of the tax system but also allows for regional variation in tax rates and policies.

4.2 Income and Wealth Tax Liability

The Swiss income and wealth tax system differentiates between limited and unlimited tax liability. Unlimited tax liability means that worldwide income of an individual is subject to income taxation except for places of business, permanent establishments, and real estate abroad.⁸ It can be either triggered by a tax abode in Switzerland or a tax domicile in Switzerland.⁹ A tax abode exists if the taxpayer stays in Switzerland for at least thirty days and pursues a gainful activity, or for at least ninety days without such

5. See CH: Constitution, Art. 3 (Bundesverfassung der Schweizerischen Eidgenossenschaft (BV; SR 101)).

6. See Art. 123(1) BV for the federal competence; besides CH: Art. 13(1) Federal Act on Tax Harmonization (Bundesgesetz über die Harmonisierung der direkten Steuern der Kantone und Gemeinden (StHG; SR 642.14)), the respective cantonal provision can be found in one of the 26 cantonal tax laws.

7. See Art. 129 BV.

8. See Art. 6(1) DBG.

9. Article 3(1) DBG.

activity. A tax domicile, on the other hand, applies if the taxpayer intends to stay in Switzerland for an indefinite period of time or if federal law grants a specific legal residence in Switzerland.¹⁰ In the case of economic affiliation, the taxpayer is liable only for income subject to limited tax liability.¹¹ However, the applicable tax rate shall be calculated based on the worldwide income of the taxpayer.¹²

Importantly, the same principles apply for wealth tax purposes. This means that a person subject to an unlimited income tax liability is also subject to unlimited wealth tax liability, except for assets attributable to foreign business operations or permanent establishments and real estate held abroad. A person becomes subject to limited wealth tax liability if the person owns real estate in Switzerland or has a permanent establishment or business operation in Switzerland.

4.3 The Swiss Wealth Tax

The Swiss wealth tax has a rich historical background and in fact predates the modern income tax. Until the start of World War I, the wealth tax was the main tax in Switzerland.¹³ Today, it is considered as a supplementary tax to the general income tax and has a certain control function with regard to the income tax by comparing the assets declared by the taxpayer in successive tax periods.¹⁴ Furthermore, while Switzerland does not tax private capital gains, it effectively compensates for this through the levying of an annual wealth tax.¹⁵ However, annual wealth tax and capital gains tax are not economically equivalent and produce different effects.

Wealth taxation applies both to individuals residing in Switzerland with unlimited tax liability and to non-residents with limited tax liability in Switzerland, typically arising from real estate, business operations, or a permanent establishment within the country.¹⁶ As previously mentioned, there is no federal wealth tax; however, the Federal Tax Harmonization Act (StHG) mandates that the cantons levy a comprehensive wealth tax. The Act also outlines certain requirements regarding the structure and implementation of this tax. According to Article 13(1) StHG, the object of wealth tax is the total net assets, defined as the excess of assets over liabilities of a taxable person.¹⁷ This means that existing debts, such as mortgages or private loans, are fully deductible.¹⁸

10. See Art. 3(3) DBG.

11. See Art. 6(2) DBG.

12. See Art. 7 DBG.

13. Peter Hongler and Fabian Mauchle, *Is Switzerland a Role Model for Wealth Taxes?*, 97 Tax Notes Int'l 645, 653 (2020).

14. SSK, *Tax information Dated April 2021 Regarding Wealth Taxes on Individuals* (2021), 1, available in German at, <https://www.estv.admin.ch/estv/de/home/die-estv/steuersystem-schweiz/dossier-steuerinformationen.html> (accessed August 15, 2024).

15. Peter Hongler and Matthias Valta, *International Perspectives on Wealth Taxation*, IFF Working Paper 14, 18 (2021), also published in German: Peter Hongler and Matthias Valta, *Internationale Perspektiven der Vermögensbesteuerung*, 90 Stuw, 6 et seq., 16 (2021).

16. Articles 3 and 4 StHG.

17. CH: Federal Supreme Court Decision 2C_874/2018 dated April 17, 2024, cons. 12.1.

18. SSK, *supra* n. 14, 21.

The two most important categories of wealth to be disclosed in the tax return are securities and real estate. Household items, like kitchen tables or beds, are not subject to wealth tax.¹⁹ However, valuable items such as an expensive painting in the living room are not considered part of the household and are therefore taxable.²⁰ Additionally, wealth transferred into the social security system is exempt from cantonal wealth taxation.²¹ The StHG also specifies that usufructuary assets are to be allocated to the usufructuary on a pro rata basis.²²

With respect to the valuation, assets are generally assessed at their market value.²³ However, under Article 14(3) StHG, moveable business assets held by a self-employed person are to be valued at book value. As we will see later, such exception can also be used for tax planning purposes.

Cantons are free to determine their applicable wealth tax rate, meaning an individual's overall tax burden depends on both their canton and municipality of residence. This highly decentralized system fosters local tax competition also for wealth tax purposes.²⁴ Wealth taxes are direct taxes, assessed through a mixed procedure, where the taxpayer has to file his tax return along with a declaration of wealth, which is then assessed by the authorities.

