Trusts in Italy as a living comparative law laboratory

Maurizio Lupoi*

Abstract

This article looks at the development of Italian trust practice under the theory of the trust 'interno' and shows how many acclimatization issues were solved thereby making trusts an efficient legal tool in professional practice. An earlier version of this article was published in *Trusts & Trustees* in June 2012.

The Hague Convention on trusts and conceptual misgivings

The Hague Convention of 1 July 1985 on the law applicable to trusts and their recognition was ratified by the Republic of Italy in 1989 and came into force in 1992.[1]

The general consensus at that time was that the Convention concerned 'foreign' trusts. 'Foreign' is a very vague notion, for no article of the Convention refers to 'foreign trusts'. However, the Convention was conceived in the domain of private international law conventions (the Hague Conference on Private International Law), and it made sense to hold that its purpose was to have a trust 'recognized' in legal systems other than the one to which it belonged (for instance, if the trustee of a New York trust intended to purchase a flat in Venice, the Convention would ensure that he would be recognized as a trustee and that the Venetian notary in charge of the purchase could not raise objections on the basis that trusts were not known in the Italian legal system.

However, it soon appeared that if a 'foreign' trust was to be 'recognized' in Venice as a consequence of the purchase of a flat by a foreign trustee, all obstacles placed by the Italian legal system against trusts had to disappear automatically and in principle. Take the time-honoured civilian misunderstanding that trusts involve two 'real' rights or rights *in rem*, neither of which is recognized by the civil law; how would it be possible that a New York trustee acquired one of those unknown rights over a flat in Venice and the trust's beneficiary the other unknown right while the Italian owners of all remaining flats in the same building could not do likewise? Limitations concerning real property must concern either everybody (*lex loci*) or nobody.

Time has shown that legal structures that mirror the respective positions of trustees and beneficiaries did and at times do exist in the civil law and that trusts in their proper sense can live without a Chancellor and an equity jurisdiction.[2] The civilian misunderstanding rooted in the alleged existence of two 'real' rights or rights *in rem*, however, still lingers on and is fostered by the unwary common lawyer. It might then be useful to explain that its reason rests, as is the case in many other domains of trust law, on an

* Emeritus Professor, University of Genova.

1. The Convention is currently in force in the following states: Australia, Canada (most provinces), China (Hong Kong), Italy, Liechtenstein, Luxembourg, Malta, Monaco, The Netherlands, San Marino, Switzerland, and the UK (and Crown Dependencies).

2. A Hodri-Winogradow, 'Shapeless Trusts and Settlor Title Retention: As Asian Morality Play', forthcoming in Loyola Law Review; LD Smith, 'Trust and Patrimony' (2008) 38 Rev Gén de droit 379; GL Gretton, 'Trusts Without Equity' (2000) 49 Intl Comp L Q 599.

 doi:10.1093/tandt/ttt034

English terminology that is liable to deceive lawyers belonging to different legal systems. By way of example, let us consider tracing. Tracing has often been described as a method to recover trust property. That is of course right, but once it is coupled with the notion that the beneficiary is the equitable owner of the trust fund, the irresistible inference for a civil lawyer is that beneficiaries can sue a third party 'in tracing' and recover the trust fund for themselves (ie the Roman law idea of *rei vindication*, which found its way in the French version of the Hague Convention[3]). A nonsense for sure but a logical assumption as well, given the terms that civil lawyers find in English-language literature.[4]

'Equitable ownership' is equally troublesome for a civil lawyer, for he is told that a legal ownership to trust assets exists side by side with an equitable ownership. Hence, the basic misunderstanding to which I referred above–two 'real' rights or rights *in rem*, neither of which is known in the civil law. One should never surmise the meaning of foreign legal terms, as every student of comparative law knows well, but on the other hand why should a civil lawyer suspect that the meaning of 'ownership' in 'legal ownership' is different from the meaning of 'ownership' in 'equitable ownership'? Indeed it is, for 'equitable ownership' no more than a figurative expression employed by English Chancellors at a loss to find a specific expression to define the entitlements of beneficiaries under the early trusts.

Most civil-law countries, including Italy, have a highly formalized land registration system. They provide an additional difficulty to accommodate trusts within their respective territories unless the two meanings of 'ownership' are disentangled. That is, what occurred in Italy quite soon after the ratification of the Hague Convention. Land registrars objected to registering trustees' titles. It took six judgments from as many Italian courts to clarify this issue and, as a consequence, nowadays trustees regularly register their title as trustees. That does not conform to English practice that has traditionally shied away from registration of trustees' titles, be they on land or on company shares, but is a necessary ingredient in Italian law to protect the trust assets and the interests of the beneficiaries.

