Forced Heirship and the Common Law Trust - Especially from the Swiss Point of View - Part I -

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At the beginning of a series of articles that appeared in the periodical "Private Client Business" entitled: "An Offshore View of Forced Heirship" the author, Mr Antony Duckworth, placed the headnote:

'Forced heirship poses a threat to all trusts, onshore as well as offshore, not just to those designed to circumvent forced heirship.'

This article, based upon a talk given on 17th January this year at a meeting of STEP German, Swiss and Liechtenstein branch in Zurich examines the position especially from the Swiss point of view.

Any Common Law jurist will naturally harbour a certain reserve against an intrinsically civil law institution such as forced heirship. Reciprocally a similar attitude may often be found when civil lawyers are confronted with the concept of the trust.

There is a certain incompatibility between the two which does not spring just from an unwillingness to understand and come to terms with a different system. The cause lies deeper. It has its roots in two fundamental differences in attitude and the legal principles resulting therefrom. This difference which Mr. Duckworth calls the global conflict of principles, is freedom of disposition of a person over his estate, both during life time and upon death, on the one side (the Common Law Concept) as against preservation of the family property or the "*patrimoine*" on the other (the Civil Law Concept).

" ... in all civil law systems ... the bulk of an individual's property passes on death to his descendants."

The Common Law system imposes a duty of care on parents to provide for their children until such time as they are able to provide for themselves. Over and above that, the child has no further claims on his or her parents' property and all remoter issue are equally excluded in this respect. (I am not dealing here with succession on intestacy, which has no direct bearing on the question).

The general rule in all civil law systems is that the bulk of an individual's property passes on death to his descendants. We have what is called universal succession ie immediate and unconditional passing of property to the descendants in shares *per stirpes*. Where there are no descendants, the parents and, if they have predeceased, the remoter ascendants ie the grandparents take, following the male line of ascendancy and descendancy of the deceased. The civil law system therefore, which stops short of saying that the property belongs to the family rather than the individual, reflects a sort of compromise between family ownership on the one hand and individual ownership on the other. Having established that, it follows logically, and therefore not surprisingly, that the concept of forced heirship is not confined to regulating the passing of property upon death but is supplemented by a number of ancillary restrictions as regards an individual's freedom of disposition over his property during his lifetime. It is these restrictions, just as much as the rules of descendancy, that may constitute a threat to a trust. They should be observed particularly where beneficiaries are resident or domiciled in a civil law country with a trust or trust property is situated in a civil law country are concerned. I will revert to this in detail later.

" ... the provisions ... may prove an obstacle to a property settlement under a trust."

1.1 The Swiss Civil Code

It is necessary to examine forced heirship rules, the ancillary provisions and the remedies in case of their violation under the Swiss Civil Code. These concern the provisions that may prove an obstacle to a property settlement under a trust. These provisions under Swiss law may, to a large extent, be considered to be characteristic for a civil law country inasmuch as, in effect, they do not vary fundamentally from those of say France, Italy or Germany.

In order to get a proper assessment of the situation we must, however, begin with the section in the Federal Code on marital property law before we move on to succession. This is often not realised by Common lawyers when confronted with civil law issues of inheritance.

1.1.2 Marital Property

Upon marriage the law imposes a property regime which is community of property, unless the future spouses enter into an express marriage contract in which they can stipulate, for instance, separation of property. Community of property gives each spouse an equal interest in the property acquired by either of them during marriage. Upon the death of one spouse (or upon divorce), the community is first dissolved. The marital property is then divided between the surviving spouse and the estate of the deceased spouse. The heirs of the deceased spouse only participate in the net estate after the share of the surviving spouse in the community has been accounted for.

Dispositions made during marriage, possibly in the form of a trust settlement, favouring a beneficiary other than the spouse, may therefore

come under attack from the matrimonial property angle.

I.1.3 Rules of Inheritance and Freedom of Disposition

The rules of inheritance are contained in arts 470 - 480 of the Federal Civil Code. This section defines the disposable quota as against the quota reserved for the forced heirs or the compulsory portion (reserve). A person leaving descendants, parents or a spouse is bound by the rules of forced heirship and can only dispose freely after allowing for the reserved quota.

The reserved quotas are:

3/4 for a descendant
1/2 for each parent
1/2 for the surviving spouse

"Dispositions made during marriage … may therefore come under attack …"

The above quotas have to be read in relation to the actual inheritance shares ie what would devolve on the legal heirs in case of intestacy.

