



26 March 2013

Private and Confidential

(By email at bc_03_12@legco.gov.hk and by post)

The Hon. Ng Leung-sing, JP
Chairman, Bills Committee
Legislative Council Complex
1 Legislative Council Road
Central
Hong Kong

Dear Mr. Ng,

Trust Law (Amendment) Bill 2013

We attach a submission addressed to the Bills Committee which contains our views on the Bill generally and specifically on the two additional areas we consider critical to giving Hong Kong an edge over competing jurisdictions, especially Singapore.

Please do not hesitate to call if you would like us to elaborate on any of the Submission's contents. Thank you for giving us the opportunity to make this Submission.

Yours sincerely,

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** JCTLR – a joint committee of The Society of Trust & Estate Practitioners (STEP) Hong Kong Branch and The Hong Kong Trustees' Association Ltd (HKTA)*

Cc: Ms Ka Shi Lau, Chairman, HKTA
Ms Sam Bradley, Chairman, STEP Hong Kong
Ms Carolyn Butler, Co-Chair, JCTLR



**SUBMISSION to LEGO BILLS COMMITTEE
in respect of the Trust Law (Amendment) Bill 2013
26th March 2013**

EXECUTIVE SUMMARY

1. The Amendment Bill makes significant improvements to Hong Kong's trust law and thus will help make Hong Kong a more attractive place from which to administer trusts.
2. The Financial Affairs Panel of the LegCo Bill's Committee requested us to comment generally on the Amendment Bill and to list two additional changes we consider critical to giving Hong Kong an edge over competing trust administration jurisdictions, especially Singapore.
3. After careful consideration, we consider that new provisions (i) giving statutory effect to clauses in trust deeds which relieve trustees from management and supervisory obligations with respect to underlying companies in certain situations and correspondingly exonerate them from claims in relation to such companies ("anti-Bartlett v Barclays" provisions) and (ii) recognizing the validity of non-charitable purpose trusts ("NCPTs") which comply with requirements of certainty and legality, would greatly assist Hong Kong in regaining its place as the region's premier trust administration jurisdiction.
4. The anti-Bartlett v. Barclays provision gives settlors certainty that they can control family companies owned by trusts; this is something particularly in demand in our region where so much business and wealth remains in families. The provision adds certainty by confirming in statute the common law principle that because trustee's duties regarding underlying companies are not core, irreducible duties a trustee owes to beneficiaries, a trustee may be relieved of them by express language in the trust instrument.
5. NCPTs are unique vehicles because (i) their "purpose" is hardwired into their constitution and enforceable in court by a nominated person and (ii) they are not owned by anyone. This makes them very useful in many legitimate commercial transactions which call for a neutral party to be entrusted to carry out a specific purpose of the transaction without being controlled by or subject to the claims on persons who would otherwise own such entities.
6. Both the anti-Bartlett v. Barclays provision and NCPTs are in place in many other respectable jurisdictions, are by no means radical in concept or difficult to draft and would give Hong Kong a significant edge over the competition, especially Singapore.



SUBMISSION
To
LEGO BILLS COMMITTEE
in respect of the
Trust Law (Amendment) Bill 2013
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1. General Overview:

- 1.1 The FSTB brief to the Legislative Council states that “it is imperative for Hong Kong to modernize its trusts laws”, because of “recent trust reforms by some major common law jurisdictions like UK and Singapore to facilitate trust administration and to attract more trust businesses.”
- 1.2 If the intention of the amendments is to assist Hong Kong to attract trust business, then UK is not the correct benchmark. Changes in UK trust law have certainly been made to better facilitate trust administration but have not been designed to attract foreigners to make trusts governed by UK law nor to have UK resident trustees. The UK is not interested in being a centre for offshore trust administration.
- 1.3 Singapore’s changes were certainly intended to attract trust business into Singapore and for the creation of trusts governed by the law of Singapore with Singapore resident trustees. However, Singapore also benchmarked itself on UK and there are views being expressed in Singapore that the changes did not address some much needed solutions with the result that business has been lost to other jurisdictions offering such solutions.
- 1.4 Whilst we applaud the intention of the Government of Hong Kong to “to bolster the competitiveness of Hong Kong’s trust services industry and attract settlors to set up trusts in Hong Kong”, we must hope that the changes proposed, which we welcome wholeheartedly, will be sufficient to do this. We feel however that, with the changes proposed, it is likely that some, perhaps many advisers in Hong Kong and elsewhere will continue to turn to the use of other governing law to achieve intended and legitimate solutions not available under the Hong Kong law as presently proposed to be amended.
- 1.5 LEGCO (via the FA Panel) has invited us to both comment on the changes proposed by the Bill and also to suggest two additions which we believe are critical to achieve the

competitiveness intended. This submission covers two provisions for consideration by the Bills Committee.