The latest trend in Italy, supported by a 2011 decision of the Turin court, is to register title in the name of the trust.[5] Civilians tend to see legal entities whenever they have a chance, but that is not the case here. If you focus on the trust assets and look at the trusts that perform functions very close to the traditional civilian foundation (for instance, trusts that own a university or a hospital or a museum), the drive towards equating them with a juridical person would be well-founded. The assets take precedence, so to speak, over the board of trustees. In addition, tax rules in many countries look at trust income as income of 'the trust'. The latter view prevails in Italy where, since 2007, tax provisions exist that tax the income of the trust assets as if the trust were an entity. That explains why land registration may be in the name of the trust. After all, the trust is a taxpayer.

The 'trust interno'—acclimatization issues

Those were the basic acclimatization issues, yet not the only ones.

First and the foremost was the notion of trust 'interno'. I propounded this notion in 1994 in order to describe a trust formed and operating in Italy with an Italian settlor and an Italian beneficiaries and usually with an Italian trustee. The only foreign element of a trust 'interno' would be its proper law, by necessity a foreign law. The Hague Convention would thus be applicable to a trust 'interno', just as it is applicable to 'foreign' trusts.

3. 'que la revendication des biens du trust soit permise . . .': art 11, third para, d).
4. Cf D Pannatier Kessler, '*Le droit de suite et sa reconnaissance selon la Convention de La Haye sur les trusts*' (2011), ch II.
5. All Italian cases in trust matters are reported in the journal 'Trusts & Attività Fiduciarie'.

The academic reaction was mostly negative and strongly so.[6]

One has to accept that the experts who drafted the Hague Convention on trusts had not considered trusts 'interni' as a possible outcome of the Convention and certainly had no intention to allow trusts to become a permanent fixture of civil-law systems. On the other hand, Italian practitioners took rapidly to the trust 'interno' and, what matters most, courts did likewise, thereby planting the seeds of a widespread acceptance in spite of the many operating difficulties that beleaguer trusts in a civil-law context. For instance, it cannot be denied that in no civilian country can there be an efficient trust administration unless the courts are willing to step in as they would in a traditional trust country. The inherent jurisdiction in trust matters is given for granted by, say, English or American lawyers and is never seen as a topic for discussion when trusts in civil-law countries are discussed. That is one of the very many comparative law shortcomings that affect the present day debate on trusts.

Italian courts have understood this need and have gone so far as to replace trustees (English law was applied in a Milan case), to appoint a new trustee when the trust instrument had no applicable rule for the appointment of a trustee after the death of the initial trustee (Jersey law was applied in a Genoa case) and to approve a variation of the trust instrument where there was a beneficiary under tutorship (English law was applied in a Florence case). It has now become frequent to have court orders sanctioning trusts agreed to by the spouses in a divorce suit or for the administration of assets belonging to the parents of a handicapped child or to support the segregation of assets in favour of the creditors of a company in the context of bankruptcy proceedings. Almost 200 orders or judgments have been handed down by Italian courts (including tax courts) in trust matters over the past 10 years.[7]

The sheer number of judicial rulings shows how widespread the use of trusts 'interni' is in Italy. One is bound to enquire into the causes of this.

What are trusts in Italy for—and fiduciary obligations

The fundamental cause is that trusts provide answers to many shortcomings of Italian law. If an American client sends money to his Italian attorney in order to have the money ready should the purchase of shares of an Italian company that he is negotiating be finalized, he believes that the attorney will place the money in a clients' account. If an American client sends money to his Italian attorney in order to show to the other party of an Italian deal that he has the financial resources to complete the deal, he believes that the attorney will place the money in an escrow account. In other words, in both instances the American client is certain that his money is protected and that his attorney's creditors shall never be able to reach it. That is not so under Italian law. It takes a trust 'interno' to achieve the American client's intended effects.

Italian law conceives of no legal relationship that efficiently goes beyond the life of the parties. One may appoint a testamentary executor to carry out his wishes but an executor must surrender the deceased's estate in its entirety to the heirs of the deceased within one year (exceptionally, within two years) so that there is very little he can usefully do past that period. Under a recent addition to the Italian civil code (article 2645-*ter*), one may segregate land or registered personal property for a beneficiary, but that is no more than a restriction on how that asset may be disposed of and is not coupled with a management structure, certainly not with a management structure that can go beyond the life of the manager.

