

Anglo Saxon trusts: Argentina and the Argentine Civil Code

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Abstract

Why do foreign trusts work in Argentina? The answer is: because of the Argentine Civil Code.

The Civil Code of the Republic of Argentina was enacted in 1869. It acquired a pre-eminent position in South America, and influenced drafting in civil law countries in the rest of the world.

Unusually, the Code is derived from Roman and Napoleonic law; little is derived from Spanish law.

One of its innovative qualities was that it developed a system of international private law. The basis of this system was that foreign law entities and systems were recognized, except to the extent that they did not offend public order and local mores. So, contracts, legal instruments, and acts are subject to the laws of the place where they were executed or performed (Article 8), (this is provided for in Article 12 of the Brazilian Civil Code also).

Argentina, in dealing with persons, adopts the principle of domicile independent of a person's nationality (Article 6), where even acts are performed, or property is situated, in Argentina. This requirement applies equally to contracts. Article 12 provides that the formal parts of contracts and public instruments are governed by the country in which they have been granted. In relation to real estate, Article 10 provides

that real estate located in Argentina is ruled by Argentine laws, principally. Nevertheless, the Code provides that contracts concluded in a foreign country, conveying rights in real estate in Argentina have the same force as if they were made within Argentina, provided they are included in a public instrument and are legalized (Article 1205). Similar criteria apply to movable property where that property is situated permanently in Argentina.

As to the effect of contracts, the Code provides that contracts entered into in Argentina or out of it, or to be performed within its territory or out of it, are governed as to their validity, nature, and obligation by the laws of the jurisdiction where the contract is executed, whether the contracting parties are nationals or not (Article 1209). Article 1205 echoes Article 8 in providing that contracts performed outside of Argentine territory will be judged as to validity and invalidity, and the nature of the rights and duties by the laws of the country in which they were signed. The only qualification to these rules is whether, under Article 14, there is anything to suggest the foreign 'figure' is inapplicable as disturbing as public order or a fundamental local norm.

These rules apply not only to contracts but all legal instruments. Consequently, they came to be recognized as applying to foreign trusts.

These principles were fused in 2005 in *Vogelius*,¹ by the eminent Argentine Judge Dr Eduardo

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1. *Vogelius, Angelina T et al v Vogelius, Federico et al* (Buenos Aires City Civil Chamber of Appeals).

Zannoni. There he held not only ‘that a trust is not a legal scheme unknown to our law’, but ‘the fact of the trust is ruled by the law of the place of execution, i.e. the English law, due to application of the *locus regit actum* principle established by Section 8 of the Code’

These rules, as found in the Code, enable the recognition of a foreign Anglo Saxon trust by Argentine law. This, of course, raises the question as to whether under other Latin American codes with similar provisions, the same result would apply.

Three misconceptions

Where does The Hague Convention fit in? The Law Applicable to Trusts and Recognition, comprised in the Hague Convention of 1 July 1985, has not been ratified by any Latin American country, although a number of Latin American countries, including Argentina, were members of the conference from which the Convention emerged. However, even if the Convention was adopted, it does not affect the rules set out above. Therefore, by reason of the above principles, the Hague Convention is irrelevant to the effectiveness of a foreign trust under Argentine law.

This points to two further confusions as to the role of trusts in Argentina.

First, there is a common-law misconception that Argentina (as with other Latin American or civil Law countries) does not recognize foreign trusts.

Second, there is a misconception that there is a trust law system equivalent to the Anglo Saxon trust in Argentina.

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The first arises from the famous case of *Brown v Gregson*² which was decided in 1920; Brown, a wealthy Scottish land owner, signed a will a few days before his death that gave all of his property equally to his children. Half of this property was land in Argentina. Just before his death he signed a codicil giving a life interest in a share to one of his daughters and the residue to her children. The will also provided that if any of the beneficiaries contested the will, they would lose their share.

Following Brown’s death, the disposition of the Argentine land was put before the Argentine Court. The Court found that the disposition of land was governed by Argentine heirship law.³ The result, therefore, was exactly the same with one exception. The daughter took her share of the land in Argentina, and her interest was not deferred. It appears, however that she then made provision for her children, so the outcome was just as Brown intended.

