U.S. CITIZENS OWNING SWISS REAL ESTATE – CROSS BORDER ESTATE PLANNING IS A NECESSITY

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INTRODUCTION

The U.S. and Switzerland have maintained successful economic and trade relations for decades. This is reflected in the two-way trade volume of goods and services between the two countries and in the ever increasing exchanges of employees and executives.

Because more and more Americans are living and working in Switzerland, it is common for American citizens to own assets in Switzerland, especially real estate. In this environment, competent estate planning is needed to ensure that American citizens can leave Swiss assets to the next generation in accordance with their will, and to do so in an economical manner. This is especially true for U.S. citizens owning Swiss real estate. This article explains the principles, possibilities, and necessities of proper estate planning when Swiss real estate is owned by American citizens.

DIFFERENT LEGAL SYSTEMS

The U.S. and Switzerland have fundamentally different legal systems. While American law is derived from English common law, Swiss law is based on the Roman legal system. Differences in the inheritance and tax laws of the two countries make estate planning in U.S.-Swiss inheritance cases particularly complex. The complexity is exacerbated by the fact that each state in the U.S. and the District of Columbia has its own inheritance law and applies its own conflict-of-laws law.

One of the most fundamental differences between American and Swiss inheritance law is that Switzerland generally follows the principle of "unity of the estate" in international inheritance cases, whereas under U.S. law applicable law regarding transfers at death may "divided" depending on the type of property that is transferred. Under the unity of the estate principle, the entire estate of a decedent is governed by the law of a single state – the state of domicile of the decedent – regardless of where particular assets are located. In comparison, the rule in the U.S. regarding real estate[1] is that law of the state in which real estate is located controls transfers at death. In Latin, this is referred to as "*lex rei sitae*." In the case of personal property, the controlling law in the U.S. is that of the place where the deceased last resided. In Latin, this is referred to as "*lex domicilii*."

A further key difference between American and Swiss inheritance laws is a person's right to control who will receive assets owned at death through the mechanism of a properly executed will. Whereas in the U.S.A. there is generally extensive freedom

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[1] In Switzerland, real estate is referred to as immovable property. In this article, the term "real estate" is used exclusively. The terms have the same meaning.

to make wills,[2] in Switzerland statutory entitlement must be respected, such as forced heirship rights of spouses and descendants.

PRIVATE INTERNATIONAL LAW AND THE TREATY OF 1850 BETWEEN SWITZERLAND AND THE U.S.

In international succession matters, the relevant conflict-of-laws law of a country must be consulted. According to this law, international treaties – if applicable – generally take precedence over domestic law (see paragraph 2 of Article 1 of the Federal Act on Private International Law ("P.I.L.A.")).[3]

Way back on November 25, 1850, the U.S. and Switzerland concluded the Convention of Friendship, Commerce and Extradition between the United States and Switzerland (hereinafter "F.C.E. Treaty"), which is still in force today. Among other things, the F.C.E. Treaty applies in the event of the death of an American citizen resident in Switzerland or a Swiss citizen resident in the U.S. It also applies to dual citizens. In particular, it is applicable if a U.S.-Swiss dual citizen dies having his or her last place of residence in the U.S. Articles V and VI of the F.C.E. Treaty control the responsibilities and the applicable law in U.S.-Swiss probate matters. With regard to the inheritance of real estate, the F.C.E. Treaty stipulates that *lex rei sitae* applies to real estate. Consequently, the law and jurisdiction of the place where the real estate is located controls.

However, if a U.S. citizen who was last resident in the U.S. owns property in Switzerland at the time of death, it is not always clear whether the F.C.E. Treaty will be applied in a challenge brought in probate court. Several U.S. courts that have considered the issue have far disregarded the F.C.E. Treaty and applied the conflicts-of-law law of the U.S. state where the decedent was domiciled at death.

Either way, the transfer of real estate owned by a U.S. citizen who is resident in the U.S. at the time of death is controlled by Swiss law. In Switzerland, Swiss law applies by reason of paragraph 2 of Article 87[4] and paragraph 1 of Article 91[5] of the

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2 In some U.S. states, children and spouses may have a right to receive a certain percentage of a decedent's estate, notwithstanding the will. The balance of the estate may pass by will. Other states have community property laws. The laws vary from state to state. A listing of state laws on this point is beyond the scope of this article.

3 In English translation, paragraph 2 of Article 1 provides that international treaties are reserved.

4 In English translation, paragraph 2 of Article 87 provides that the authorities at the place of origin always have jurisdiction when a Swiss citizen having the last domicile abroad submits, in a will or a contract of succession, the decedent's entire estate or the portion thereof located in Switzerland to Swiss jurisdiction or Swiss law. However, paragraph 2 Article 86 is reserved. Paragraph 1 of that article provides that the Swiss judicial or administrative authorities at the last domicile of the deceased have jurisdiction to take the measures necessary to settle the estate and to hear disputes relating thereto. Nonetheless, paragraph 2 provides that exclusive jurisdiction claimed by a state where immovable property is located is reserved.