- 1.6 We wish to express our gratitude to the Government of Hong Kong for the considerable work and efforts it has expended over the last eight years and we certainly do not wish the proposals invited from us to delay the passing of the present Amendment Bill which is urgently needed.

2. Submissions on the Bill:

- 2.1 In 2002 the Hong Kong Trustees Association (“HKTA”) and STEP Hong Kong (“STEP”) asked for and obtained detailed advice on proposed changes to the trust law of Hong Kong. This advice was updated in 2007.
- 2.2 HKTA and STEP formed their Joint Committee on Trust Law Reform (“JCTLR”) and JCTLR has had the benefit of many discussions with the Government of Hong Kong and have taken part in several consultation exercises over the period. JCTLR has been invited to provide its views both on the proposed amendments and on additions to them.
- 2.3 JCTLR has done a thorough comparison of trust laws of 18 different jurisdictions (including Hong Kong) on 22 different aspects of the law and the exercise highlights some important provisions that are currently not included in the Amendment Bill.
- 2.4 The introduction of the statutory duty of care for trustees and the introduction of default powers for trustees of investment, delegation (including nominees and custodians), remuneration and insurance are similar to those of the UK, which have also been followed by Singapore. This method of heightening the responsibilities of trustees and sharpening the performance required of them is for the good of the industry as a whole.
- 2.5 It is proposed to permit perpetual trusts. Some jurisdictions still adhere to a maximum fixed period for a trust (for example: Cayman 150 years, UK 125 years and Singapore 100 years) but the modern trend is to permit perpetual trusts. We welcome this.
- 2.6 Similarly, the Bill removes the limitations on the period during which the income of a trust can be accumulated. This too accords with modern practice and the wishes of settlors and is welcomed.
- 2.7 The prevention of an express provision in a trust deed enabling a trustee to avoid liability for his own fraud, willful misconduct and gross negligence is in line with modern limitations on such exculpation clauses, can only be seen as far and is very welcome.

- 2.8 The ability of beneficiaries who are all of full age and capacity to remove and appoint trustees is a sensible addition.
- 2.9 The proposals for protecting movable property transferred to a trust governed by the law of Hong Kong from foreign rules of forced heirship is a provision much needed and which appears in many other jurisdictions.

There is also a proposal to enable a trust to contain reserved powers confined to investment and investment management to a Settlor of a trust. Whilst we welcome the introduction of reserved powers to a Settlor, we do not consider that these are sufficient and this is one of the two matters which we wish to address.

3. Additional matters:

In terms of additional solutions needed to make Hong Kong's proposed amended trust law more competitive. JCTLR intends to confine its suggestions to two and these are as follows:-

STATUTORY "ANTI-BARTLETT V. BARCLAYS" CLAUSE

- 3.1 It is doubtful whether the Amendment Bill's provisions reserving investment powers to Settlers and the consequent removal of liability of trustees in those circumstances addresses the wider issue of the management of underlying companies. Many intending Settlers wish that they, and indeed others, may be able to retain control of the day to day running of family companies without the interference of trustee shareholders. Some jurisdictions (VISTA in BVI, LST in Labuan and (proposed) SISTA in Samoa) are examples of special legislation in trust law permitting trustees to retain the shares of a company without diversification and to permit the directors to continue to run the company without interference from the trustees and without liability to the trustees in these respects. JCTLR suggested such legislation to the Government of Hong Kong, which felt, unjustifiably in the view of JCTLR, that such legislation could be misused and might render trusts "sham", which would not be so in law. Another major barrier to this approach was the need to align company law (by amendment) with these VISTA type provisions. This was, understandably in the JCTLR's view, a bridge too far given other long delayed amendments to our company law.
- 3.2 This is one of the areas where some practitioners in Singapore feel that their trust law is inadequate and that business is being lost to them. JCTLR believe that competitiveness means giving those who would use the trust law of Hong Kong the solutions which they really want, provided that these are wholly legal and sensible. One of the main cases where trustees were held liable for losses related to permitting directors of a company, the shares of which were assets of the trust, to run the company unsupervised by the trustees is ***Bartlett v Barclays Bank Trust Company Limited***. This case has given rise to "anti-Bartlett

