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Panel on Financial Affairs
Meeting on 1 March 2010

Background brief on review of the Trustee Ordinance and related matters

Purpose

This paper sets out background information on the review of the Trustee Ordinance (Cap. 29) (TO) and related matters, and provides a summary of the views and concerns expressed by members when the subject was discussed at the meeting of the Panel on Financial Affairs (FA Panel) on 6 July 2009.

Background

Existing trust law regime

2. The trust law regime in Hong Kong is mainly based on the principles derived from rules of equity. They are supplemented by several pieces of legislation including the TO and the Perpetuities and Accumulations Ordinance (Cap. 257) (PAO). The TO was enacted in 1934, based on the Trustee Act 1925 of the United Kingdom (UK). Other than the range of authorized investments in its Schedule 2, the TO has not been substantially reviewed since its enactment. The PAO was enacted in 1970, based on UK's Perpetuities and Accumulations Act 1964, to amend the common law rules regarding perpetuities and accumulations of income. The PAO has not been reviewed since its enactment.

Review and consultation

3. In August 2007, the Joint Committee on Trust law Reform, which was formed by the Hong Kong Trustees' Association and the Society of Trust and Estate practitioners, submitted proposals to the Government, advocating a comprehensive review of the trust law regime. The review of the provisions in the TO was included as a new initiative in the Policy Agenda of the 2007-08 Policy Address. The Administration started the review in early 2008 with the following aims:

- (a) to modernize the trust law to facilitate more effective trust administration;
- (b) to reform the TO for the protection of, and to offer guidance to settlors, trustees and beneficiaries by prudential default provisions;
- (c) to clarify issues and uncertainties in the existing law; and
- (d) to promote the wealth management business in Hong Kong.

4. As part of the review exercise, the Financial Services and the Treasury Bureau published a “Consultation Paper on Review of the Trustee Ordinance and Related Matters” on 22 June 2009 to consult the public on the proposals to reform the TO and the law relating to trusts. The consultation lasted for three months. The Administration then aimed to introduce the relevant legislative amendments into the Legislative Council in 2010-2011.

Deliberations of the Panel

5. At the FA Panel meeting on 6 July 2009, the Administration briefed members on the main legislative proposals which cover those issues that are relatively more straight-forward and have been reviewed in some comparable common law jurisdictions such as the UK and Singapore. A list of these legislative proposals is given in **Appendix I**. The major areas covered by these proposals include: -

- (a) trustees’ powers in relations to investment, delegation to another trustee, employment of nominees and custodians, insurance of trust property and charging of remuneration;
- (b) trustees’ duty and standard of care and exemption clauses;
- (c) beneficiaries’ right to information relating to trust and to remove trustees; and
- (d) rules against perpetuities and excessive accumulations of income.

6. At the meeting, the Administration also presented a number of issues on which it needs to hear more views before forming definitive proposals on them. These issues mainly cover trustees’ power to appoint agents to carry out fiduciary functions, remuneration of trustees of charitable trusts, role of protectors, reserved powers of settlors, governing law of trust, non-charitable purpose trusts and forced heirship rules in relation to the TO. A list of these issues is given in **Appendix II**.

7. Panel members gave the following concerns and views at the Panel meeting on 6 July 2009: -

- (a) the general public might not possess the expertise to give comments on the legislative proposals which involved highly technical issues;
- (b) in the public consultation exercise, the interests of beneficiaries might not be equally represented as those of the trustees as there was no particular organization representing the interests of the beneficiaries;
- (c) the Administration should consult the relevant professional bodies and the legal profession requesting them to provide views from the perspective of their clients who were beneficiaries;
- (d) review of the trust law regime based on the reform experience in UK was inadequate and the Law Reform Commission should be asked to study the proposals to ensure adequate protection of the interests of beneficiaries;
- (e) as the permissible investments contained in Schedule 2 of the TO included debentures which might include high risk structured products as revealed after the Lehman Brothers Minibonds incident, the Administration should address the concern in the review.

8. Acknowledging that the subject of the review was highly technical, the Administration advised that it had considered inviting the Law Reform Commission to study the review proposals. This had not been pursued in the light of the advice of the Department of Justice (DoJ) that Hong Kong could leverage the reform experience in overseas jurisdictions. Apart from the reform of the Trustee Act in UK, the Administration had also made reference to the reform experience/proposals of other jurisdictions. In view of members' concern, the Administration undertook to further discuss with DoJ to determine whether a study by the Law Reform Commission should be pursued.

9. On the concern that "debentures" in the TO might include high risk structured products, the Administration advised that the definition of "debenture" under Schedule 2 of the TO might be amended to narrow down the scope of permissible investments by excluding any "structured products". Such amendment would tie in with any amendment to the definition of "debenture" under the Companies Ordinance rewrite exercise.