5 In English translation, paragraph 1 of Article 91 provides that the estate of a person who had a last domicile abroad is governed by the law referred to by the private international law rules of the state of domicile.

P.I.L.A. In the U.S., courts will look to Swiss law to control the transfer of real estate located in Switzerland.

For U.S. citizens having a last place of residence in the U.S.A. or U.S.-Swiss dual citizens having a last place of residence in the U.S.A., it is essential for to undertake estate planning in accordance with Swiss law with regard to real estate located in Switzerland. This is the only way to ensure the orderly and efficient settlement of estates involving real estate in Switzerland.

ESTATE PLANNING OPTIONS AND INSTRUMENTS

In the U.S.A., there are several ways to plan for a person's estate. As American probate proceedings are generally public and can quickly become time-consuming and cost-intensive, will-substitute arrangements are often used. the aim of these arrangements is to exclude as many assets as possible from subsequent probate proceedings. Life insurance policies, joint bank accounts and revocable or irrevocable trusts are commonly used for this purpose.

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Switzerland has two main instruments for estate planning. One is a will and the other is an inheritance contract. The latter generally is not found under U.S. law. The concept of a trust is fundamentally foreign to Swiss law, even though it is widely used in the U.S.A. In early 2022, a draft bill proposing the adoption of a trust law in Switzerland was published, triggering a consultation period for the submission of comments. Comments were mostly negative and in January 2024, the proposal was dropped from further consideration.

Nonetheless, Switzerland has ratified the Hague Trust Convention, which, among other things, allows for the recognition of trusts formed under U.S. law. Even so, estate planners in the U.S. must continue to take into account restrictions under Swiss inheritance law that may invalidate certain trust provisions that take effect at the death of the settlor. Examples include statutory entitlement to Swiss real estate, transfers of Swiss real estate to a remainderman, transfers pursuant to a surviving spouse's marital property rights, and transfers yielding favorable results for the decedent under U.S. tax law.

In addition, problems may be encountered at an earlier point in time, when a U.S. trust – whether foreign or domestic for U.S. income tax purposes – attempts to acquire Swiss real estate. Swiss law contains a statutory authorization requirement when it comes to the acquisition of real estate in Switzerland. The law, known as *lex Koller*,[6] must be respected both at the time of purchase and the time of transfer at the death of the settlor.

In sum, use of a U.S. trust as an estate planning instrument may be subject to significant difficulty when real estate in Switzerland is owned by a trust as part of a will substitute.

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[6] Among other things, *lex Koller* provides that persons who do not have Swiss citizenship and are not resident in Switzerland generally require a permit to purchase real estate in Switzerland.

PRACTICAL EXAMPLE

A practical example illustrates the scope of estate administration issues that may need to be resolved when a U.S. citizen and resident owns real estate in Switzerland at the conclusion of life.

Facts

Married couple A and B are U.S. citizens. At some point in the course of their marriage, the couple moved to Switzerland when A took up a senior position at a Swiss subsidiary of A's employer. While living in in Switzerland, the couple purchased an apartment in Switzerland. As they were resident in Switzerland at the time, they did not require a permit to purchase real estate.

After a few years, couple A and B returned to the U.S.A. They kept the apartment in Switzerland and partly rented it out or used it as a vacation home.

Close to A's retirement, couple A and B determined it was time to pay attention to estate planning. They sought the advice of an American lawyer for their estate planning. He recommended the use of a revocable trust to own the bulk of their estate. This provided the greatest degree of flexibility as to ownership of assets and the transfer of assets to a revocable trust would not be treated as a completed gift during lifetime. The plan did not address the apartment in Switzerland, which continued to be owned as co-owners.

Couple A and B are the beneficiaries and trustees of the trust. The couple are childless. Consequently, a nephew of B was appointed as the beneficiary who would take after the death of the surviving spouse.

Pursuant to the plan, assets were transferred to the trust during the couple's lifetime. Upon the death of the second to die, remaining assets actually owned by the surviving spouse were to be transferred to the trust.

Problems That May Be Encountered

When A dies, no probate proceedings would be carried on in the U.S. for the bulk of his assets in the U.S. that are held in the trust or that are owned as joint tenants with rights of survivorship. Regarding the latter, because A and B are married, the survivor automatically takes over the interest of the deceased spouse. However, Swiss law must be examined with regard to the apartment owned in Switzerland as co-owners in the land register.

Upon A's death, B wants to transfer A's share of the apartment to herself. This will allow her to easily sell the apartment. In order to remove A as owner and to take sole title in the apartment, B must register as a new owner in the land register with regard to the share that was previously owned by A. This requires a so-called disposal transaction and an obligation transaction. The latter registration forms the basis of the transfer of ownership. It may take the form of purchase agreement, a gift agreement or, in the case of inheritance, the certificate of inheritance with an inheritance partition agreement. The certificate of inheritance is the equivalent of probate. In the example, no document of transfer or inheritance exists. Consequently, the land registry in Switzerland likely will refuse to transfer ownership.