The notion of 'dedicated patrimony', that is, assets devoted to the furtherance of an objective, is foreign

6. On the academic debate in Italy and on its final outcome, see M Graziadei, 'Recognition of Common Law Trusts in Civil Law Jurisdictions Under the Hague Trust Convention with Particular Regard to the Italian Experience' in L Smith (ed), *Imagining the trust* (Cambridge University Press, 2012) 29; A Braun, 'The Trust Interno', in D Hayton (ed), *The International Trust*, 3rd edn (Jordan Publishing Ltd, 2011) 777–817.

7. On Italian case law, see Graziadei and Braun (n 6).

to current Italian law other than through the formation of an entity, such as a foundation or a company, or through the creation of limitations on the use of the assets in question that act much in the same way as an easement would: they concern the thing, not the obligations of its owner towards those who are intended to benefit.

In this connection, it must be pointed out that also the notion of fiduciary obligation is foreign to current Italian law. Again, words may play dangerous tricks: there are 'fiduciary agreements' in Italy, but they have nothing to do with trusts. The concept of 'fiduciary agreement' goes back to the German doctrine of the late XIX and early XX century ('fiduziarische Geschäft')) and is no more than a mandate coupled with the transfer of assets to the fiduciary. He has to deal with the assets as provided for in the fiduciary agreement, but third parties are not bound by that agreement, so that those assets are seen by the law as owned by the fiduciary and are available to his creditors. Moreover, the fiduciary has a duty towards the party who appointed him and not to the beneficiaries (the latter being a notion that is foreign to the civilian theory of fiduciary agreements). Beneficiaries may well not exist at all and, if they do, they can at most be seen as the recipients of a contract in favour of third parties. That does not create any fiduciary obligation of the fiduciary towards them.

Italy also has 'fiduciary companies' but they are not trust companies, they simply perform the role of a fiduciary under a 'fiduciary agreement' and are subject to State supervision. The advantage of contracting with a fiduciary company is that the assets they receive are considered not to belong to them. That is so because those assets still belong in the eyes of the law to the party who entered into the fiduciary agreement. Not a shade of trusts can be detected in these arrangements.

The lack of the notion of 'fiduciary obligation', as understood in the common law, is crucial. Trusts are but one of the relationships that are worthy of protection because of their fiduciary nature. A still not totally explored domain exists in this respect in the common law[8] and most of its components stem from 'confidence', a notion that left Europe's *ius commune* or common law in the 15th to 16th centuries to become embedded in English law, as is apparent from the long-standing expression 'trust and confidence'; on the Continent, it progressively lost ground and significance.[9] 'Confidence', according to many, is at the root of the trusts and fiduciary obligations. The semantic area of 'confidence' is both very wide and subject to change over time. Hence, its prowess to encompass varying situations as they come to the attention of the courts and to provide a protection that a stricter conceptual system would be unable to achieve. It may be that the growing civilian familiarity with trusts shall bring 'confidence' back to its original lands.

There are signs that there is more than a mere possibility for this. Trusts 'interni' could have been used by Italians as a means to hide their assets and to defeat their creditors, let alone those family members who are entitled by law to a share of the decedent's estate. That has neither occurred nor have the trusts been devoted primarily to the management of wealthy estates. One of the peculiarities of trusts 'interni' is that they care primarily for everyday occurrences, in respect of which the shortcomings of Italian law are easily apparent. The fact situations I shall now summarily refer to correspond to the most common occurrences of trusts in Italy and cannot be efficiently dealt with in Italian law other than by means of a trust.

Separation or divorce agreements where assets of one of the spouses are to be put in order to become owned by the children of the marriage at a given date or upon a certain occurrence; in the meanwhile, those assets must be segregated and properly managed either by one of the spouses in a fiduciary capacity or by a third party.

8. A Scott, 'The Fiduciary Principle' (1949) 37 Calif LR 539; LS Sealy, 'Some Principles of Fiduciary Obligation' (1963) Cambridge LJ 119; EJ Weinrib, 'The Fiduciary Obligation' (1975) 25 Univ Toronto LJ 1; PD Finn, *Fiduciary Obligations* (Cambridge University Press 1977); T Frankel, 'Fiduciary Law' (1983) 71 Calif LR 795; R Flannigan, 'The Fiduciary Obligation' (1989) 9 Oxford J Leg St 285; P Birks, 'The Content of Fiduciary Obligation' (2000) 34 Isr LR 3.

