

The Trust: a Powerful Wealth Tax Planning Tool for International Families in Switzerland

Viewed from abroad, Switzerland is regarded as a tax haven. Some of you may disagree, especially those of you who (intend to?) live in this country and (will) pay wealth tax. Very much to your disappointment, not only does wealth tax exist in Switzerland, but tax planning tools allowing its mitigate are scarce. Moreover, be well advised to stay shy from “aggressive” tax avoidance schemes! The good news that I would like to share in this article, is that there are legitimate ways to reduce the burden your Swiss wealth tax. Using trusts is one of them, and a particularly “non-aggressive” one for international families which have not settled yet in Heidi’s land, or for families expecting to receive gifts or bequests from parents or relatives living abroad. Caution -- using trusts without all the required skill could just as well turn into a true tax disaster.

The very concept of trust is as simple as genius. The owner of assets (the “settlor”) transfers these to a third party (the “trustee”, typically acting in a professional capacity). The trustee legally becomes the owner of these assets, yet has a duty to manage them in the best interest of the so-called “beneficiaries” (typically the settlor’s family, why not the settlor himself). This structure is praised for allowing a smooth and flexible transfer of family assets to the next generation, while serving numerous other purposes. The idea is generally to resolve the quasi-metaphysical dilemma “To have or not to have...”, i.e. trying to provide a family with all the advantages of owning wealth without incurring the downsides of it (protection against creditors, reducing exposure to wealth or estate tax, ...)

The relationship between Switzerland and trusts is quite a paradox. As a world-leading wealth management center, this country unsurprisingly boasts a rather flourishing trust industry. Many Swiss resident families already use trusts to hold all or part of their wealth. Yet, interestingly, the Swiss Civil Code does not contain a single provision on trusts! How so? Because Switzerland is not a « Common Law » country. In other words, its legal system does not follow the English law tradition, but rather the Roman law tradition, in which trusts are unknown. However Switzerland applies the Hague Convention on the recognition of trusts and as a party to it, recognizes trusts organized under foreign law, allowing for a satisfactory legal framework in the use of trusts in Switzerland, in terms of legal certainty and predictability. It even allows trustees to manage trusts from Switzerland. Switzerland also has a tax system favorable to beneficiaries of trusts, at least in some specific contexts. Two examples will illustrate this better than legal Mumbo Jumbo. First example: A foreign family (parents and children) is planning a move to Switzerland. Before actually moving, they transfer say 20% of their wealth to an irrevocable trust. The Swiss tax authorities will recognize that the trust fund no longer forms part of their taxable wealth, thus allowing the family to reduce its taxable wealth by 20%. The condition is that our family cannot directly benefit from the trust fund, but more remote relatives and future generations can, as well as charities. Second example: an elderly lady living abroad intends to bequeath her wealth to her son, who happens to live in Switzerland. If she does so, he will inevitably pay Swiss wealth tax on whatever he will inherit. In contrast, if she creates a discretionary trust for the benefit of her son instead of that outright bequest, the assets could remain outside of the son’s taxable wealth, while still benefitting him. Other scenarios can give rise to interesting opportunities too. Note that in each case, the trustee can be based in Switzerland. Of course, both examples require proper and careful structuring. Badly drafted or poorly organized trusts may lead to administrative nightmares, and to dramatic tax consequences, in particular in relation to gift and inheritance taxes. **Me Guillaume Grisel Private Client Partners : Yves Bonnard, Stéphane Lagonico, Guillaume Grisel**