What then happened was a testament to legal opportunism. The daughter’s children claimed that the other beneficiaries, by reason of their inheriting the Argentine land by operation of law and not under the will, forfeited, under the will’s terms, their rights to the balance of Brown’s estate. A majority of the House of Lords held that this could not be treated as an election for the purposes of the will, and the argument failed.

For English law, it is in election that the importance of this case lies. But in the course of the judgment a number of unfortunate comments were made by their Lordships about the status of trusts under Argentine law. Viscount Haldane said that Argentine law ‘does not permit trusts or contracts which restrict the free

2. [1920] AC 860.

3. Art 90, point 7 of the Civil Code provides that the last domicile determines the place in which probate must be granted. Furthermore, art 3283 of the Code provides that the right to be an heir is ruled by the law of the last domicile of the testator, and also determines, in principle, the competent judge (art 3284), whether the heirs are Argentine or foreign. An exception to this rule is found in ss 10 and 11 (already quoted) in respect of real estate and movable assets permanently located in Argentina.

disposal of land by its owner'.⁴ Lord Moulton referred to the 'refusal of Argentina to permit lands to be held by a trustee... on grounds of public policy' and 'a system of trusts which [Argentine] law prohibits'.⁵ Viscount Finlay referred to Argentine law 'which does not admit of trusts on land'.⁶

It would have been more accurate to say that a foreign will could not override the laws of succession in Argentina, but the prejudice stuck. For the purposes of conflicts of law, it was thereafter assumed that trusts would not be recognized in Argentina.

It is quite possible that this assumption affected common lawyer's views of the trusts in Latin American countries, as noted above; as all of these countries adopted a broadly similar Code.

The correct position was set out in *Vogelius*, where it was stated that pursuant to the Code 'there were good reasons to admit *inter vivos* trusts' as being recognized by Argentine law, and in *Moreno* (2007)⁷ where the Court held, following Articles 12 and 1205 of the Code, that a foreign trust, properly established, would be recognized.

As pointed out in *Vogelius*, this is quite different from considering a trust's effect in Argentina, as this may be limited by Argentine law. This was in fact the case in *Brown v Gregson*. It was not that the will established by Mr Brown was not valid; it was the fact that it could not control the disposition of the Argentine land on his death. In that sense, the exception provided in Articles 10 and 14 applied.

The third misconception is more easily described.

It is true that there is a form of fiduciary ownership in the Code. It is also true that legislation (Act 24,441 of Housing and Construction Financing (1995)) introduced a type of trust in Argentina (more commonly called a *fideicomiso*). However, the *fideicomiso* is not the same as an Anglo Saxon trust. It lacks the support of a well developed doctrine of equitable and fiduciary rules. It is a creation of statute. Although it

helps to understand a trust by analogy, it is not a trust as is known in common law countries. Furthermore, this structure is used for business trusts (constructions, vineyards, commodities production, forestry, etc) and securitization vehicles, and not for wealth preservation of succession planning.

Establishment of a foreign trust and reserved powers

An imperfect understanding of the Code has also led to some trust planning coming to grief, especially in the context of reserved powers. In *Deutsch* (2009)⁸ the rules as to recognition set out above were affirmed. However, there were serious problems with the evidence presented to the court.

There was no evidence as to the transfer of the assets to the trust, or acceptance of those assets by the trustee. The trust document had not been notarized, the signatures were illegible, and the signatories were not identifiable. The signatories claimed to act on behalf of entities outside of Argentina without providing information as to those entities or how they were bound. The beneficiaries were not named. The trust instrument provided that none of the beneficiaries should be informed of their beneficial interest. The trust period was not defined.

There must be a suspicion in this case that the trust was created *ex post facto*. In any case, the failure to comply with the most elementary formalities of execution before a notary would immediately raise the suspicion of any civil law judge, and it is hard to imagine that any common law judge would give effect to such a document, especially when substantial assets were involved.