9. M Lupoi, 'Trust and Confidence' (2009) 125 LQR 253.

The fate of a handicapped child (especially of a mentally handicapped child) after the death of his or her parents—he or she would probably own no assets in his or her own right and his or her future livelihood and personal care will thus depend on the assets that his or her parents will have devoted for that purpose without actually transferring them to him or her. Of course, there can be a tutor appointed by the court to look over those assets, but a tutor does not have to take care of the personal needs of his or her pupil (which in the case of a handicapped person may be of paramount importance) and, furthermore, the deceased parents of the pupil cannot give binding instructions to a tutor. The insufficiency of the tutorship is shown by the fact that some civil-law countries, such as the Spanish region of Cataluña, have enacted specific statutes to cope with those situations (Spain had enacted a national law in 2003 on this same subject matter but it was felt that it had not gone far enough to insulate the assets devoted to the handicapped person).

Setting aside an asset to assure that certain conditions relating to a transaction will be fulfilled—a pledge over a movable asset would take that asset away from its owner, whereas a hypothec would require a cumbersome procedure to be created, enforced and, if need be, extinguished. On the other hand, once the asset in question becomes subject to a trust, the interests of the parties involved are properly protected.

Skipping one generation in business matters—that is a common occurrence in the United States but it meets the obstacle of the reserved shares of family members in most civil-law jurisdictions. The majority of Italian businesses are family-owned and it is not unlikely that no child of the owner of the business is apt to take over from him or her. A sale of the business is usually ruled out; the hope of the owner being that the second generation of his or her descendants will succeed where the first generation has failed. The first generation will receive the income of the business in the meanwhile.

Skipping one generation in family matters—that concerns families where the head of the family also owns non-business assets and has little confidence that his children shall keep them within the family (at times, some of the assets have been owned by that family for centuries). There may be unmarried children without any obligation to keep a significant part of their assets within the family, divorced children, spendthrift children, and so on. The first-generation descendants will not only enjoy the income produced by the assets but also hold powers to direct the trustee as to their management and their disposition. Their position will thus be very close to the position of an owner, but they will never receive any part of the capital.

Some of the structures I have just outlined conflict with Italian succession law in that they deprive one or more family members of their respective entitlements. The legal consequence of transferring assets to a trustee rather than, by gift or will, to the family members in whose favour the law reserves a share of the estate of the decedent is not, however, that the transfers are void. They are and remain perfectly valid, without prejudice to the claim of a family member to have them set aside to the extent that is necessary to make him receive the reserved share provided by the law in his favour. In spite of the many occurrences of trusts 'interni' that would come within this rule, there has not been a single instance of a claim by a prejudiced family member until now. That shows the strength of family ties in Italian society and the respect paid to the wishes of a deceased parent. It probably also shows that the provisions of the trust instruments in question were reasonable and did not unduly prejudice the first-generation descendants.

Italian trust instruments under a foreign law—more acclimatization issues

Trust instruments creating trusts 'interni' are of course drafted in Italian in spite of their being subject to a foreign law. Hence, two sets of problems.

Some English terms cannot be translated; therefore, 'trust' and 'trustee', just as 'charitable trust' and 'wilful default' are kept in English. The translation of

other terms is possible but may be misleading; therefore, 'power of advancement' or 'protective trust' are translated into Italian, but the corresponding English terms are added in parenthesis. Other terms can be translated without difficulty; for instance, 'protector' or 'enforcer' are translated as 'guardiano'.

The acclimatization of trusts calls for the insertion into trust instruments of provisions that find no counterpart in foreign models, for trusts, just like any legal institution, cannot be transplanted into a foreign legal system without heeding the reactions of the receiving system. It is not a matter of adapting trusts. That cannot happen because the theory of trusts 'interni' subjects any trust 'interno' to a specific foreign law and as a consequence, a trust 'interno' has to abide by that law. It is a matter of modifying the working of trusts to make them conform to the applicable principles and rules of Italian law without in any way impinging on the foreign trust law by which they are governed. A good instance of this mechanism concerns the acts performed by a trustee. Italian trust instruments require the trustee to hold himself out as a trustee whenever he enters into a contract or registers title to land. That is not required by any foreign law and yet does not contradict any foreign law in that trusts 'interni' deal with Italian assets.[10] At the same time, it follows Italian law rules relating to acts, the consequences of which do not affect the personal assets of the person who performs the act. Here, as in many other domains, rules of procedure and of evidence interact with rules of substance. A defendant before an English court may prove by his own testimony, as well as by the testimony of other people, that a bank account he has opened in his own name is a trust account and that the money deposited into that account is not his own money. That would be most difficult before an Italian court, if not outright impossible, and explains why Italian trustees are bound to hold themselves out as trustees in every possible circumstance and to label every asset, including a bank account, as a trust asset (actually, as an asset included in the fund of a specific trust).