We therefore get the following reserves as against the disposable quotas,

depending on the class of legal heirs that participate.

Only descendants:	3/4	1/4
Only parents:	1/2	1/2
Only brothers and sisters:	1/4	3/4

(For further quotas depending on the number of heirs and the proximity of relationships see Annex I)

Example

A short example may illustrate the *modus operandi*:

A dies leaving a spouse **B**, two children **C** and **D** and a parent **G**.

A has brought 150.000 into his marriage, **B** 100.000. During their marriage they have increased their marital property by a further 400.000, so that at the time of **A**'s death it amounts to 650.000.

Their matrimonial property regime was the usual Community of Property.

"The surviving spouse, when competing with descendants, can be given his or her share in ownership or in usufruct."

(a) The first stage after **A**'s death is the dissolution of marital property. The property shares originally brought in are re-allocated. Consequently 100.000 will go to **B** as surviving spouse and 150.000 into **A**'s estate. For the sake of simplicity, let us assume that the 400.000 were acquired during marriage through joint efforts by the two spouses. This so-called surplus or profit is in the second stage divided equally. **B** will therefore get an additional 200.000 and the other 200.000 will go into **A**'s estate. This will leave 350.000 for distribution by inheritance.

(b) The reserved quotas by forced heirships rules will then be as follows:

3/4 of 1/2 = (3/8) to the surviving spouse **B**

1/2 = (4/8) of the whole to the two children **C** and **D**

Disposable free quote: 1/8

G has no duty share because the parental line will only take if the deceased leaves no children.

Expressed in figures, we will get the following result:

B:

300.000	out of the dissolution of the maritial property
131.250	3/8 as reserved quota
431.250	Total for **B**

C and D

175.000	or 87.500 each as reserved quota
43.750	1/8 free disposable quota
650.000	total

Assuming **A** dies leaving no children but his parent **G**, we get the following situation:

(a) Division of marital property as in the previous example.

(b) Reserved portions by forced heirship rules:

B: 3/8
G: 1/8

Expressed in figures, we will get the following result:

B:

300.000	out of the dissolution of the marital property
131.250	3/8 as reserved quota
431.250	Total for **B**

G:

43.750	1/8 reserved quota
175.000	1/2 free disposable quota
650.000	Total

ANNEX I

• **Compulsory quota**		• **Disposable quota**
- Descendants only	3/4	1/4
- Parents only	1/2	1/2
- Parents & brothers and/or sisters	1/4	3/4
- Brothers & sisters only	0	1
- Grandparents only	0	1
- Descendants & spouse	1/4 + 3/8	3/8
- Parents & spouse	3/8 + 1/8	1/2
- Parents & brothers/ sisters & spouse	3/8+1/16+0	9/16
- Brothers/sisters & spouse	3/8 + 0	5/8
- Grandparents & spouse	1/2 + 0	1/2

The surviving spouse, when competing with descendants, can be given his or her share in ownership or in usufruct. Whether the surviving spouse gets one or the other is irrelevant for the calculation of the reserved portion and the corresponding disposable quota which is always made on the assumption of allocation of ownership. Unlike France, where the surviving spouse has no forced heirship right and the reserved quota varies according to the number of descendants, under Swiss Civil Law, it is always 3/4, regardless of the fact whether there is only one or whether there are five or ten children.

"A gift ... may be ... specified ... as an advance towards the donee's right of inheritance."

The actual estate which forms the basis for the calculation of the disposable portion as against the reserved quota is the net value at the time of the death of the individual (assets minus liabilities and certain allowable deductions connected with the demise). So far everything would seem straight forward. However, legal regulations do not stop here. Art 475 of the Civil Code expressly stipulates that gifts or allocations (German: "*Zuwendungen*", French: "*liberalités*"), which essentially comprises any transfer of property without consideration for value received during the deceased's lifetime, must be included in the assessment of the estate, because they may be subject to the so-called "*Herabsetzungsklage*" (French: *réduction*). For lack of an exact equivalent, this may be translated into English as "Claw-back claim".

