

Proposed Ratification of the Hague Trust Convention



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On 2 December 2005, the Federal Council submitted draft legislation to the Swiss Parliament for the ratification of the Hague Trust Convention ("HTC") and its implementation in Swiss law. Prompt ratification of the HTC is intended to provide greater legal certainty for the use of trusts in Switzerland.

The Status of the Trust under Swiss Law before the HTC

Swiss law does not have a form of property ownership equivalent to the form of ownership known as a trust in Anglo-Saxon jurisdictions – the vesting of legal title to property in a trustee by a donor (known in law as a "settlor") for the benefit of specified beneficiaries. Even though a trust cannot be created under Swiss law, the trust nevertheless plays an important role in international private banking and corporate financing.

Provided that the assets of a trust are sufficiently independent from the trustee and the settlor a majority of commentators on Swiss law classify a trust as an organized economic unit ("*organisierte Vermögenseinheit*") as that term is used in Art. 150 para. 1 of the Private International Law Act ("*PILA*"), which provides the definition of business organisations used in the PILA.

Pursuant to Art. 154 para. 1 PILA, the law governing the existence of an organized economic unit is the law of the state under which it was organized. In general this results in the recognition of the trust under the present Swiss law if the legal requirements of the jurisdiction of its organization have been met. If these organizational requirements have not been satisfied, then under Art. 154 para. 2 PILA, the trust will be governed by the law of the jurisdiction in which it is actually managed. If the trust is managed in Switzerland, it will not be recognized as a trust.

The Hague Trust Convention

The HTC provides rules for determining the law governing a trust, but it does not contain any provisions on jurisdiction for the recognition and enforcement of foreign judgements.

The HTC applies only to trusts created voluntarily and evidenced in writing (Art. 3). Therefore, fiduciary relationships which arise by operation of law in some jurisdictions, so-called constructive trusts, are outside the scope of the HTC. Further, the HTC does not apply to "preliminary issues relating to the validity of wills or of other facts by virtue of which assets are transferred to the trustee" (Art. 4).

A trust is to be governed by the law chosen by the settlor (Art. 6), but if a governing law has not been chosen, then the HTC provides that a trust shall be governed by the law with which it is most closely connected (Art. 7). In order to ascertain such law reference is to be made in particular to:

- a) The place of administration of the trust designated by the settlor;
- b) The situs of the assets of the trust;
- c) The place of residence or business of the trustee;
- d) The objects of the trust and the places where they are to be fulfilled.

The law with which the trust is most closely connected also is applicable if the law chosen by the settlor does not provide for the creation of trusts (Art. 6 para. 2). If the law with the closest connection to the trust also does not provide for the creation of trusts, then the HTC is not applicable (Art. 5). Finally, the settlor may specify that a different governing law be applied to a "severable aspect" of the trust, "particularly matters of administration" (Art. 9).

Amendments to the PILA

In order to implement the HTC in the Swiss legal system, the draft legislation would add a chapter dealing with trust matters in the PILA. Pursuant to the new chapter the applicable law is to be determined in accordance with the HTC. However, this

new chapter has a broader scope than the HTC since it also would apply to trusts which are not evidenced in writing and to trusts to which the HTC does not apply because the law of the jurisdiction deemed to apply under Art. 7 does not permit the creation of the trust involved (Art. 5). As a result, the new chapter of the PILA would extend the principles of the HTC to trusts which are not evidenced in writing or fall outside the scope of the HTC pursuant to Art. 5.

The jurisdiction applicable to judicial proceedings in respect of a trust may be specified by the settlor. In conformity with the Lugano Convention on jurisdiction and the enforcement of judgements in civil and commercial matters, the specification of jurisdiction must be in writing or evidenced in writing. If jurisdiction has not been specified or if the chosen jurisdiction does not have exclusive jurisdiction, the following courts may accept jurisdiction:

- a) The courts at the domicile or, if not applicable, at the habitual residence of the person against whom the action has been brought;
- b) The courts where the trust is located, or
- c) In proceedings which have as their object the activity of an entity's branch in Switzerland, the courts where that branch is located.

The location (*situs*) of a trust is the place referred to in writing or evidenced in writing in the trust document. If the situs of the trust is not defined in the trust document, then situs is deemed to be the place where the trust actually is managed.

In addition to provisions on the recognition of foreign judgements in respect of trusts, a new chapter of the PILA also would provide for the registration of the trust in the land register and the intellectual property register. Trusts claiming rights which are not registered in connection with the types of rights registered with these registers may not be asserted against a bona fide, third-party acquirer of such rights.

Amendments to the DEBA

The amendments to the Debt Enforcement and Bankruptcy Act ("DEBA") also would recognize the segregation of trust assets from the assets of the trustee and would specify the procedure applicable to the enforcement of claims against a trust. Enforcement proceedings in connection with a claim against the trust will have to be instituted in the relevant court at the situs of the trust. Proceedings against the trust must be addressed to the trustee. Enforcement proceedings may lead to the bankruptcy of the trust,

i.e. all assets of the trust being realized by general execution ("*Generalexekution*").

The question whether the trustee has become personally liable for the debts of the trust is to be determined in accordance with the law applicable to the trust. If the trustee is found to have personal liability, a creditor has to institute enforcement proceedings against both the trustee and the trust. In bankruptcy proceedings against the trustee, the assets of the trust are segregated from the personal assets of the trustee.

Conclusion

The ratification of the HTC eliminates the uncertainties with respect to the application of Art. 150 PILA to trusts. Furthermore, the new provisions to be included in the PILA harmonize the operation of the Convention and the PILA. The provisions dealing with jurisdiction and the recognition and enforcement of foreign judgments in respect of trust matters will supplement the provisions of the HTC for the determination of the applicable law. Finally, the new provisions of the DEBA ensure the segregation of the assets of the trust and the trustee. The ratification of the HTC and the adoption of the amendments to the PILA and the DEBA ensure a firm foundation of the trust in the Swiss legal system and create greater legal certainty.

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