Legal entities are not subject to the Swiss wealth tax; instead, they are subject to a capital tax, which essentially functions as a wealth tax for corporations, levied on their net equity.²⁵ Partnerships, however, are generally treated as transparent in Switzerland, meaning that their assets are attributed proportionately to the individual partners or members for tax purposes.²⁶

4.4 Comparative Analysis

As we have outlined at a different instance, wealth taxes can be structured in a variety of forms. Depending on the tax system, this structure can range from a tax on single assets, such as real estate, to a comprehensive wealth tax, i.e., a tax on all assets owned by a taxpayer.²⁷ However, even if a country chooses a comprehensive system, certain exemptions are common: For example, assets held in pension or life insurance accounts are often excluded from the tax base, as are household items in some cases.

19. Article 13(4) StHG.

20. See CH: Decision of the Zurich Administrative Court SR.2011.00019 dated March 9, 2012 regarding the Giacometti painting.

21. See CH: Art. 84 Federal Act on Occupational Pension Schemes (Bundesgesetz über die berufliche Alters-, Hinterlassenen- und Invalidenvorsorge (BVG; SR 831.40)).

22. See Art. 13(2) StHG.

23. See Art. 14(1) StHG.

24. Ulrich Cavelti and Bernhard J. Greminger, *10 Jahre Steuerharmonisierung*, 79 Archiv für Schweizerisches Abgaberecht, 447 et seq., 478 (2010/2011); Florian Scheuer and Joel Slemrod, *Taxing Our Wealth*, 35 J. Econ. Persps., 211, 230 (2021) <https://doi.org/10.1257/jep.35.1.207> (accessed May 28, 2025).

25. See Art. 29 StHG.

26. Hannes Teuscher and Frank Lobsiger, in *Kommentar zum Schweizerischen Steuerrecht, Bundesgesetz über die Harmonisierung der direkten Steuern der Kantone und Gemeinden (StHG)* Art. 13 n. 3 (Martin Zweifel and Michael Beusch eds., 2022).

27. Hongler and Valta, *supra* n. 15, 7 et seq.

Moreover, exemptions or reduced rates might be foreseen for one's primary real estate or more generally, the rules for wealth tax might differ between real estate and financial assets.²⁸

Over the decades, many countries have abolished their wealth tax regime. Within the OECD, the number of states knowing wealth taxes decreased from twelve to four between 1990 and 2017, leaving France, Norway, Spain and Switzerland.²⁹ Norway and Switzerland have chosen a rather comprehensive wealth tax as in general all assets are subject to the wealth tax.³⁰

Other countries have chosen a more limited scope.³¹ France, for instance, converted its wealth tax into a real estate tax.³² The Netherlands does not levy a wealth tax either but replace it equivalently with a deemed income tax.³³ In Germany the wealth tax has been the subject of an ongoing debate over decades.³⁴ In 1995, the Federal Constitutional Court declared the wealth tax levied at that time to be unconstitutional because real estate and property assets were treated unjustifiably more favorably than other types of assets.³⁵ Despite this, the Wealth Tax Act has neither been reformed nor repealed; the federal government simply allowed the wealth tax to expire.³⁶

In Spain, as in Switzerland, wealth taxation has been delegated to subcentral governments, which have the legislative power to define certain aspects of its framework.³⁷ However, to mitigate the wealth tax burden, Spanish legislation has introduced a list of exemptions over the years, such as business assets, pensions plans or even main residences.³⁸

28. Scheuer and Slemrod, *supra* n. 24, 209.

29. See OECD, *The Role and Design of Net Wealth Taxes in the OECD* No. 26 (April 12, 2018) 16, https://www.oecd.org/en/publications/the-role-and-design-of-net-wealth-taxes-in-the-oecd_9789264290303-en.html (accessed August 10, 2024).

30. For Norway, see 4-1 of the Norwegian Income Tax Act.

31. For an overview see Hongler and Valta, *supra* n. 15.

32. The so-called *impôt sur la fortune immobilière* applies to all individuals with a net worth more than EUR 1,300,000, see Arts. 964 et seq. of the French General Tax Code (CGI).

33. Hongler and Valta, *supra* n. 15, 14.

34. For a detailed historical background, see Victor von Kommer and Lambert F. Kusters, *Möglichkeiten der Wiedereinführung der Vermögensteuer in Deutschland und denkbare Alternativen*, Kurzgutachten zu Optionen einer Reform der Vermögensteuer in Deutschland, erstellt im Auftrag des Wirtschafts- und Sozialwissenschaftlichen Instituts (WSI) in der Hans-Böckler-Stiftung, 3 et seq. (2013).

35. See DE: Decision Federal Constitutional Court BVerfG dated June 22, 1995, 2 BvL 37/91 BVerfGE 93, 121.

36. Johanna Hey, Ralf Maiterth and Henriette Houben, *Zukunft der Vermögensbesteuerung*, 20 (2012).

37. José María Durán-Cabré, Alejandro Esteller-Moré and Mariona Mas-Montserrat, *Behavioural Responses to the (Re)introduction of Wealth Taxes. Evidence from Spain*, IEB Working Paper, 1, 70 (2019).

38. See Art. 4 of Act 19/1991 regarding the Spanish Wealth Tax Act.

5 FOUNDATIONS UNDER CIVIL LAW

In the following sections, we will analyze the treatment of domestic and foreign foundations from a civil law perspective, as this will be crucial in determining the tax consequences.