Art. 475 contains a cross-reference to art 527 of the Code, which enumerates four main instances, giving rise to a claw-back claim. They are:–

1. Gifts *inter vivos* made by the deceased in satisfaction of the donee's right of inheritance or by way of dower, or as a division of the donor's estate where they are not liable to be brought into hotchpot;
2. Alienations in consideration of a renunciation or sale of rights of inheritance;
3. Gifts which the donor had full liberty to revoke and those which he made within five years preceding his death with the exception of presents made on occasions where they are customary;
4. Alienations made by the deceased with the evident intention of evading the rules of his freedom of disposition;

"An implied intention of an evasion ... is more likely to be presumed than in the case of an irrevocable gift ..."

To clarify matters, it should be added in connection with s1 that the law requires everything to be brought into hotchpot which the deceased has given during his/her lifetime by way of advancement on a share in the inheritance. This, of course, does not imply any duty of restitution but is required as a means of assessing the so-called "inheritance mass" or estate of the deceased for purposes of calculation of the reserved as against the disposable portion. A gift *inter vivos* may be made and specified as such as an advance towards the donee's right of inheritance. Such a gift normally, and by definition, should not be exposed to a claw-back claim, as it is an advance towards the donee's share of inheritance. It may, however, be so exposed if, in effect, it curtails the reserved portions of the other legal heirs, either outright or in the final analysis ie if taken together with further shares granted or bequests made to the donee later under a will. In the same way a gift not specified as an advance to a donee's right of inheritance may become subject to claw-back.

"The onus of proof that the donor had the intentino of evasion lies with the claimant invoking claw-back."

Section 2 deals with a similar situation except that here the deceased has alienated a portion of his estate *inter vivos* to an heir who in turn voluntarily has renounced his right of inheritance. The alienated portion may, at the time of the donor's death, turn out to be in excess of the disposable portion. If so, the other legal heirs may bring a claw-back claim in as much as their duty portion has been curtailed. Here, however, art. 535, subs 2, limits the right of claw-back to the amount by which the donee has been unduly enriched. Conversely, such a donee is barred from claw-back if his portion eventually turns out to be less than his duty share, because he has renounced his right of inheritance.

Sub-section 3 is not without controversy, both in its wording and in the interpretation given to it by the courts. Freely revocable gifts become irrevocable with the donor's death. They are subject to claw-back claims even if in violation of the reserved portion as a "*donation à cause de mort*" and even if the promise of gift was made more than five years prior to the donor's death. An implied intention of an evasion of the rules of freedom of disposition is more likely to be presumed than in the case of an irrevocable gift, executed during the donor's lifetime. This really leaves only one loophole in the net of possible claw-back claims: **Irrevocable gifts made more than five years before the donor's death**. They must, according to prevailing opinion, not only be made but also executed before the crucial five years period, even though the wording of the sub-section would allow for a broader interpretation.

There is a further and final catch in subs 4. It subjects all alienations made by the deceased during his lifetime to claw-back if made with the **evident intention of evading the rules of his freedom of disposition**. The wording of the article hardly leaves any doubt that the intention to evade must be evident and be the motivating force behind any such alienation of property. The interpretation given to it both in jurisprudence and literature is, however, more restrictive. It will suffice that such a donation is made primarily in favour of a third party whereby possible future violations of reserved portions of legal heirs may result. Claw-back may take effect even against the donee who received in perfect good faith. This is expressly mentioned in art 528 subs 1, whereby the bona fide donee is liable to restore what he received, only, however, up to the amount by which he is still enriched by the gift at the time of the opening of the succession of the donor's estate. The onus of proof that the donor had the intention of evasion lies with the claimant invoking claw-back. He has to prove to the court's satisfaction that the property (or property rights) have been alienated, that the deceased did so with the intention of evading the rules of freedom of disposition and that by doing so he did in effect exceed such freedom. To substantiate his claim, he has to furnish evidence concerning the amount of the gift at the time of donation and as to the present value of the property donated. Detailed information may not always be easily available, even though as a legal heir a plaintiff will have full right of access to the deceased's estate. The term "alienation" finally, as used in subs 4, is interpreted in a very broad sense. Apart from an outright gift it may comprise any kind of transaction in favour of a third party without proper consideration such as a so-called mixed donation, a forgiveness of debt, a waiver of claim etc. An insurance policy taken out by the

deceased on his life and assigned without consideration to a third party will also be liable to claw-back at the redemption value.

