

**DETAILED LEGISLATIVE
PROPOSALS
ON TRUST LAW REFORM**

CONSULTATION PAPER

Financial Services and the Treasury Bureau
www.fstb.gov.hk
March 2012

ABOUT THIS DOCUMENT

1. This paper is published by the Financial Services and the Treasury Bureau (“FSTB”) of the Government of Hong Kong Special Administrative Region to seek views and comments on the detailed legislative proposals on trust law reform.
2. After considering the views and comments received, we aim to introduce the relevant amendment bill into Legislative Council in 2012-13.
3. Please send your comments to us on or before **21 May 2012** by one of the following means:

By mail to: Division 6
Financial Services and the Treasury Bureau
15/F, Queensway Government Offices
66 Queensway
Hong Kong

By fax to: (852) 2869 4195

By email to: to_review@fstb.gov.hk

4. Any questions about this document may be addressed to Miss Joey LEE, Assistant Secretary for Financial Services and the Treasury (Financial Services), who can be reached at (852) 2867 5465 (phone), (852) 2869 4195 (fax) or joylee@fstb.gov.hk (email).
5. This consultation paper is also available on the FSTB’s website <http://www.fstb.gov.hk/fsb>.
6. Submissions will be received on the basis that we may freely reproduce and publish them, in whole or in part, in any form, and use, adapt or develop any proposal put forward without seeking permission or providing acknowledgment of the party making the proposal.
7. Please note that the names of respondents, their affiliations(s) and comments may be posted on FSTB’s website or referred to in other documents we publish. If you do not wish your name or affiliation to be disclosed, please state so when you make your submission. Any personal data submitted will only be used for purposes which are directly related to consultation purposes under this consultation paper. Such data

may be transferred to other Government departments/agencies for the same purposes. For access to or correction of personal data contained in your submission, please contact Miss Joey LEE (see paragraph 4 above for contact details).

CONTENT

| | <i>Page</i> |
|---|-------------|
| ABBREVIATIONS | 1 |
| EXECUTIVE SUMMARY | 2 |
| CHAPTER 1 INTRODUCTION | 4 |
| CHAPTER 2 AMENDMENTS TO THE TRUSTEE ORDINANCE | 11 |
| CHAPTER 3 AMENDMENTS TO THE PERPETUITIES AND ACCUMULATIONS ORDINANCE..... | 24 |

ABBREVIATIONS

| | |
|-----------|---|
| EPAO | Enduring Powers of Attorney Ordinance (Chapter 501) |
| PAO | Perpetuities and Accumulations Ordinance (Chapter 257) |
| STA | Singapore Trustee Act |
| TA 1925 | Trustee Act 1925 of the UK |
| TO | Trustee Ordinance (Chapter 29) |
| UK | United Kingdom |
| UKTA 2000 | UK Trustee Act 2000 |
| RAP | Rule Against Perpetuities |
| REA | Rule Against Excessive Accumulations of Income |

EXECUTIVE SUMMARY

1. The Government is reviewing the trust law regime in Hong Kong, mainly to amend and modernise the Trustee Ordinance (Cap. 29) (“TO”) to provide a better framework for the operation of trusts in Hong Kong. Reforming our trust law will bring our regulatory regime in line with other comparable common law jurisdictions such as the United Kingdom (“UK”) and Singapore. It will provide a more clearly defined framework that governs the respective rights and duties of parties to a trust, and better cater for the need of modern-day trusts. This will in turn strengthen the competitiveness of Hong Kong’s trust services industry and will further consolidate our status as an international asset management centre.
2. The Government conducted a public consultation on the review of the TO and related matters in 2009¹. The consultation conclusions were issued in February 2010². We also reported the consultation conclusions to the Legislative Council’s Panel on Financial Affairs in March 2010.
3. Based on the consultation conclusions, we have prepared the detailed legislative proposals on trust law reform for further consultation. The reform will cover clarification of trustees’ duties and powers, better protection of beneficiaries’ interests, and modernisation of trust law. The major proposals include:
 - (a) Clarification of trustees’ duties and powers
 - i. imposing a statutory duty of care on trustees;
 - ii. improving and clarifying the law relating to short-term delegation by a single trustee;
 - iii. providing trustees with a general power of appointing agents, nominees and custodians;
 - iv. giving trustees wider powers to insure any trust property against risks of loss by any event;
 - v. allowing professional trustees to receive remuneration for rendering services to charitable and non-charitable trusts;

¹ The consultation paper is available at http://www.fstb.gov.hk/fsb/ppr/consult/doc/to_review_consultation_e.pdf

² The consultation conclusions are available at http://www.fstb.gov.hk/fsb/ppr/consult/doc/to_review_conclusion_e.pdf

- (b) Better protection of beneficiaries' interests
 - i. regulating the exemption clauses of professional trustees who receive remuneration for their services;
 - ii. providing a mechanism for beneficiaries to remove a trustee on fulfilling certain conditions;
- (c) Modernisation of trust law
 - i. clarifying that a trust is not invalid by reason only of a limited reservation of the settlor's power;
 - ii. abolishing the rule against perpetuities with respect to new trusts; and
 - iii. abolishing the rule against excessive accumulations of income with respect to new non-charitable trusts.

4. During the review, we have also considered the following issues:

- (a) Beneficiaries' right to information – we have engaged an authority on trust law in Hong Kong to conduct a consultancy study. The study concludes that there are no imminent or compelling reasons to introduce legislation on beneficiaries' right to information in Hong Kong. We concur with the conclusion of the study. We will monitor the evolution of the common law and overseas practices in this area and keep under review the need and appropriateness to introduce any statutory requirement.
- (b) Provisions against forced heirship rules – we indicated our intention, in the 2010 consultation conclusions, to introduce provisions against forced heirship rules modeled on the Singapore approach. Subsequent research shows that the interaction of such provisions with overseas legislation and rules will require further examination. We are conducting further study on this subject and will consider incorporating such provisions in the light of the study findings.