5.1 Domestic Foundations

The foundation is conceptually a legal entity that is removed from the will or decisions of its governing bodies, beneficiaries, and even—once it has been established—its founder.³⁹ Therefore, it is also described as a personalized special-purpose asset, constituting a distinct category of legal entities under Swiss federal private law.⁴⁰ In order to establish a foundation, assets must be dedicated to a specific purpose,⁴¹ whereby the purpose of foundations varies greatly. Here, a distinction is made between the “classical” foundation (i.e., in particular nonprofit foundations) which is primarily regulated in Articles 80 et seqq. ZGB and special foundations such as the family foundation under Article 335 ZGB or the ecclesiastical foundation.⁴²

In each case, the foundation acquires legal personality upon entry in the commercial register.⁴³ In addition, classic foundations are subject to supervision by the authorities with the exception of family and ecclesiastical foundations.⁴⁴ Mixed foundations are also possible, which are described as hybrid forms between family or church foundations or private or charitable foundations.⁴⁵ After all, the foundation deed—especially the stated purpose—determines how the foundation is classified.⁴⁶

Due to the lively discussions and the relevance of this chapter, it seems appropriate at this point to delve into the topic of family foundations. By law, family foundations are limited in their purpose to the extent that they are established solely to meet the costs of educating, equipping or supporting family members or for similar purposes.⁴⁷ Accordingly, family maintenance foundations (*Unterhaltsstiftungen*) are prohibited if they grant benefits from the foundation’s assets to the beneficiaries without any special conditions linked to a particular situation in life, simply to enable them to have a higher or more comfortable standard of living.⁴⁸ As a result, Swiss law does not allow for a legal structure that enables estate assets to be tied up long term in a single legal entity without shareholders, in which family members are beneficiaries in

39. Hans Michael Riemer in *Berner Kommentar zum schweizerischen Privatrecht, Die Stiftungen Art 80-89c ZGB*, Erster Teil: Systematischer Teil n. 37 (2020).

40. Riemer, *supra* n. 39, Erster Teil: Systematischer Teil n. 22.

41. See CH: Art. 80 Swiss Civil Code (Schweizerisches Zivilgesetzbuch (ZGB; SR 210)).

42. Riemer, *supra* n. 39, Erster Teil: Systematischer Teil n. 154.

43. See Art. 52(1) ZGB.

44. See Art. 87 ZGB.

45. Riemer, *supra* n. 39, Erster Teil: Systematischer Teil n. 441.

46. This is because the foundation deed or the disposition on death is decisive for the establishment of a foundation, see Art. 81(1) ZGB.

47. See Art. 335(1) ZGB.

48. Art. 335(2) ZGB; see also CH: Federal Supreme Court Decision BGE 108 II 393 cons. 6.

a broad or comprehensive sense.⁴⁹ This restriction has been criticized on several occasions and has been described as outdated in the face of international competition.⁵⁰ In December 2022, Thierry Burkart, a member of the Council of States, submitted a motion calling for the ban on maintenance foundations to be lifted in order to strengthen Swiss family foundations.⁵¹ The motion received clear majority support, passing in the Council of States in December 2023 and in the National Council in February 2024. As a result, the Federal Council is now obligated to present a draft bill within two years.⁵² Conversely, the motion to introduce trusts into Swiss law was rejected, with the Federal Council arguing that the case for liberalizing family foundations is more compelling.⁵³ As the possible introduction of Swiss trusts was under discussion at the time, the motion was rejected by the Federal Council in September 2023.⁵⁴

5.2 Foreign Foundations

Given the lack of flexibility in the Swiss Civil Code regarding the establishment of (family) foundations, foreign foundation vehicles are frequently used as an alternative. However, the question of recognition of the foreign foundation arises if the settlor, beneficiaries and assets such as estate are located in Switzerland.

Under Swiss private international law the legal system under which a legal entity was established is generally the decisive one.⁵⁵ Consequently, companies and foundations are governed by the law of the state where they are organized, provided they adhere to that country's publicity or registration requirements. This approach, known as the *incorporation theory*, has two restrictions: A company established under foreign incorporation law whose de facto registered office is in another country can be denied legal personality if this violates the Swiss public policy.⁵⁶ This reservation also applies

49. Olaf Gierhake and Natalie Peter, *Einsatzszenarien von liechtensteinischen Stiftungen und stiftungsähnlichen Zweckvermögen unter dem neuen DBA Schweiz: Liechtenstein*, 70 StR, 630, 649 (2015); Opel and Oesterheldt, *supra* n. 4, 952.

50. *See supra* n. 4.

51. *See* motion (22.4445) of Member of the Council of States Thierry Burkart "Die Schweizer Familienstiftung stärken. Verbot der Unterhaltsstiftung aufheben" of December 15, 2022, <https://www.parlament.ch/de/ratsbetrieb/suche-curia-vista/geschaefte?AffairId=20224445> (accessed June 10, 2024).

52. For the status of the negotiations, *see ibid.*

53. *See* Explanatory report of the Federal Council of January 12, 2022 on the opening of the consultation procedure on the introduction of the trust: Amendment of the Code of Obligations, 32 et seq., <https://www.admin.ch/gov/de/start/dokumentation/medienmitteilungen.msg-id-86746.html> (accessed August 30, 2024).

54. Report on the repeal of motion 18.3383 of the Legal Affairs Committee of the Council of States "Einführung des Trusts in die schweizerische Rechtsordnung" from September 15, 2023, <https://www.parlament.ch/de/ratsbetrieb/suche-curia-vista/geschaefte?AffairId=20183383> (accessed June 10, 2024); for an overview *see also* Kneifl, *supra* n. 4, 89.

