

Sham trusts and reserved powers: when courts disregard a structure

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A trust protects assets only as long as it is respected as a genuine structure. Where the settlor continues to treat the assets as their own, creditors, spouses and heirs may argue that the trust should be disregarded.

1 What a sham is

In common law systems, a trust may be treated as a sham where the settlor and the trustee never intended to create the rights and obligations set out in the documents and intended to give a false impression to third parties. The threshold is generally high, because courts presume that documents mean what they say. Evidence typically includes the trustee following the settlor's instructions without independent judgement, the settlor using trust assets for personal expenses and correspondence suggesting that the deed was a formality.

2 Reserved powers and control

Many trusts allow the settlor to retain powers, for example over investments or the appointment of beneficiaries. Reserved powers do not by themselves make a trust a sham, and several offshore jurisdictions expressly permit them. Extensive control can nevertheless support related arguments, for instance that the settlor retained rights equivalent to ownership which form part of their estate or of their assets in divorce or insolvency, depending on the law applied.

3 The Swiss perspective

Switzerland recognises trusts under the Hague Trust Convention, which preserves mandatory rules of the law otherwise applicable, including rules on matrimonial property, succession rights such as compulsory portions

and the protection of creditors. Swiss courts may also consider the prohibition of abuse of rights (Art. 2 para. 2 CC) where a structure is used to circumvent obligations. In addition, transfers that harm creditors may be challenged through avoidance actions under Art. 285 et seq. of the Debt Enforcement and Bankruptcy Act (DEBA), subject to the conditions and time limits set out there.

4 Consequences for creditors, spouses and heirs

If a structure is disregarded or its assets are attributed to the settlor, creditors may enforce against them, spouses may include them in matrimonial property claims and heirs may include them when calculating compulsory portions. The outcome depends on the courts involved and the laws they apply, so the same structure may be treated differently in Hong Kong, Switzerland or elsewhere.

5 What pays off in practice

- **Examine how the trust was run** since the way a trust was administered often decides the case.
- **Obtain trustee records** including minutes and correspondence on distributions.
- **Choose the forum carefully** because jurisdictions differ markedly in their approach to reserved powers.

6 How Ressos Legal helps

I advise creditors, spouses, heirs and trustees on attacking or defending trust structures with links to Switzerland. [Contact me](#) for a first conversation.

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