

## Professional Real Estate Dealer Classification and Implications



**Under certain circumstances, private individuals may be classified by the tax authorities as professional real estate dealers. As a result, gains on private real estate may be taxed additionally at federal level, and social security contributions may also have to be paid.**

### Basic Principle

Neither gains on private real estate nor those on movable private assets are taxed on the basis of the Direct Federal Taxation Act (DBG) (art. 16, para. 3, DBG). Cantonal provisions are reserved.

The question as to an individual's classification as a professional real estate dealer is very important in connection with the treatment of real estate sales effected by private individuals under income tax law as well as social insurance law.

### 1. Case Law of the Federal Supreme Court

For a private individual subject to tax to earn taxable income from self-employment, he/she must not merely sell real estate in connection with the management of the asset or in order to exploit an opportunity which arises by chance; rather, the individual must engage in this activity systematically, with the intention of making a profit (ruling of the Swiss Federal Supreme Court (BGE) 125 II 113). For such an activity to be classified as self-employment, the individual subject to tax does not have to participate visibly in economic transactions, or perform the activity under the auspices of an actual, organized business.

### 2. Factors Influencing Classification as a Professional Real Estate Dealer

The decision of the Swiss Federal Supreme Court BGE 125 II 113 states that the Federal Supreme Court's existing practice on the taxation of real estate dealers continues to apply, and is governed in particular by the following specific criteria:

- Systematic or planned nature of the operation
- Frequency of transactions
- Close links between this activity and professional activities
- Specialist expertise in this area
- Short period of ownership
- Use of substantial borrowed funds to finance the transactions
- Reinvestment of gains in similar assets

However, the aforementioned criteria need not apply cumulatively in order to assume that professional real estate trading is taking place. Instead, according to the Federal Supreme Court, the circumstances of the specific individual case must be considered in their entirety as the basis for classifying an individual as a professional real estate dealer.

In the Federal Supreme Court's opinion, the **frequency of sales activities** and **planned nature of the operation** are sufficient to determine its professional status. In exceptional cases, however, this professional status can even be confirmed if the case only involves one single property sale, provided that the sale of the real estate goes beyond the mere scope of management of private assets (see BGE 104 Ib 168 et seq.).

### 3. Tax Treatment for Classification as a Professional Real Estate Dealer

#### 3.1 Under Federal Law

For private individuals, gains realized from professional real estate trading are additionally subject to ordinary income tax at Federal level (as well as cantonal tax), and also to social insurance contributions. Furthermore, the annual revenues generated from real estate are subject to social insurance contributions. On the other hand, losses can be deducted for tax purposes and carried forward for up to seven years if necessary, provided that such losses are posted and recognized correctly from an accounting perspective. If a private individual subject to tax engages in professional real estate trading, the relevant real estate must be allocated to business assets. For this purpose, real estate dealers must book the real estate intended for trading as "Merchandise held for resale" in current assets.

### 3.2 Under Cantonal Law

Taxation of gains from the sale of real estate differs fundamentally depending on which of two different taxation systems is applied: these are the dualistic and monistic systems.

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#### Breakdown by Canton

System	Cantons
Dualistic	AG, AI, AR, FR, GL, GR, LU, NE, OW, SG, SH, SO, TG, VD, VS, ZG
Monistic	BE, BL, BS, JU, NW, SZ, TI, UR, ZH

Canton GE has a specific regime.

#### Dualistic System

As is the case under direct Federal tax law, capital gains realized on the sale of real estate that forms part of business assets, or which originate from professional real estate trading, are subject to ordinary income tax and are added to other income in those cantons with the dualistic system (special cantonal regulations must be taken into account in each specific case).

#### Monistic System

In cantons with the monistic system, gains from the sale of real estate that forms part of the business assets or which originate from professional real estate trading are generally covered by real estate gains tax (special cantonal regulations must be taken into account in each specific case).

### 3.3 Sale of an Investment Property

When selling an investment property, it is advisable to consult a tax specialist who will – in advance of the transaction – analyze whether it constitutes professional real estate trading or, if necessary, will obtain a ruling from the relevant tax authority to clarify this issue. The tax specialist may also assist with examining alternatives.

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#### Contact us

We will be happy to arrange a personal consultation. Call us at 0844 200 114\*; Mon.–Fri., 08:00–20:00. For more information, visit our website at:

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