55. CH: Art. 154(1) Federal Act on Private International Law (Bundesgesetz über das Internationale Privatrecht (IPRG; SR 291)).

56. This is the so-called reservation of the *ordre public* according to Art. 17 IPRG.

if there is no separation between the company's assets and the personal assets of the partners, which can be particularly risky for foundations.⁵⁷

Additionally, overriding mandatory rules of Swiss law and foreign intervention norms may still apply, regardless of the corporate law governing the company.⁵⁸ However, this rule does not apply to mandatory provisions of Swiss company law, as doing so would undermine the incorporation theory.⁵⁹

It also implies that the abovementioned prohibition of family maintenance foundations under Article 335(2) ZGB does not fall under this restriction and, therefore, does not apply to foreign foundations.⁶⁰ Liechtenstein, in particular, imposes no such limitations, which is why family maintenance foundations are common there.⁶¹ It is generally accepted that Liechtenstein family foundations do not violate public policy and are thus recognized under Swiss civil law, regardless of their form and purpose.⁶²

6 FOUNDATIONS UNDER TAX LAW

The taxation of a foundation essentially depends on its recognition as a taxable entity and its underlying purpose. Thus, according to Article 59(1) DBG, legal entities, including foundations that pursue public or charitable purposes, are tax-exempt.⁶³ The law also indicates that a corporate purpose does not qualify as charitable; however, a partial tax exemption is possible if the corporate purpose plays a subordinate role to the charitable activity.⁶⁴ The following analysis will explore the tax implications of domestic and foreign foundations that do not pursue a public or charitable purpose.

6.1 Domestic Foundations

In principle, foundations are taxed as legal entities in the same way as corporations pursuant to Article 49(1) lit. b DBG and Article 20(1) StHG. In this context, tax law links the definition of a legal entity to the provisions of private law under Articles 52 et seqq.

57. Jolanta Kren Kostkiewicz, in *Orell Füessli Kommentar zum Bundesgesetz über das Internationale Privatrecht (IPRG) und zum Lugano-Übereinkommen (LugÜ)* Art. 154 N 6 (2019).

58. See Arts. 18 et seq. IPRG, which are also called *lois d'application immédiate*.

59. CH: Federal Supreme Court Decision BGE 117 II 494 cons. 7.

60. CH: Federal Supreme Court Decision BGE 135 III 614 cons. 4.3; for a detailed analysis of the case law see Peter Fröhlich, *Die kontrollierte Stiftung: Rechtssicherheit und Realität!*, 72 StR, 273, 283 (2017).

61. See FL: Art. 552 § 2(4) no. 1 Federal Act of Personal- and Company law (Personen- und Gesellschaftsrecht (PGR; 261.0)).

62. As already mentioned, Art. 335(2) ZGB does not qualify as *lois d'application immédiate* under Art. 18 IPRG (see *supra* s. 5.2); see also CH: Federal Supreme Court Decision 2C_527/2022 dated November 24, 2022, cons. 4.3.

63. See also Art. 23(1) lit. b StHG; for the detailed requirements see ESTV, *Circular letter No. W95-012D Dated July 8., 1994 on the requirements for tax exemption due to charitable status and public purposes*, <https://www.estv.admin.ch/estv/de/home/direkte-bundessteuer/fachinformationen-dbst/dbst-kreissschreiben.html> (accessed August 5, 2024).

64. See Art. 56 lit. g DBG.

ZGB.⁶⁵ The dedicated assets and income are taxed at the foundation level, not at the founder's level, resulting in corporate income and capital taxes.⁶⁶

However, Swiss tax law grants some relief for foundations: First, foundations benefit from privileged tax rates at both federal and cantonal levels.⁶⁷ Second, contributions to a foundation's assets, whether made by the founder or third parties, are excluded from taxable corporate income.⁶⁸ However, the deductibility of distributions from foundations to beneficiaries as business-related expenses remains undecided by the Swiss Federal Supreme Court.⁶⁹ Foundations also enjoy the same participation relief as corporations.⁷⁰

Given these privileges, it is unsurprising that establishing a foundation offers significant tax-saving opportunities for individuals. When a founder transfers assets to a foundation, those assets are no longer subject to wealth tax, and income is no longer subject to income tax. However, since foundations are recognized as legal entities, they are still subject to capital tax.⁷¹ The tax assessment for foundations is based not on equity capital listed in the tax balance sheet (which is the case for corporations), but on net assets, calculated in accordance with the rules that apply to individuals.⁷² Net assets represent the sum of all assets minus all liabilities, with wealth tax regulations guiding their calculation and valuation.⁷³ Depending on their purpose, foundations may even be fully exempt from capital tax, although they may still be subject to real estate gains tax.⁷⁴ Additionally, if a foundation is situated in a tax-favorable canton and considering the application of the participation relief, there is substantial potential for tax planning, though this comes with a risk of abuse.

A foundation can be deprived of its subjectivity under tax law for civil law reasons.⁷⁵ This is the case, for example, if the founder retains the same unrestricted control over the foundation's assets as over his or her personal funds, thereby maintaining a separate pool of assets that cannot be reached by third parties, creditors, or tax authorities.⁷⁶ The purpose of the foundation is precisely the dedication of the

65. Peter Locher, Ernst Giger and Andrea Pedrolin in *Kommentar zum Bundesgesetz über die direkte Bundessteuer, Teil II: Art. 49-101 DBG*, Art. 49 n. 4 (Peter Locher et al. eds., 2022).