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4. Ibid 866.

5. Ibid 869.

6. Ibid 865.

7. *Moreno, Julio C v Tax Authorities Buenos Aires City* Contentious Chamber of Appeals (Administration) 2007.

8. *Deutsch, Gustavo*. Division A, National Court of Appeals, Criminal Economic matters, 15 May 2009.

law judge, and it is hard to imagine that any common law judge would give effect to such a document, especially when substantial assets were involved

In addition, Article 1802 of the Code provides that a donor cannot make a donation subject to 'a condition, precedent or subsequent that vests the donor or with the power to revoke, neutralize or restrict its effects'. Consequently, a settlement of a trust in which the settlor retains power of revocation, and substantive dispositive powers, particularly to himself, will run into difficulties.

This is precisely what happened with *Deutsch* and also with *Eurnekian*.⁹ In the case of *Eurnekian*, it was established in the facts that the settlor kept for himself the right to appoint and replace all persons in charge of the administration, and controlled the disposition of trust funds by the trustees until his death. Furthermore, it was clear that he effectively exercised day to day control over all aspects of the trust administration. At first the trust was considered a sham, although this was rejected in a fresh hearing where Article 1205 was held to apply to the trust, and it was held to be valid.

The Tax Court has now released its decision in *Eurnekian*. It followed the decision of the Criminal Court in upholding the validity of the foreign trust. The court relied on the provisions of Article 1205 of the Code, which upheld the validity of instruments made in accordance with the law of a country outside Argentina. In this case the court noted that the trust instrument had been validated before a notary in the Cayman Islands, as a public instrument. In addition the court referred to Article 19 of the Argentine Constitution to the effect that no person may be prevented from doing that which the law does not prohibit. In answer to the tax authorities' argument that there was no genuine reason for the settlor to

establish the trust, the Court held that the advantage of using a trust was obvious; it allowed the taxpayer to place the assets in the hands of third parties who were obliged to administer the property in accordance with their fiduciary obligations until the settlor's death.

There is a third case that is currently being considered by the Federal Tax Court. At first instance it was held that there was no evidence of the effective transfer of assets (shares in Argentine companies) to the trustee on the basis that there was no evidence of a share transfer; the trust was revocable or at least determinable at any point by the settlor; there was no reference to the acceptance of the assets in the trust document; the settlor enjoyed the absolute right to receive the trust income; and after settlement and the alleged transfer of the shares the settlor was appointed to be a board member of the companies in order to represent the shares supposedly held by the trustee. This decision is under appeal, but seems likely that it will be decided against the settlor on the basis that there was no true disposition of assets and powers to administer them to the trustee. In other words, this was incomplete for the purposes of Article 1802, just as a common lawyer would say that there had been an incomplete disposition of property to the trustee.

These decisions should not be surprising to any lawyer of whatever stripe. For example in *Deutsch*, at common law, the absence of two certainties essential for a trust, ie identifiable beneficiaries and identifiable property comprising the trust fund would be fatal.

Finally, it appears that the jurisdiction in which the trusts have been established, in these cases the countries involved, were those 'blacklisted' by Argentina. It therefore seems likely that the location of the trustee in a tax haven will be an adverse evidentiary factor, especially in a tax case.

9. *Eurnekian*, Eduardo. Buenos Aires City Criminal Court of Appeals 2003; Division 3 Oral Criminal Court.

The tax position of a foreign trust in Argentina

For tax purposes a foreign trust is a recognized entity. Under Ruling No 23 of 7 August 2000 of the Argentine Tax Authority a foreign trust was analysed and the view was expressed that Argentine law is only applicable to trusts created in Argentina, and foreign trusts are ruled by their applicable law. And it is made clear by the Argentine taxation legislation that foreign sourced income distributions obtained by an Argentine beneficiary or foreign trust are considered foreign sourced income. However, the trust must be properly established. This was the point in issue in *Eurnekian*.¹⁰

Argentine law is only applicable to trusts created in Argentina, and foreign trusts are ruled by foreign law

Taxation on distribution to Argentine beneficiaries

Assuming the problems arising with the recognition and funding of a trust above can be overcome (as has occurred with a large number of foreign trusts that have been inspected and accepted by the Argentine Tax Authorities), the following tax treatment should apply.