clauses” in modern trust deeds which seek to limit trustee obligations in relation to the ownership and management of underlying companies and to consequently relieve trustees from liabilities to beneficiaries for losses arising from such companies in limited circumstances. It is widely accepted that such limitation clauses are generally effective and enforceable under the common law both in England and Hong Kong but there is uncertainty surrounding the extent of circumstances where they are effective and enforceable. The basic reason such clauses are effective is that the courts have ruled that the duties of a trustee in relation to an underlying company are not part of the “core, irreducible” duties a trustee owes to beneficiaries and thus a trustee may be relieved of them by express language in the trust instrument.

3.3 The essence of an anti-Bartlett clause is that a trustee is not liable if he does not enquire, monitor or supervise with regard to the actions of the directors of a company, the shares of which are assets of the trust. Such a clause has three limitations:-

3.3.1 it does not apply where the trustee is in fact involved in the running of the company;

3.3.2 it does not apply where the trustee has actual knowledge of the action complained of; and

3.3.3 it effects the extent of the trustee’s duty to the beneficiaries of the trust and not the duty of the director owed to the company – a matter of company law.

3.4 We therefore suggest that a statutory anti-Bartlett clause would provide a simple way to give certainty to a Settlor and his family that they can use the law of Hong Kong to create a trust for the shares of the family company and still run the company day to day without interference from the trustee, who will be protected as far as possible in this respect. This is not creating new law but rather confirming and clarifying in statute the common law which would add considerable certainty to, and thus the attractiveness of, our trust law.

3.5 We suggest that such a provision might be of the following nature:-

“A provision or provisions in a trust deed, where the trust is governed by the law of the Hong Kong Special Administrative Region of the People’s Republic of China (“HKSAR”) and where an asset of the trust is a share or shares in a company, whether incorporated in the HKSAR or not, shall be valid and enforceable to the extent that it provides for the following:-

- that the trustee may retain the share or shares without diversifying them;
- that the trustee shall have no duty to monitor, interfere in or become involved in the administration, management or conduct of the business and affairs of the company;

- that the trustee shall leave the administration, management and conduct of the business and affairs of the company to the directors and officers of the company and shall not be required to supervise such administration, management and conduct;
- that the trustee shall not be required to exercise any voting rights or rights of representation or intervention conferred on the trustee by the share or shares;
- that the trustee may assume, unless and until the trustee has actual knowledge to the contrary, that at all times the administration, management and conduct of the business and affairs of the company is being carried on by the directors or officers of the company competently, honestly and diligently and in the best interests of the shareholder or shareholders and that the directors and officers of the company are properly appointed and authorized;
- that the trustee shall not be required to take any steps to ascertain if the assumptions are correct;
- that the trustee shall not be required to remove or appoint any director or officer of the company; and
- that the trustee shall not be required to exercise any power to require the payment of any dividend whether of income or capital

and the trustee shall:

- be deemed not to have committed gross negligence by reason of compliance with this provision;
- not be required by any beneficiary of the trust to exercise any powers as shareholder of the company or to intervene in any way in the administration, management or conduct of the business and affairs of the company;
- not be liable for any acts or omissions of any director or officer of the company; and
- not be liable in any way for any loss to the company or to the capital or income of the trust fund of the trust by reason of compliance with the provision.”

3.6 Legislation, such as VISTA (the Virgin Islands Special Trusts Act), requires that there shall be a BVI licensed trustee of a trust governed by BVI law holding the shares of a BVI company. We suggest that for this provision the trust only needs to be governed by the law of the HKSAR. This makes this provision wider and more attractive to those who would seek its benefit.