66. Philipp Betschart in *Kommentar zum Schweizerischen Steuerrecht, Umstrukturierungen* §14 n. 1 (Martin Zweifel et al. eds., 2022).

67. According to Art. 71(1) DBG, the profit tax for foundations is only 4.25% of the net profit, while for corporations and cooperatives it is 8.5 % of the net profit. The article also states that profits under CHF 5,000 are not taxed; for the various cantonal special tax rates see Betschart, *supra* n. 66 §14 N 8.

68. See Art. 66(1) DBG and art. 26(1) StHG.

69. CH: Federal Supreme Court Decision 2A.668/2004 dated April 22, 2005, cons. 2.4.

70. See Art. 69 DBG.

71. For more details on capital tax, see s. 4.3.

72. Article 29(2) lit. c StHG.

73. Articles 13-14a StHG, see *supra* Chapter 4, s. 4.2.

74. Article 23 StHG.

75. See, e.g., CH: Federal Supreme Court Decision BGE 140 II 255 cons. 4.1. et seq.; CH: Federal Supreme Court dated April 22, 2005 2A.668/2004, cons. 3.4.2; CH: Federal Supreme Court Decision BG 73 II 81 cons. C; but decided differently in CH: Federal Supreme Court Decision BGE 93 II 439 cons. 3c.

76. See CH: Federal Supreme Court Decision BGE 140 II 255 cons. 5.3.

assets in favor of a special purpose.⁷⁷ This suggests that the donated assets are no longer under the control of the founder and have their own independent legal personality.⁷⁸ The tax authority can determine such unlawfulness on a preliminary basis without examining the criteria for tax avoidance.⁷⁹

Tax authorities have the authority to preliminarily assess the validity of a foundation under civil law, though their jurisdiction is limited to obvious and serious defects that could render the foundation null and void. Until then, even an unlawful or immoral foundation remains a taxable entity for the tax authorities as long as it has not been formally dissolved by a civil court.⁸⁰

6.2 Foreign Foundations

Foreign entities are treated as equivalent to domestic legal entities they most closely resemble, either legally or factually.⁸¹ It is therefore essential to distinguish between corporations and cooperatives on the one hand and associations, foundations, and other legal entities on the other. The classification based on legal criteria generally relies on the typical formal characteristics of the foreign entity.⁸²

However, the criterion of substance is relevant as well, emphasizing that the actual attributes of the foreign companies are crucial. Therefore, it is important to examine the actual activities carried out by the company.⁸³ Whether a foreign legal form is recognized as a “foreign legal entity” depends on its civil law characteristics, with previously discussed incorporation theory serving as the guiding principle.⁸⁴ However, the civil law qualification in the foreign jurisdiction does not automatically result in an equivalent tax treatment in Switzerland.⁸⁵

Once the foreign foundation is acknowledged, its income from donated assets is taxed at the foundation level rather than at the founder’s level.⁸⁶ Thus, a foreign foundation is treated in the same non-transparent way as the domestic foundation.⁸⁷ This applies in particular if the founder no longer controls the foundation and the beneficiaries do not have fixed entitlements (so-called uncontrolled foundation with no

77. See Art. 80(1) ZGB.

78. CH: Federal Supreme Court Decision BGE 140 II 255 cons. 4.1.

79. CH: Federal Supreme Court Decision BGE 140 II 255 cons. 5.4.

80. CH: Federal Supreme Court Decision BGE 140 II 255 cons. 5.4; see also CH: Federal Administrative Court BVGer B-951/2020 dated August 16, 2021, cons. 6.

81. Article 49(3) DBG and Art. 20(2) StHG.

82. The Liechtenstein establishment (*Anstalt*) was thus categorized as similar to a foundation, and the indications pointing in the direction of a corporation were regarded as secondary by the lower court, see CH: Federal Supreme Court 2C_564/2017 dated April 4, 2019, cons. 4 et seq.

83. CH: Federal Supreme Court 2C_564/2017 dated April 4, 2019, cons. 5.4.1.

84. Stefan Oesterhelt and Susanne Schreiber, in: Zweifel and Beusch, *supra* n. 26, Art. 20 n. 71; for the relevance of the terms under private law for tax law see CH: Federal Supreme Court Decision BGE 140 II 255 cons. 3; for incorporation theory see *supra* 5, s. 5.2.

85. The issue arises with hybrid entities that are classified as legal entities under foreign civil law but are treated as fiscally transparent under foreign tax law, see CH: Federal Supreme Court 2C_895/2013 dated September 18, 2015, cons. 31.

86. See *supra* Chapter 3, s. 3.2.

87. For the tax implications see *supra* s. 5.1.

predetermined distribution mechanism).⁸⁸ As a result, a “shielding effect” on income and assets can be achieved with foreign foundations—unlike an irrevocable discretionary trust set up in Switzerland, where its assets and income continue to be attributed to the Swiss founder for tax purposes.⁸⁹

However, if it turns out that the civil law structure is invalid or void, the tax-relevant facts have not materialized.⁹⁰ The intended transfer of assets from the founder to the foundation, which was supposed to occur with the dedication of the assets, did not actually take place. Consequently, the assets remain legally attributed to the founder under civil law, and this attribution must also be recognized for tax purposes.⁹¹