In Switzerland, the decedent's estate must be formally opened, limited to the real estate. Opening the estate in Switzerland can be authorized separately under the F.C.E. Treaty, as previously mentioned, or as an ancillary proceeding of the U.S. estate. In either event, the goal is to obtain a certificate of inheritance. For this purpose, an American must be submitted to the Swiss probate authority. The existing trustee (here B) must be appointed as heir in a U.S. will. An extensive translation of the will must be submitted to the Swiss probate authority accompanied by a legal opinion from an American lawyer as to the provisions of the will. If the U.S. will contains detailed dispositive provisions separate and apart from the trust, the process may be straight forward. However, if the will merely provides for a transfer to the trust, additional difficulties may be encountered with the entry in the land register due to the provisions of *lex Koller*.

Steps To Be Taken During Lifetime

This example illustrates that the process of transferring ownership of one-half of the apartment from the deceased spouse to the surviving spouse is much simpler if, during lifetime, each spouse executed a separate Swiss property only will. The problem could pop-up a second time when the surviving spouse dies. B's nephew is a beneficiary of the revocable trust. Again, there is no will. This illustrates that, in the Swiss property only will, each will should appoint B's nephew as heir to take only if, at the time of death, the other spouse is not alive. Such wills are one page or so in length. Nonetheless, they serve as a magic key that eliminates headaches regarding the transfer at death of real estate owned in Switzerland.

Other Issues

Once the transfer of ownership is addressed, Swiss counsel will typically address Swiss inheritance tax at the time of transfer at death. Depending on the degree of consanguinity of the heir, inheritance tax may be charged in Switzerland. The tax base is limited to the property located in Switzerland. Spouses are exempt from inheritance tax. However, depending on the canton, B's nephew will incur inheritance tax of up to 45%, unless the property is located in the cantons of Schwyz and Obwalden, neither of which imposes inheritance tax.

It should also be noted that most people who own real estate in Switzerland typically have a Swiss bank account that is used to pay ancillary costs, taxes, and maintenance in Switzerland. The assets in this bank account constitute movable assets and would therefore not be covered by the F.C.E. Treaty or the jurisdiction in Switzerland for the opening of the estate in Switzerland. The Swiss certificate of inheritance is limited to real estate in Switzerland.

If, in our example, A maintained a separate Swiss bank account, the account would be subject to the inheritance laws of his state of residence in the U.S. An order of a U.S. probate court would need to be provided to the bank in order for the balance in A's bank account to be released. With planning, two alternative paths forward could be followed in order for funds to be released by the Swiss bank. The first is that an executor has been appointed and a certificate of executorship is provided to the bank. The second is that the bank account takes the form of a joint account between A and B during their lifetime. This allows the surviving spouse to dispose of this Swiss bank account even after the death of the other spouse because it is in the name of both spouses.

FORMAL REQUIREMENTS FOR A SWISS WILL

In addition to the contract of inheritance, Swiss law provides for a will, which generally can take two forms. The first is that it is handwritten from beginning to end and signed and dated with the month, day, and year. Alternatively, the will can be made in the form of a public deed. In this case, the will must be witnessed and notarized.

In addition to these two forms of ordinary wills, Swiss law provides for an emergency will, which is used in the event of extraordinary circumstances involving imminent danger of death. In broad terms, the emergency will entails an oral communication to two witnesses who immediately write down the contents and submit them to court authorities or record them with those authorities.

Switzerland also recognizes testamentary dispositions under certain conditions if foreign formal requirements are met. Switzerland is a party to the Hague Convention on the Conflicts of Laws relating to the Form of Testamentary Dispositions (hereinafter "Convention"). According to Article 1 of the Convention, testamentary dispositions are considered valid with regard to their form if they comply with the internal law of any of the following jurisdictions:

- The place where the testator executed the will.
- The place of the testator's nationality, either at the time when the will was executed or at the time of his death.
- The place in which the testator had his domicile either at the time when he made the disposition or at the time of his death.
- The place in which the testator had his habitual residence either at the time when he made the disposition or at the time of his death.
- So far as real estate is concerned, the place where the real estate is situated.

As the foregoing indicates, Switzerland recognizes a broad set of forms of will. In the specific case of Swiss-U.S. estate planning discussed above, either the form of a handwritten will authorized by the place where the property is located (Switzerland) or the form at the testator's last place of residence in the U.S. could be chosen.

RECOMMENDATIONS

The instrument that is best suited to planning a U.S.-Swiss estate depends on the facts involved in the particular matter. The instrument that transfers title to real estate in Switzerland should be a separate will that is limited to the property in Switzerland. As in all cross border matters, legal advice should be taken from legal counsel admitted to practice in the relevant jurisdiction. In the case at hand, that means a competent Swiss lawyer. It is also advisable to appoint a Swiss executor who will take care of the tax declaration for the real estate at the date of death, any assessment and payment of inheritance tax, and the general handling of the estate in Switzerland. Swiss wills are usually rather brief, but their benefits to heirs inheriting Swiss real property can be huge when measured against the costs of cleanup.