10. At the Panel's request, the Administration has provided supplementary information (**Appendix III**) on the comparison between the Administration's proposals to reform Hong Kong's trust law regime and the trust statutes of some common law and offshore jurisdictions.

Recent development

11. The Administration will brief the FA Panel at the meeting on 1 March 2010 on the progress of the review and outcome of the public consultation.

Relevant papers

12. The relevant papers are available at the following links:

Consultation Paper on Review of the Trustee Ordinance and Related Matters (June 2009)

<http://www.legco.gov.hk/yr08-09/english/panels/fa/papers/fa0706cb1-2094-e.pdf>

Administration's paper on "Review of the Trustee Ordinance and Related Matters" (June 2009)

<http://www.legco.gov.hk/yr08-09/english/panels/fa/papers/fa0706cb1-2095-2-e.pdf>

Minutes of the FA Panel meeting on 6 July 2009 (Paragraphs 37 to 45)

<http://www.legco.gov.hk/yr08-09/english/panels/fa/minutes/fa20090706.pdf>

Paper to follow up the FA Panel meeting on 6 July 2009: Comparison between the Trust Law reforms proposed by the Administration and the Trust Statutes of selected jurisdictions

<http://www.legco.gov.hk/yr08-09/english/panels/fa/papers/fa0706cb1-2394-1-e.pdf>

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Main legislative proposals

- (a) Introduce a statutory duty of care for trustees.
- (b) Retain the range of authorized investments defined in Schedule 2 to the TO, subject to review from time to time to keep up with market needs and evolving market circumstances.
- (c) Enhance the safeguard in temporary delegation of trustees' powers so that the number of trustees will not be reduced to one which is against the will of the settlor.
- (d) Repeal section 8(3)(a) of the Enduring Powers of Attorney Ordinance (Cap. 501) so that the power of delegation by an individual trustee is entirely governed by the TO¹.
- (e) Provide trustees with a general power to employ nominees and custodians with necessary safeguards².
- (f) Empower trustees to insure any trust property against risks of loss or damage by any event and pay premiums out of the trust funds³.
- (g) Provide a default charging clause in the TO that enables the remuneration of professional trustees of non-charitable trusts.
- (h) Subject the trustee exemption clauses seeking to exempt professional trustees who receive remuneration for their services to some statutory control. In this connection, relevant professional bodies should promulgate a code of practice in relation to the use of trustee exemption clauses.
- (i) Provide certain basic rules regarding beneficiaries' right to disclosure by trustees of information, accounts and documents relating to the trust.
- (j) Provide an alternative court-free route for beneficiaries, who are of full age and capacity and are absolutely entitled to the trust property, to remove a trustee.
- (k) Reform the rule against perpetuities (RAP⁴) by either abolishing the rule altogether or by introducing a fixed perpetuity period.
- (l) Abolish the rule against excessive accumulations of income (REA⁵).

¹ The repeal resolves the inconsistencies caused by the overlapping provisions in the Enduring Powers of Attorney Ordinance and the TO

² The safeguards aim at protecting the interests of the beneficiaries against any potential risk posed by the trustee's power to employ nominees and custodians

³ Existing TO does not empower trustees to insure any loss or damage by events other than fire and typhoon and only empowers trustees to pay insurance premiums out of the income of trust properties.

⁴ RAP under common law was varied by the PAO in 1970 which specifies that trusts created after 13 March 1970 are subject to a statutory "wait and see" rule such that the creation of a future estate or interest is not invalidated until it becomes apparent that the future estate or interest must vest outside the perpetuity period. For the purposes of the "wait and see" rule, the PAO also prescribes persons who could be used as lives in being. On the other hand, settlors may choose a fixed perpetuity period of not exceeding 80 years.

⁵ REA under sections 17 to 20 of the PAO provides that settlors of trusts may choose one of the six statutory accumulation periods for which the income of a trust may be accumulated.

Issues inviting more views before forming definitive proposals

- (a) Whether trustees should be given a wider default power to appoint agents who may exercise asset management functions, such as discretionary fund managers.
- (b) Whether trustees' power of appointing agents as mentioned in (a) above should be applied to charitable trusts but with some refinement.
- (c) As for charitable trusts, whether professional trustees should be allowed to charge a reasonable amount for their services in the absence of a charging provision in the trust instruments and what constraints should be imposed if they are allowed to so charge.
- (d) Whether REA should be retained in some form with regard to charitable trusts.
- (e) Whether the role of protectors of trusts should be defined in the TO.
- (f) Whether the law should provide that a trust will not be invalidated by certain reserved powers of settlors.
- (g) Whether the common law principles in relation to the governing law⁶ of trusts should be codified.
- (h) Whether statutory provisions should be introduced to the effect that forced heirship rules will not affect the validity of trusts.
- (i) Whether non-charitable purpose trusts should be allowed