Even a foundation that has been validly established under civil law can still be treated transparently for tax purposes. However, if a foreign jurisdiction applies transparent taxation, this does not alter the foundation’s civil-law status abroad, nor does it override its classification under Swiss law pursuant to Article 49(3) DBG and Article 20(2) StHG.⁹² Cantonal practices and the case law of the Federal Supreme Court vary significantly in this regard:

The Federal Supreme Court utilizes the concept of so-called “pass-through” concept for structures when the individuals involved are suspected of abusing the organization for tax avoidance purposes.⁹³ It is particularly relevant when the foundation is closely tied to an individual, and the economic interests of the legal entity and the person controlling it are essentially aligned.⁹⁴ In such scenarios, the legal independence of the entity can be disregarded, allowing direct access to the individual behind it. The assets and income of the foundation are not attributed to the foundation itself but rather the economically dominant person—namely the founder or beneficiary—with corresponding income and wealth tax implications.⁹⁵ This examination of the pass-through is based on the criteria of tax avoidance.⁹⁶ However, each situation must be assessed on its own merits; it cannot be assumed that foundations controlled by an individual are automatically treated transparently.⁹⁷

88. Stefan Oesterhelt and Andrea Opel, *Statuswechsel von liechtensteinischen Familienstiftungen*, EF 487, 494 (2021); however, this form has disadvantages with regard to inheritance and gift tax, see Maja Bauer-Balmelli and Nils Olaf Harbeke, 5 *Die Liechtensteinische Stiftung im Schweizer Steuerrecht*, zsis Monatsflash, s. 7.3 (2009).

89. See for Trusts ESTV, *Circular letter No. 20 Dated March 27, 2008 on the taxation of trusts*, s. 5.2.3., <https://www.estv.admin.ch/estv/de/home/direkte-bundessteuer/fachinformationen-dbst/dbst-kreisschreiben.html> (accessed August 5, 2024).

90. For the restrictions under civil law see *supra* s. 5.2.

91. Fröhlich, *supra* n. 60, 280.

92. Frank Roth, Sybille Fankhauser and Maxi Müller, *Steuerliche Behandlung einer US S-Corporation in der Schweiz*, EF 183, 187 (2023); Andrea Opel, *Familienstiftung und Trust—Postulat für eine kohärente Besteuerung*, 78 ASA 270, 288 (2009).

93. CH: Federal Supreme Court 2C_527/2022 dated November 24, 2020, cons. 4.3; CH: Federal Supreme Court 2C_826/2019 dated March 17, 2020, cons. 5.3.1; CH: Federal Supreme Court 2C_711/2012 dated December 20, 2012, cons. 4.1.

94. CH: Federal Supreme Court 2C_527/2022 dated November 24, 2020, cons. 4.5; CH: Federal Supreme Court 2C_638/2010 dated March 19, 2012, cons. 4.1.

95. Oesterhelt and Opel, *supra* n. 88, 489.

96. CH: Federal Supreme Court 2C_638/2010 dated March 19, 2012, cons. 4.1.

97. See CH: Federal Supreme Court Decision 5C.201/2001, cons. 2c.

In general, the cantons also apply transparent treatment to these so-called controlled foundations. However, they take it a step further: In certain cases, some cantons assume transparent treatment of foundations regardless of the tax avoidance criterion.⁹⁸ For instance, tax recognition is usually denied if the founder retains control over the foundation, as from an economic standpoint, as there is no effective reduction in the founder's wealth.⁹⁹ When the criteria for a controlled foundation are met, the foundation assets are attributed to the individual who—alongside the foundation board or other legal bodies—exercises control over the foundation. The exact practice might differ from canton to canton; only two cantons have published guidelines for the transparent treatment of foreign foundations.¹⁰⁰

The transparent treatment of a foreign foundation in Switzerland brings forth tax delineation challenges. This issue is particularly significant in an international context, where a foundation might be recognized as a taxable entity under foreign law but not under Swiss law. This discrepancy raises concerns about tax jurisdiction over the foundation's income and assets, potentially leading to the risk of double taxation.¹⁰¹

7 WEALTH TAX PLANNING IN SWITZERLAND

7.1 Overview

Although Switzerland knows a comprehensive wealth tax, there are some wealth planning options to reduce the wealth tax burden. At least the following instruments are used in practice:

- Transfer of wealth to a foreign *permanent establishment*: As Switzerland unilaterally exempts both income and wealth attributable to a permanent establishment, the wealth tax burden can be reduced by transferring wealth to a foreign permanent establishment.¹⁰² This could, for instance, mean that a person rents an office in a foreign country and employs several persons managing his or her wealth so that the requirements of permanent establishment are fulfilled. However, authorities apply a high threshold to accept such a planning option and these structures have also been challenged in court.¹⁰³
- Transfer of funds to a foundation as discussed in this contribution.

98. See further Fröhlich, *supra* n. 60, 276; Hans Jürg Steiner, Sibylle Fankhauser and Eric Brügger, *Transparente Behandlung juristischer Personen in der Schweiz*, EF 532, 536 (2019).

99. Betschart, *supra* n. 66, §14 N 2; Oesterhelt and Opel, *supra* n. 88, 487.

100. See “Praxisfestlegung ‘Familienstiftungen’” dated April 15, 2013 of the Canton of Graubünden, <https://www.gr.ch/DE/institutionen/verwaltung/dfg/stv/dokumentation/praxis/PraxisEinkommenVermogen/16-01-01.pdf> (accessed August 4, 2024), as well as the “Steuerbuch Steuerverwaltung St. Gallen ‘ausländische Stiftungen’” dated April 23, 2009 of the Canton of St. Gallen, https://www.sg.ch/content/dam/sgch/steuern-finanzen/steuern/steuerbuch/art-70-104-stg/070_1.pdf (accessed August 4, 2024); for a detailed analysis of cantonal case law see Fröhlich, *supra* n. 60, 276 ff.