In general terms, Argentine resident individuals are taxed on their worldwide income with rates that ranges from 9 per cent to 35 per cent. Furthermore, personal assets tax applies on Argentine domiciled individuals on their worldwide assets existing as of 31 December of each year. This applies at effective rates that range from 0.5 per cent to 1.25 per cent of the total assets involved.

Under a properly constituted trust, the settlor will not be subject to income tax on the profits obtained by the foreign trust. The beneficiaries would not be

subject to these taxes until distribution. Neither the trust nor the trustee, assuming there is no Argentine sourced income involved, would be subject to these taxes. Furthermore, the settlor would not be subject to personal assets tax on their assets held by the trust.

In relation to distributions, the distribution made by a foreign trust will be considered foreign source income for the local beneficiary. The law allows a recipient to claim part of a distribution as free from tax as long as it can be clearly proved that the distributions were made from the corpus of the trust fund; only accumulated earnings and income will be taxable on distribution. If the jurisdiction of the trust is, and its bank accounts are in a country that is included in the so called 'Argentine blacklist' the payments will be assumed to be undeclared funds and attract a more substantial tax, unless the origin of the funds can be clearly established to the Tax Authorities.

The distribution made by a foreign trust will be considered foreign source income for the local beneficiary

Imperfect donation

'A donation cannot be perfected without the donee's acceptance' (Article 1792). This created serious problems in *Deutsch*,¹¹ where the trust instrument specifically provided that the beneficiaries were not to be notified of the trust. The Court held this as an important factor in finding that the trust could be considered invalid.

A donation cannot be perfected without the donee's acceptance

This presents a number of problems in trust practice when dealing with an Argentine settlor. It is not clear how the common lawyer can best address this. Following *Deutsch*, it would be ideal for the

10. Ibid.

11. See n 8, above.

beneficiaries to acknowledge the funding of the trust. This is, in the case of a discretionary trust, impracticable. It is submitted that documentary proof that the primary beneficiaries are aware of the trust and its assets may be sufficient. However, extreme care must be taken in every case to ensure that this requirement is fulfilled.

This case is on appeal, so the final position cannot be determined. It is safe to assume that a minimum requirement is that there is clear acceptance by the trustee of the transfer of assets to the trust.

Community property and succession

Care must be taken in the settlement of Argentine community property on a foreign trust. Broadly, community property comprises property acquired during the course of the marriage, or gains made by pre-marriage property during the course of the marriage. Pursuant to Article 1277 of the Civil Code, the settlor's spouse must consent to the transfer of such property. In addition Articles 1218 and 1219 of the Civil Code prevent spouses from contracting out of the community property regime. Again a settlement on a trust, even when consented to by a spouse, must not be in breach of this requirement.

Articles 1218 and 1219 of the Civil Code prevent spouses from contracting out of the community property regime

In Argentina, a surviving spouse is entitled to one half of the marital property. Otherwise, surviving descendants are entitled to four-fifths of the deceased's estate, in equal shares. In common with other civil law jurisdictions, this calculation also includes assets that have been gifted during the deceased's life time.

Where the trust assets are not situated in Argentina the position is straight forward. In *Wertheim v Gotlib*¹² (Supreme Court of New York) (1993), the deceased who was domiciled in Argentina, opened two Totten Trust Accounts with a New York bank. He wrote a will with the bank naming his brother as beneficiary. The deceased then married, but did not change the beneficiary of the will or in the accounts. On appeal the Court held for the brother. The widow argued that under Argentine law she was entitled to a share of half the funds in the Totten Trusts. The Court relied on the decision in *Wyatt v Furth*¹³ (1986) in which it was held that 'it seems preferable that as to property which foreign owners are able to get here physically and concerning which they request New York law to apply to their respective rights when it actually gets here, that we should recognize their physical and legal submission of the property to our laws. Even though under the laws of their own country a different method of fixing such rights would be pursued'.