Acclimatization issues do not stop here.

The traditional English trust deed does not always recite what the intention of the settlor and the purpose for which the trust is being formed are; indeed, it traditionally only recited that property had been transferred to A. e B. and then it set out the terms of the trust. Such a structure does not sit easily with a civil-law context, where property cannot be conveyed without showing a cause and, additionally, where the choice of a foreign law to govern a relationship that would otherwise be governed by the local law calls for an explanation when, as is the case with trusts, it allows the parties to achieve objectives that could not be achieved under the local law. Italian trust instruments regularly recite the intention of the settlor and the purpose of the trust. Once again, let us be cautious with words. Every trust has a purpose even when it is a trust for beneficiaries and there is nothing wrong in setting out that purpose in the trust instrument.

One might object that it is obvious that trustees must act in the interest of the beneficiaries, what other purpose could there be? This matter, however, is not so easily disposed of, for 'the interest of the beneficiaries' is only a catch-sentence does not catch the actual structure of modern trust instruments. They usually allow the trustees to consider the interests of one or more beneficiaries, disregarding the interests of all other beneficiaries and everyday experience sh\ows beneficiaries at odds with each other in pursuit of diverging interests. The commonly held view that a trustee does not have to provide any explanation as to how he has exercised his discretion is a compounded factor to the effect that 'the interest of the beneficiaries' has little, if any, meaning left.

Another acclimatization issue concerns the structure of trust instruments as unilateral acts. It is a basic tenet of trust law that trusts are not contracts.[11]

10. For instance, shares of an Italian company. The trustee will be entered in the register of members as trustee; that would run against s 126 of the Companies Act 2006 if the company were an English company.

11. See, however, JH Langbein, 'The Contractarian Basis of the Law of Trusts' (1995) 105 Yale LJ 625.

That does not imply that trust instruments might not be seen as 'contrats' in French law, just as the French *fiducie* is a 'contrat'. The same could be said with reference to 'contratti' under Italian law. Here, we have a simple comparative law issue, since it is well known that common law contracts do not correspond to 'contrats' or 'contratti', but the question remains open: are trusts 'contrats' or 'contratti' in spite of their not being contracts? It is equally well known that the word 'trust', just as the expression 'fiduciary obligation',[12] encompasses nowadays a wide array of legal arrangements, so that one might query whether it should be appropriate to devise new terms in order to identify as many categories of trusts. Trusts for purposes, for instance, have very little in common with trusts for beneficiaries. The same could be said of trusts for creditors compared with trusts for family members. It could be argued that some trust types are contracts, while others are not. Even so, the comparative law issue would remain unsolved.

I would submit that under Italian law, trusts must be seen as 'accordi' (agreements) and kept outside the area to which 'contratti' belong, basically because 'contratti' entail an action for breach that terminates the contract. That would be a mischief and it would deny the very essence of trusts. A trust must go on in spite of a breach by its trustee and that is what occurs in trust law. Fiduciary law rules ensure that fiduciaries do not proffer compensation and keep illegal profits.[13] Should it be any different, we would be facing a different legal institution.

Conclusion

The interplay between foreign trust law and Italian law is as complex as the interplay between foreign-established practices and the developing Italian trust practice. At the same time, issues that foreign lawyers have seldom canvassed in depth have come to the fore. Trusts 'interni' are a living comparative law laboratory.

Maurizio Lupoi *has published extensively in comparative legal matters. Two of his books, originally in Italian, were translated and published by Cambridge University Press: The Origins of the European Legal Order and Trusts, both in 2000. His book on the drafting of trust instruments in Italian has set the current standard in Italy. He teaches Comparative Legal Systems and The Law of Trusts at the University of Genoa. Email: maurizio.lupoi@unige.it*

12. Birks (n 8).
13. J Getzler, '"As if." Accountability and Counterfactual Trust' (2011) 91 Boston Univ L R 973.