101. On the international issue, see in particular Steiner, Fankhauser and Brügger, *supra* n. 98, 533.

102. See Art. 6(1) DBG.

103. See CH: Federal Supreme Court Decision 2C_707/2016 dated March 23, 2018, cons. 2.4.1. et seq.

- Transfer of funds to a trust: Trusts are used as a pre-immigration tool for tax planning. The reason being that irrevocable but discretionary trusts are a way of reducing the wealth tax burden but only if the settlor is not yet a tax resident in Switzerland.¹⁰⁴ This means that the transferred assets to the trust will not anymore be recognized as assets of the settlor.
- Transfer of private assets into the business sphere of an individual. This does include transfer of assets to a self-proprietorship (but not to a company). In this case, the assets are valued at book value and in general no annual revaluation is necessary. Therefore, over time, taxpayers can reduce their tax burden as the book value will not necessarily reflect the fair market value. However, it is important to consider that this comes at a price as assets in the business sphere are subject to a capital gains taxation, whereas in the private sphere these gains are exempt from income taxation.
- Wealth as part of certain pension schemes is not subject to the wealth tax:¹⁰⁵ Therefore, by transferring funds into a pension scheme, the wealth tax burden can be reduced. As pension schemes are highly regulated, this option knows its limits. For instance, there are maximum amounts of contributions and limitations on when a repayment of these contributions can be initiated.
- A last but very prominent example is the lump-sum tax regime: A person subject to the lump-sum tax regime pays a wealth tax but only a deemed amount and not on the actual global wealth.¹⁰⁶

While not a matter of tax planning per se, a systemic reason why declared wealth may fall short of actual fair market value lies in the valuation methods applied—particularly for real estate and unlisted shares—which often result in structural underestimations. There might be further opportunities to reduce the wealth tax burden (e.g., through certain fund structure).¹⁰⁷ The present contribution, however, focuses on the role of foundations.

7.2 How Large Is the Wealth Tax Gap?

To date, there are no detailed studies about how large the wealth tax gap is—that is, the amount of wealth that remains untaxed but would be subject to taxation under a fully effective and comprehensive wealth tax. However, comparing the declared wealth and calculations by more popular sources indicates that the gap might be significant.

104. See ESTV, *supra* n. 89.

105. See Art. 84 BVG.

106. We are not outlining the calculation in detail. See, for instance, the practice in the Canton of Lucerne, https://steuern.lu.ch/natuerlichepersonen/besteuerung_aufwand (accessed August 23, 2024).

107. In particular funds owning real estate directly might create planning opportunities, see Art. 49(2) DBG; see also ESTV, *Circular letter No. 25 Dated February 23, 2018 on the Taxation of collective investment schemes and their investors*, s. 3.3.

According to the popular magazine *Die Bilanz*, the richest three hundred persons have a wealth of approx. CHF 800 billion.¹⁰⁸ In contrast, publicly available data shows that the richest twenty thousand taxpayers have declared a combined wealth of “only” around CHF 770 billion.¹⁰⁹ There seems to be a considerable wealth tax gap.

Of course, parts of it can be traced to methodological differences: According to the calculations of the journal *Bilanz*, wealth of some families is consolidated (i.e., several taxpayers might count as one), and the journal looks for publicly available information (i.e., they are not referring to taxpayer data). While such factors explain some variance, these calculations remain very rudimentary and partly flawed.

8 SHOULD THERE BE WEALTH IN THE CLOUD?

8.1 In General

We assume that a comprehensive wealth tax should in very general terms ensure that non-taxed wealth does not exist unless there is a clear macroeconomic purpose or another justification. The reason is that a wealth tax has the purpose of taxing persons depending on their wealth and any deviation from such purpose needs to be justified. This brings us back to some of the planning opportunities above. Some of them have rather a clear purpose:

- For instance, ensuring that wealth attributable to a trust before the relocation has the purpose of being attracting for UHNWI who want to relocate to Switzerland. Of course, whether this is justified depends on the line of argumentation. For instance, one position would be that the welfare increases in Switzerland due to these relocations are larger than the impact lower tax payments have.
- The non-taxation of wealth attributable to foreign permanent establishments or the non-taxation of foreign real estate¹¹⁰ could be justified by a variety of systematic reasons. One would be that this would create a significant administrative burden as tax authorities would need to assess in more detail the value of these assets abroad. Second, it could be argued that the risk of double taxation would be higher. The latter risk, of course, depends on whether other states indeed still know a wealth tax.
- The particular calculation of the wealth tax for persons subject to lump-sum taxation could be justified as Switzerland aims to be attractive for relocation of UHNWI to Switzerland. Historically, it was sometimes argued that the burden of the authorities would be significant to calculate the tax in these situations.

108. See *Bilanz, Die 300 Reichsten, Guide für die Reichstenliste* (23 Nov. 2023), <https://www.handelszeitung.ch/bilanz/der-guide-fur-die-reichstenliste-547821> (accessed August 20, 2024).

109. See <https://www.bfs.admin.ch/bfs/de/home/statistiken/wirtschaftliche-soziale-situation-bevoelkerung/einkommen-verbrauch-vermoegen/vermoegen.html> (accessed August 23, 2024).