I.1.4 The Operation of Claw-back

Without going into the intricacies of the claw-back claim under Swiss law and the nature of such legal action for reduction, one can sum up matters as follows:

The testator, depending on his legal heirs in each individual case, has a larger or smaller freely disposable quota. If he exceeds such quota by will or by disposition *inter vivos* in favour of extraneous parties, his will or the disposition in question will primarily stand. The legal heirs have to prove that their duty share has been curtailed and they have to initiate legal action. Such action, if successful, does not invalidate the will or the disposition *inter vivos* in question but results in an order for adjustment. Reductions are made in the first place on testamentary dispositions and then on gifts *inter vivos*, beginning with the latest in point of time and continuing in that order until the compulsory portions are fully satisfied.

""The action for reduction or claw-back claim is subject to a relatively short period of notice."

The action for reduction or claw-back claim is subject to a relatively short period of notice. It must be brought within a year from the time when the heirs receive cognizance of the infringement of their rights and at any rate not later than ten years from the opening of the will in respect of testamentary dispositions and from the death of the donor in case of a disposition *inter vivos*.

1.2. Other Systems

"The court's view of what is reasonable depends on the circumstances of the case."

As mentioned *above* the Swiss Civil Law rules on forced heirship may be considered as being characteristic of most civil law systems. This statement has to be qualified, in as far as the methods of securing the proper application of the rules of forced heirship differ between the various civil law countries. At one end of the scale we have strict forced heirship as it is applied, for instance, by the French "Code Civil", where the individual's power of testamentary disposition is *ab initio* limited to a portion of his property (*quotité disponible*). The remainder (*réserve héreditaire*) devolves automatically and without regard to the testator's wishes upon the persons prescribed by law as the forced heirs. The same restriction applies to lifetime gifts which, in effect, may only be made from the "*quotité disponible*".

"The trust may be attacked after the settlor's death ..."

Strict forced heirship also applies in Spain, with varying rules from one part of the country to another, in Scotland, with fixed portions for the surviving spouse and descendants but no claw-back for lifetime gifts, in Latin America and, apart from some other European states, under Islamic law. Islamic law has complex devolution rules which vary between the different schools of Islamic law. An interesting feature here is that no account is taken of lifetime dispositions and there is no claw-back except if a gift was made during the individual's "death illness".

More liberal than the strict form is the forced heirship by indefeasible shares, the system followed by Switzerland, as just described, and by German law. In Germany also, the testamentary powers, strictly speaking, are not restricted but succession rights are conferred on forced heirs. It is up to the forced heirs to pursue their claims against the testamentary heirs or third party donees. They must do so within three years after the testator's death. The entitlement for inclusion for lifetime gifts to third parties can be extended back to ten years before the testator's death.

Interestingly, the legislation of some of the states in the USA offers examples of forced heirship by indefeasible shares in favour of the surviving spouse, and in the State of Louisiana, for instance, also for children.

At the other end of the scale we have what may be called forced heirship by judicial adjustment. This category of legal systems comprises England, Ireland and a number of former British colonies.

Under English law the individual may by will, as mentioned initially, dispose of his estate as he pleases. However, the Provision for Family and Dependants Act 1985 enables a surviving spouse, former spouse, child or other dependant of the deceased to apply to the court for relief if the deceased has failed to make "reasonable financial provision" for the applicant. In the case of children and other dependants the expression contemplates the applicants' maintenance, nothing else. In the case of the surviving spouse, the court will take regard to the provision the surviving spouse might have expected, had the marriage ended by divorce rather than by death. The court's view of what is reasonable depends on the circumstances of the case. The act does not restrict the individuals freedom of disposition *inter vivos* except that there is an anti-avoidance rule which may apply if, within the last six years before his or her death, the individual disposed of property for less than full consideration with the intention of defeating applications under the Act. The court, in any case, has discretion and will rule, having regard to the circumstances of the case. It is important to remember that the Act only applies to an individual dying domiciled in England.

II.1 The Trust

Forced heirship may be a problem for both the trustee and the beneficiaries under a trust. The trust may be attacked after the settlor's death by persons claiming forced heirship entitlements over property held in trust or distributed from the trust.

