Switzerland

How Swiss companies should apply the income tests for FATCA classification purposes


Ferdinando Mercuri and Adam Jagusiewicz, Deloitte

As for most Swiss banks the review of individual accounts is practically reaching its end under their due diligence procedures, the time has come to enquire about the entity client status under FATCA.

For entities like Swiss banks, broker-dealers, asset managers, or insurance companies offering cash value or annuities contracts, the answer is rather easy as these entities fall under one of the FATCA categories of foreign financial institutions (FFI). What about a non-listed operating company, Company C, with premises and staff engaged in a commercial (non-financial) business for more than 30 years, which has granted to a professional asset manager a mandate to partially manage its cash and financial assets on a discretionary basis and deriving from this activity an important financial income: is such entity an FFI or a non-financial foreign entity (NFFE)?

Under the applicable FATCA regulations in Switzerland, if an entity's gross income is primarily attributable to investing, reinvesting or trading in financial assets because such entity's financial assets are managed for such purposes by another FFI which through its management activities derives over the last three years (or the period during which the entity has been in existence) 50% or more of financial income, then such entity qualifies as an FFI (investment entity). In other words, for Company C, the question would be to examine its total gross income over the last three years and assess if its gross income derived from the activities of investing, re-investing or trading of its financial assets by its asset manager equals or exceeds 50% of its total gross income(s). If the financial income meets the required 50% threshold, then Company C will need to consider the status of an FFI. Otherwise, Company C will consider the status of an NFFE.

But this may not be the end. If, after assessment, Company C considers itself as an NFFE, it still needs to examine if it is an active or a passive NFFE. Here, the entity will have to apply a passive income test. This test encompasses a different scope of income than the one considered under the financial income. Under the passive income test, if Company C's gross income (usually for the preceding calendar year) is less than 50% of passive income and less than 50% of its assets produce or are held for the production of passive income, then Company C can consider the status of an active NFFE.

Finally, if these conditions are not met by Company C (more than 50% of its assets produce passive income), then Company C will need to consider the status of a passive NFFE.

Although the process might be burdensome for some companies to go through the assessment, the good news however, is that once it is properly done, it can be used under the OECD standard for automatic exchange of information as the same tests apply.

Ferdinando Mercuri (fmercuri@deloitte.ch) and
Adam Jagusiewicz (ajagusiewicz@deloitte.ch)
Deloitte
Tel: +41 58 279 9242 and +41 58 279 9204
Website: www.deloitte.ch