110. See *supra* Chapter 4, s. 4.2.

In the next section, we will particularly focus on the question of whether exempting wealth transferred to certain foundations is justified.

8.2 Foundations in Particular

As with any other measures that make certain investments more attractive, policymakers should assess whether exempting wealth transferred to a foundation is justified from a macroeconomic perspective. Besides macroeconomic justifications for exempting wealth transferred to foundations from wealth taxation, there is of course always the legal argument that in case of genuine transfers of wealth to foundations, the wealth does not anymore belong to the property of the taxpayer and, therefore, should not be taxed in the hands of the taxpayer. We will distinguish in the following the case of nonprofit foundations and private or family foundations.

There is a broad variety of literature about the macroeconomic impact of the nonprofit sector in general.¹¹¹ The main argument is that exempting the nonprofit sector from taxation might create spillovers for the whole society. Moreover, with nonprofit foundations, the risk is minimal that they are misused as a cloud to place wealth for a certain period of time in order to reduce the wealth tax burden.

With respect to private foundations, the justification is more challenging as also tax planning opportunities are more obvious. The line of argumentation for providing an attractive tax environment by excluding transferred assets from the wealth tax could be as follows. It might enable a more liberal transfer of assets to the heirs by enabling more opportunities on when and how wealth is transferred to the next generation. The question of course is whether other means (e.g., a more liberal inheritance law) could not create similar incentives. Moreover, depending on the civil law background, it could also enhance asset protection against the state which in some circumstances might indeed be justified. The analysis is also different if the wealth planning sector is itself an important sector of the economy. This might be the case for Liechtenstein. Therefore, by granting an attractive tax regime to foundations by exempting the transferred wealth from the wealth taxation, the entire wealth tax planning sector becomes more attractive.¹¹²

All of these arguments would need to be balanced with the loss in tax revenue and should be assessed in a democratic process. We should not underestimate the fact

111. See, e.g., Richard Steinberg, Chapter 23: Nonprofit organizations and the macroeconomy in *Handbook of Research on Nonprofit Economics and Management*, 442-460 (Bruce A. Seaman and Dennis R. Young eds., 2018); K.V. Bagmet, Olena Haponova, *Assessing the Impact on Social Sector: A Macroeconomic Approach*, 2 SocioEcon. Challenges 103-108 (2018) [https://doi.org/10.21272/sec.3\(2\).103-108.2018](https://doi.org/10.21272/sec.3(2).103-108.2018) (accessed May 28, 2025); on the philanthropic sector see, e.g., Nathalie Monnet and Ugo Panizza, *A Note on the Economics of Philanthropy*, Working Paper, Graduate Institute of International and Development Studies, International Economics Department 1-34 (2017); Lilly Family School of Philanthropy, *The Philanthropy Outlook 2024 & 2025*, <https://philanthropy.indianapolis.iu.edu/research/latest/index.html> (accessed August 20, 2024); Richard Michon and Atul Tandon, *Emerging Philanthropic Markets*, 17 Int'l J. Nonprofit. Vlty. Mktg. 352-362 (2012) <https://doi.org/10.1002/nvsm.1435> (accessed May 28, 2025).

112. See also on the tax incentives from an economic perspective Monnet and Panizza, *supra* n. 111.

exempting wealth transferred to foundations from wealth taxation can undermine the effectiveness of a wealth tax system in general. This is particularly true if foundations can be misused as clouds in order to place assets temporarily. Therefore, it seems very challenging to commit to a comprehensive wealth tax while simultaneously allowing for a reduction of the wealth tax burden through the transfer of assets into family or private foundations.

We are unable to provide a final answer within this contribution to the concerns raised. However, what does seem evident is that the justification for offering a wealth tax exemption for contributions to nonprofit foundations differs fundamentally from the rationale for offering the same tax treatments to private or family foundations.

Lastly, there is always a more technical debate about when a tax system can really assume that wealth or income is attributable to the taxpayer. In case of a nonprofit foundation with no involvement of the donor, it might be very difficult to technically argue that wealth is still attributable to a person. The case is of course different for private and family foundations which are still partly controlled (even *de facto*) by the settlor.

9 CONCLUSION

This contribution has shown that foundations cause a significant challenge for wealth tax systems. As the introductory example demonstrated, this is particularly the case when they enable the transfer of wealth from one individual to another individual while temporarily escaping the wealth tax regime. Wealth tax regimes must deal with such challenges.

Essentially, it boils down to the question of whether a wealth tax system should enable the transfer of assets into a “cloud” and whether sufficient measures are in place to challenge such structures. As it was outlined, the Swiss approach is based on applying anti-avoidance measures by at the same time emphasizing the control aspect, i.e., whether the settlor still has a *de jure* or *de facto* control over the assets and in particular whether the foundation can be revoked.

We have argued that in case a country aims at a comprehensive taxation of wealth, deviations from such approach need to be justified in particular by macroeconomic reasons, be it, for instance, the exemption and proactive acceptance of nonprofit foundations. For family foundations, however, it is much more challenging to justify that a transfer of wealth to such a foundation is also accepted for wealth tax purposes. Therefore, a more liberal treatment of family foundations from a civil law perspective, as it is currently discussed in Switzerland, could pose a significant challenge to the effectiveness of the Swiss wealth tax system and may not necessarily be justifiable.