NON-CHARITABLE PURPOSE TRUSTS ("NCPTs")

- 3.7 The other solution which JCTLR seek is the introduction of NCPTs. We explain the concept of NCPTs and why legislation is required for them to be valued below.
- 3.8 "The essence of a trust is that it is an obligation concerning property which is enforceable in the courts which will control the trustees and, in a rare case, even carry out the trust. There must be beneficiaries who can apply to the court to enforce their rights. As Millett L.J. states, "if the beneficiaries have no rights enforceable against the trustees there are no trusts. It follows that a trust may be created for the benefit of persons but not a purpose unless that purpose be charitable, for a purpose cannot sue, but if it be charitable the Attorney-General may sue to enforce it"¹.
- 3.9 Therefore NCPTs are invalid under our law in the absence of a specific statute which would recognize their validity. Such validity would be conditional on the purposes being legal, not against public policy and sufficiently certain and that persons are appointed to enforce the trusts in the courts ("Enforcer") thus curing the unenforceability problem alluded to above.
- 3.10 NCPTs possess two distinct features which make them ideal for use in various commercial situations. The first is that the commercial purpose of the trust is enshrined in the constitution of the NCPT itself and enforceable through the courts by the appointed Enforcer. The specific purpose is not subject to decisions made by those who would normally control an entity through shareholding (in the case of a company) or beneficiaries (in the case of a normal beneficiary trust). This "specific purpose" feature adds certainty to parties to commercial transactions.

The second is that unlike companies and beneficiary trusts NCPTs are not owned by shareholders or beneficiaries. Therefore, the problems associated with ownership interests in vehicles being amenable to their creditors or heirs means that NCPTs are both remote from the bankruptcy of individuals and the vagaries of succession on death of those with ownership rights. This is referred to as the "no owner" feature.

We will now set out examples of how these two features make NCPTs attractive in particular circumstances.

- 3.11 Examples of use of purpose trusts:
- 3.11.1 To own the shares of a family company that acts as trustee of a family trust. If individuals own those shares their creditors or heirs could come to control the trustee company and thus the trust which could frustrate the wishes of the

founder of the trust. A purpose trust – for the purpose of owning the shares of the family trust company – ensures no one individual can get control and that the trustee company is maintained for the benefit of all the beneficiaries of the trust for the long term – the no owner feature.

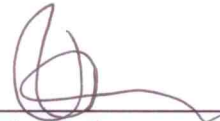
- 3.11.2 To own shares in vehicles which own and allocate employee benefit scheme shares. The purpose trust ensures that there is a neutral intermediate owner of shares in a company that will be allocated to employees according to scheme rules rather than owned by the employing company itself or a particular group of employees – both the specified purpose feature and the no owner feature.
 - 3.11.3 To own shares in a business controlled by a client who wished the shares to be sold after his death and the proceeds distributed in accordance with Sharia law – both features.
 - 3.11.4 For clients looking for a neutral party in a network of commercial transactions. For example, a purpose trust might stipulate that its specified purpose is to establish an underlying company and to enter into agreements relating to a specific transaction. Often there will be no assets left within the structure after the consummation of the transactions and discharge of the associated costs. Before that however the SPV is remote from the bankruptcy of parties who might otherwise be a shareholder of it thus compromising the security of the SPV – both features.
 - 3.11.5 To promote benevolent and quasi-charitable purposes that might fall outside the strict definition of “charitable purposes” for example, a trust to promote the maintenance of the graves of a particular family – the unenforceability problem is overcome.
- 3.12 As demonstrated above there are sound business reasons for the establishment of these types of trusts and Hong Kong’s lack of legislation in this area means that such business activities go to other jurisdictions. NCPTs are subject to the same anti-money laundering rules as are beneficiary trusts and companies and thus offer no advantage to would-be money launderers or others in pursuit of nefarious purposes.

3.13 Both the solutions which we have mentioned are ones which Singapore does not have and are both causes for the loss of business to Singapore. Hong Kong could benefit accordingly.

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- 1 From The Law of Trusts – Third Edition by Professor D.J. Hayton.
 - 2 At least nine respected trust administration centres have legislated to permit NCPTS.



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**List of recipients of Submission to LegCo Bills Committee
in respect of the Trust Law (Amendment) Bill 2013
26th March 2013**

1. Starry Lee Wai-king and Chan Kin-por, LegCo Members
2. Ng Leung-sing, Chairman, Bills Committee
3. Edwin Ing, Interim Chief Executive, Hong Kong Institute of Chartered Secretaries
4. Joyce Wong, The Law Society of Hong Kong
5. Susanna Chiu, Hong Kong Institute of Certified Public Accountants
6. Paul Shieh, Hong Kong Bar Association
7. Simon Ngan, Legal Committee, Hong Kong General Chamber of Commerce