⁶ Question to the governing law of the trust arises when a trust has links with more than one country. The rules regarding the governing law of trusts are mainly found in common law until supplemented by the "Hague Convention on the Law Applicable to Trusts and on their Recognition" (Hague Convention). The Hague Convention was incorporated into the laws of Hong Kong by the Recognition of Trusts Ordinance (Cap. 76) in 1990. Article 6 of the Hague Convention provides that a trust shall be governed by the law chosen by the settlor, and Article 7 provides that where no applicable law has been chosen, a trust shall be governed by the law with which it is most closely connected, having particular regard to the place of administration of the trust designated by the settlor, the situs of the trust assets, the place of residence or business of the trustee, and the objects of the trust and the places where they are to be fulfilled.

Comparison between the Administration’s Proposed Trust Law Reforms and the Trust Statutes of Selected Jurisdictions¹

	Hong Kong Existing Position²	Hong Kong Reform Proposals³	United Kingdom⁴	Singapore⁵	Cayman Islands⁶	British Virgin Islands⁷
Trustee’s duty of care	No general statutory duty of care	Introduce a general statutory duty of care	Statutory duty of care	Statutory duty of care	No general statutory duty of care	No general statutory duty of care
Trustees’ general power of investment in default of express provisions in the trust instrument	Limited to investments authorised in Schedule 2 to the TO	Retain the range of authorised investments in Schedule 2 to the TO, subject to modifications and periodic reviews	General power of investment by trustees	General power of investment by trustees	Power of investment limited to certain categories (but including securities in which trustees in England are allowed to invest)	General power of investment by trustees

¹ These jurisdictions are selected because:

- (a) our review proposals have made reference to the recent reforms in the UK and Singapore; and
- (b) the trust laws of Cayman Islands and British Virgin Islands are more commonly adopted as the governing law for trusts created in Hong Kong.

² Mainly with reference to the Trustee Ordinance (Chapter 29) (“TO”), the Perpetuities and Accumulations Ordinance (Chapter 257) and the Recognition of Trusts Ordinance (Chapter 76).

³ See Consultation Paper on the Review of the Trustee Ordinance and Related Matters (June 2009).

⁴ UK Trustee Act 1925, UK Trustee Act 2000, UK Trusts of Land and Appointment of Trustees Act 1996 and UK Perpetuities and Accumulations Bill.

⁵ Singapore Trustees Act (Chapter 337).

⁶ Cayman Islands Trusts Law (2007 Revision).

⁷ British Virgin Islands Trustee Ordinance 1961 (Chapter 303).

	Hong Kong Existing Position	Hong Kong Reform Proposals	United Kingdom	Singapore	Cayman Islands	British Virgin Islands
Trustee's Power to delegate to sole co-trustee	No delegation to sole co-trustee, except for trust corporation	Retain the restriction on delegation to sole co-trustee with augmented safeguards	No restriction on delegation to sole co-trustee	No restriction on delegation to sole co-trustee	No provisions on delegation	No restriction on delegation to sole co-trustee
Trustees' power to employ agents	General power of appointing agents except for fiduciary functions	Invite views on whether trustees should be given a general power of appointing agents even for some fiduciary functions ⁸	General power of appointing agents even for some fiduciary functions ⁹	General power of appointing agents even for some fiduciary functions ¹⁰	General power of appointing agents except for fiduciary functions	General power of appointing agents except for fiduciary functions
Trustees' power to employ nominees and custodians	No general power to employ nominees and custodians	Introduce a general power to employ nominees and custodians	General power to employ nominees and custodians	General power to employ nominees and custodians	No general power to employ nominees and custodians	No general power to employ nominees and custodians
Trustees' power to insure	Power to insure against loss or damage by fire and typhoon	Power to insure against loss or damage by any event	Power to insure against loss or damage by any event	Power to insure against loss or damage by any event	Power to insure against loss or damage by fire	Power to insure against loss or damage by fire

⁸ The proposed power/provision may not be applicable to charitable trusts subject to public views.

⁹ Power of appointing agents is different between non-charitable trusts and charitable trusts.

¹⁰ See footnote 9.