The Court also referred to *Neto v Thorner*,¹⁴ where a Brazilian domiciliary established a Totten Trust in New York. His wife was not the beneficiary. When he died, it was found that he had executed a will in Brazil which named his wife as beneficiary. In this case, the Court held that the Brazilian executor could not maintain a claim against the beneficiary of the trust for funds. The Court rejected the executors request to have Brazilian law invoked, holding that the substantive law of New York includes New York's choice of law principles.

In relation to family succession, *Vogelius*¹⁵ (2005) and *Graziella* (2004)¹⁶, which were considered by Argentine courts, took a different approach.

In *Vogelius*, the settlor, while living in London transferred London real property to a foreign trust, appointing only two of his five children as the

12. *De Wertheim v Gotlib* 188 AD2d 108 [1993], lv denied 81 NY2d 711 [1993].

13. *Wyatt v Fulrath* [1965] 16 NY2d 169.

14. *Neto v Thorner* 71 8 F Supp 1222 [SD NY 1989].

15. See n 1, above.

16. *De Luca Ma Ada Graziella*, National Court of Appeal, 26 March 2004.

beneficiaries of the trust. The trust was recognized but the Court held that that did not mean that the effects of the trust could not be analysed under Argentine law. Accordingly, the Court ordered that as there were disposable assets held in Argentina, an adjustment should be made for the remaining three beneficiaries to compensate them for the loss of benefit of the assets that had been disposed of by the trust. The same result was applied in *Graziella*.

Again, formalities must be strictly applied. In *Gilchrist*¹⁷ (1956), the deceased who lived in Scotland was unmarried and would, under the rules in Argentina, have had to dispose of a half share in his estate to his mother. His will, made in Scotland, only provided income for his mother during his lifetime. He died domiciled in Argentina. Although not all of the assets were in Argentina, it was found that the will did not comply with the formalities required under Argentine law. The will was therefore declared a nullity.

Rules for the adviser

It is tempting to say that in the cases where the trusts were not successfully upheld, that given proper legal advice, the settlors objectives may have been met. Although, there is no final decision yet, if Mr Deutsch had set up his trust according to basic principles and the trust fund had been funded correctly, he would not be facing scrutiny of his structure. Certain formalities and legal requirements as well as the provision of the Code should have been respected.

A series of general minimum rules for an adviser can be suggested.

1. Wherever possible a jurisdiction with a robust trust law should be used.
2. The trust should be irrevocable and discretionary and in a conventional form. It should have a fixed term.

3. Extensive powers should not be reserved to the settlor or his nominees, and the settlor should not be a beneficiary, directly or indirectly.
4. The trustee, and the protector committee (who should not be based in Argentina), should have broad and independent administrative and distributive powers.
5. Wherever possible, an underlying entity should be used as the direct owner of the assets.
6. The assets transferred to the trust or the underlying entity must be transferred effectively and in compliance with the laws of the country where the assets are situated, and the country of the trustee. Wherever possible the primary beneficiaries must be aware of and accept the form of the trust and the assets transferred.
7. The trust instrument should record, wherever possible, the assets and purpose of the trust or at the very least, contemporary records should show the commercial or family purpose for the establishment of the trust. The settlor should not be a *de facto* or actual manager of these assets.
8. The trust should clearly identify the beneficiaries, and those beneficiaries should be entitled to be informed as to the property held in the trust.
9. Wherever possible the formalities for verifying and registering documents in all relevant countries (eg notarization and apostille) must take place, and if Argentina assets are held, the trust deed must be registered in Argentina.
10. Argentine “blacklisted” jurisdictions should be avoided both as to the trustee’s proper law and bank accounts.

As a final point, it is worth observing that there have been in practice, many foreign trusts that have been properly established and accepted by the Argentine authorities. The cases we see, apply, obviously, where things have gone wrong. It is to be hoped that the guidelines set out above will help prevent further challenges to foreign trusts.

17. *Gilchrist* Harry B, Court of Appeal, St Nicolas, 1956.