We are concerned here with trusts created *inter vivos*, not testamentary trust where the possible conflict does not arise. An *inter vivos* trust may exist for years before the trustee or any other involved party becomes aware that the settlement is liable to forced heirship attack. Nationality, domicile, the permanent place of residence or the general circumstances of the settlor at the time of his death may be different from what they were at the time the trust was created. At the time of creation of a trust one can only talk in terms of possibilities, at best probabilities. Even if,

initially, the settlor has no links with a forced heirship regime, things may look different later. Uncertainties or problems, if they arise, are invariably due to claw-back. If forced heirship rules were restricted to succession only, the situation would be simpler and straight forward.

For the trustee, the problem of forced heirship is given an extra edge. A trustee obliged to succumb to claw-back may have to compensate forced heirs for amounts exceeding the remaining trust assets in his hands if we take distributions to beneficiaries, possible investment losses, the trustees fees and other costs since the creation of the trust into account. The trustee may conceivably have to incur additional significant expenses in having to defend the trust from forced heirs. These are, so to speak, the risks of the "métier" of a trustee.

"A trustee ... may have to compensate forced heirs for amounts exceeding the remaining trust assets in his hands."

Forced heirship, on the other hand, may constitute an opportunity. It adds to the list of reasons for having a trust. An individual who is dissatisfied with the restrictions that will or may apply to his estate, will endeavour to find more satisfactory arrangements. Dealing with international situations, as is normally the case with offshore trusts, the identification of an individual's succession law may foreseeably be a matter of dispute. Will the link of attachment for the law of succession applicable be domicile, nationality or the last habitual residence? Loopholes or openings may be found here.

II.2.1 Confrontations

Confrontations are almost bound to occur occasionally between trust arrangements on the one hand forced heirship claims on the other, particularly with offshore trusts where often multinational connections are involved. Such confrontations may be a matter of accident due to unforeseen circumstances. They may, however, also be a matter of the settlor's design.

The crucial question is, are the trust arrangements such that they can and will survive possible attacks by the settlor's heirs. In other words, the survivability of the trust.

"No state is invariably sympathetic and no state, probably, is invariably unsympathetic."

II.2.2 Survivability

Survivability of a trust against attacks by the settlor's heirs can comprise a whole bundle of issues. Each of these may be answered separately by courts of different states. It is not only the domestic law that differs but different conflict of law rules lead to different conclusions on the preliminary and vital question: "Which state's law will govern the substantive issue?" Forced heirs may attack a trust on the grounds of the domestic law of the forum, they may invoke foreign law and they may question the validity of the trust. They may question the settlor's title to the property or they may directly invoke forced heirship, they may obtain a foreign judgment and try to enforce it or they may look for other grounds. Any claim that will undermine the trust and throw the property back into the estate of the settlor will serve the purpose of the attacking heirs. A forum that refuses to recognise foreign forced heirship rights for instance (as some of the recent offshore legislations) may still be unfavourable for a trustee in terms of survivability of a trust; for instance,if it refers questions of legal capacity to the domestic law of the settlor, which in turn may deny him the capacity to create a trust.

The survivability may, in essence, be dependent on the following issues:

a. The validity of the trust. Heirs may claim and bring proceedings to the effect that the trust, according to the applicable laws, is invalid.

b. The settlor's title to the property under the applicable law may be questioned.

c. Heirs may question the validity of the disposition. They may try to assert that under the applicable law there was some defect, be it in the capacity of the settlor or in the observance of the form or otherwise.

d. Direct enforcement of the heirs' rights. The heirs may refer to the succession rights they enjoy under the succession law applicable and try to enforce them directly in the forum.

e. Claims for restitution. Even if the heirs have no proprietary interest and are unable to proceed with the direct claim, they may, under the applicable law, be entitled to restitution.

f. Enforcement of a foreign judgment. If the heirs have obtained a favourable judgment in the courts of another state on any of the above issues, they may try to enforce it in the forum in question.

g. Succession law. Would the heirs be recognised as such in the forum ? If not the forum would not even acknowledge that the heirs had claims in respect of the settlor's estate, let alone in respect of the trust.

h. Assumption of jurisdiction. Will the forum assume jurisdiction over the claims of the heirs? If they cannot go into the court, all other questions will be academic.

i. Bars to the heirs' claims. Are the heirs' claims barred due to some procedural rules or on a substantive issue? - Is there eg a statute of limitations?

These survivability issues will indicate, whether a forum is sympathetic or unsympathetic to a trust. No state is invariably sympathetic and no state, probably, is invariably unsympathetic.

This article will be continued in the next issue of TRUSTS & TRUSTEES.

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