	Hong Kong Existing Position	Hong Kong Reform Proposals	United Kingdom	Singapore	Cayman Islands	British Virgin Islands
Professional trustees' entitlement to receive remuneration	No default charging provision for professional trustees	Introduce a default charging provision for professional trustees ¹¹	Default charging provision for professional trustees ¹²	Default charging provision for professional trustees	No default charging provision for professional trustees	No default charging provision for professional trustees
Trustees' exemption clauses	No control on trustee exemption clauses	Subject professional trustees' exemption clauses to control	No control on trustee exemption clauses	No control on trustee exemption clauses	No control on trustee exemption clauses	No control on trustee exemption clauses
Beneficiaries' right to information	No provision on beneficiaries' right to information	Provide in statute certain basic rules regarding beneficiaries' right to information	No provision on beneficiaries' right to information	No provision on beneficiaries' right to information	No provision on beneficiaries' right to information (save for (i) exempt trusts which require information to be provided to the Registrar of Trusts and (ii) Special Trusts ¹³ which may	No provision on beneficiaries' right to information (save for purpose trusts which require information to be provided to enforcers)

¹¹ See footnote 8.

¹² The default provision is not applicable to charitable trusts.

¹³ Those trusts, including non-charitable purpose trusts, permitted under Part VIII of the Cayman Islands Trusts Law (2007 Revision).

	Hong Kong Existing Position	Hong Kong Reform Proposals	United Kingdom	Singapore	Cayman Islands	British Virgin Islands
					require information to be provided as if the enforcer is a beneficiary)	
Removal of trustees by adult beneficiaries who are absolutely entitled	No express provision in the TO but court may order substitution of trustees	Provide an alternative court-free route for these beneficiaries to remove trustees	Provide an alternative court-free route for these beneficiaries to remove trustees	No express provision but court may order substitution of trustees	No express provision but court may order substitution of trustees	No express provision but court may order substitution of trustees
Rule against perpetuities	Allow settlor to set a perpetuity period not exceeding 80 years but not mandatory	Abolish the rule against perpetuities altogether OR Introduce a fixed perpetuity period	A bill has been introduced to replace the existing common law and statutory perpetuity periods with a single perpetuity period of 125 years.	A single perpetuity period of 100 years	The rule against perpetuity does not apply to the Special Trusts (for other trusts, a single perpetuity period of 150 years)	The rule against perpetuity does not apply to purpose trusts (for other trusts, settlor may set a perpetuity period not exceeding 100 years)
Rule against excessive accumulations of income	Choice among six statutory accumulation periods for which the income of a	Abolish the rule against excessive accumulations of income so that income can be	A bill has been introduced to abolish the rule against excessive accumulations of	Income can be accumulated for the duration of the trust	Income can be accumulated for the duration of the trust	Income can be accumulated for the duration of the trust

	Hong Kong Existing Position	Hong Kong Reform Proposals	United Kingdom	Singapore	Cayman Islands	British Virgin Islands
	trust may be accumulated	accumulated for the duration of the trust ¹⁴	income so that income can be accumulated for the duration of the trust ¹⁵			
Defining “protectors” of trust and their functions and duties	No definition of “protectors”	Invite views on whether “protectors” and their functions and duties be defined	No definition of “protectors”	No definition of “protectors”	No definition of “protectors” but has made reference to the term	Contain provisions on protectors
Reserved powers of settlors	No statutory provision	Invite views on whether to allow the settlor to reserve certain powers	No statutory provision	Settlor can reserve the power of investment or asset management functions	Wide range of powers can be reserved by settlors	Wide range of powers can be reserved by settlors
Governing law of trusts	Mainly governed by the Hague Convention on the Law Applicable to Trusts and on their Recognition (“Hague Convention”)	Propose maintaining the status quo	Mainly governed by the Hague Convention	Not signatory to the Hague Convention No specific provisions on governing law of trusts	The Hague Convention not applicable in Cayman Islands Have statutory provisions on the governing law of	Mainly governed by the Hague Convention

¹⁴ See footnote 8.

¹⁵ UK Perpetuities and Accumulations Bill retains a 21-year restriction on accumulation for charitable trusts.

	Hong Kong Existing Position	Hong Kong Reform Proposals	United Kingdom	Singapore	Cayman Islands	British Virgin Islands
					trusts	
Forced heirship	No statutory provisions to shore up the supremacy of Hong Kong trust laws over forced heirship rules	Invite views on whether to introduce statutory provisions to shore up the supremacy of Hong Kong trust laws over forced heirship rules	No statutory provisions to shore up the supremacy of its local trust laws over forced heirship rules	Statutory provisions to shore up the supremacy of its local trust laws over forced heirship rules	Statutory provisions to shore up the supremacy of its local trust laws over forced heirship rules	Statutory provisions to shore up the supremacy of its local trust laws over forced heirship rules
Non-charitable purpose trusts	Non-charitable purpose trusts generally void	Invite views on whether non-charitable purpose trusts should be allowed	Non-charitable purpose trusts generally void	Non-charitable purpose trusts generally void	Non-charitable purpose trusts are allowed	Non-charitable purpose trusts are allowed