5. This consultation paper invites views on the detailed legislative proposals on trust law reform. The Government will carefully study the comments received during the consultation before finalising the amendment bill. Subject to the outcome of the consultation, we plan to introduce the amendment bill into the Legislative Council in 2012-13 to take forward the reform.

CHAPTER 1

INTRODUCTION

Background

- 1.1 A trust is the relationship that arises wherever a person (called the trustee) holds property for the benefit of some other persons (who are termed beneficiaries) or for some objects permitted by law, in such a way that the real benefit of the property accrues, not to the trustee, but to the beneficiaries or objects of the trust.
- 1.2 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, the most important one being the TO.
- 1.3 Essentially, there are two categories of trust law provisions. The first category comprises “mandatory” rules, i.e. those statutory provisions that cannot be derogated from by the terms of the trust instrument. Examples are the rules against perpetuities and excessive accumulations of income. The second category is “non-mandatory” or “default” provisions which apply to a trust if there is no trust instrument or where the trust instrument is silent on a particular issue. For example, the TO provisions on trustees’ powers belong to the second category.
- 1.4 The TO was enacted in 1934 to supplement and amend the common law rules relating to trustees. It was substantially based on the UK Trustee Act 1925 (“TA 1925”). Since its enactment, it has not been substantially reviewed and amended.
- 1.5 In addition, the Perpetuities and Accumulations Ordinance (Cap. 257) (“PAO”) was enacted in 1970 to amend the common law rules regarding perpetuities and accumulations of income. The PAO was largely based on the UK’s Perpetuities and Accumulations Act 1964, and has not been substantially reviewed and amended since its enactment.

Reasons for the Review

- 1.6 Hong Kong is a major asset management centre in Asia. At the end of 2010, our total combined fund management business amounted to some HK\$10,091 billion, representing an increase of 18.6% over 2009. Funds sourced from overseas investors accounted for about 66% of the total fund management business (excluding real estate investment trusts). Asset management, which accounted for the largest share of the combined fund management business, amounted to HK\$6,841 billion, and recorded an impressive growth rate of 17.5% in 2010.³
- 1.7 Trusts have been playing a useful role in the asset management business. Apart from being used for family estate planning, trusts also serve as vehicles for various commercial transactions like unit trust investment arrangements and share ownership arrangements. In addition, trusts are commonly adopted for socially beneficial non-commercial activities in the form of charitable trusts.
- 1.8 Some major common law jurisdictions like the UK and Singapore have recently reviewed and reformed their trust laws to facilitate trust administration and attract more trust businesses. For instance, the UK reformed its trust law by introducing the Trustee Act 2000 and Singapore amended its Trustees Act in 2004. By comparison, since the TO has not been substantially reviewed and amended since 1934, some of the provisions, especially those regarding the powers and duties of trustees, are outdated and cannot meet the need of modern-day trusts.
- 1.9 The Hong Kong Trustees' Association and the Society of Trust and Estate Practitioners – Hong Kong Branch formed a Joint Committee on Trust Law Reform (“the Joint Committee”) and submitted proposals to the Government in 2007, advocating a comprehensive reform of the trust law in Hong Kong. The Joint Committee believes that a modern, predictable and equitable trust law will attract more trust business for Hong Kong.
- 1.10 The Government agrees that there is a need to review our trust law regime, particularly the TO. Modernising our trust law will bring our regulatory regime in line with other comparable common law

³ Fund Management Activities Survey 2010 conducted by the Securities and Futures Commission (“SFC”) and published in July 2011.

jurisdictions. It will provide a more clearly defined framework that governs the respective rights and duties of parties to a trust, and better cater for the need of modern-day trusts. This will in turn strengthen the competitiveness of Hong Kong's trust services industry and will further consolidate our status as an international asset management centre.

The Review

1.11 Through the review which began in early 2008, we aim to:

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

1.12 The Government launched a three-month public consultation on the review of the TO and related matters in June 2009.⁴ The consultation paper was circulated to the Joint Committee on Trust Law Reform, relevant professional bodies and practitioners, trust service providers, chambers of commerce, financial services regulators, major charitable organisations and academics. It was made available to the public on the FSTB website. A total of 36 submissions were received. The consultation conclusions, which summarised the views collected and stated the Government's positions on the individual issues, were issued in February 2010⁵. In short, all the respondents indicated general support for most of the proposals and many respondents considered the review timely and necessary. We reported the consultation conclusions to the Legislative Council's Panel on Financial Affairs in March 2010.

1.13 Based on the consultation conclusions, we have prepared the detailed legislative proposals on trust law reform for further consultation. The reform will cover clarification of trustees' duties and powers, better protection of beneficiaries' interests, and modernisation of trust law. The major proposals are highlighted below:

⁴ The consultation paper is available at http://www.fstb.gov.hk/fsb/ppr/consult/doc/to_review_consultation_e.pdf

⁵ The consultation conclusions are available at http://www.fstb.gov.hk/fsb/ppr/consult/doc/to_review_conclusion_e.pdf

- (a) Clarification of trustees' duties and powers
 - i. imposing a statutory duty of care on trustees;
 - ii. improving and clarifying the law relating to short-term delegation by a single trustee;
 - iii. providing trustees with a general power of appointing agents, nominees and custodians;
 - iv. giving trustees wider powers to insure any trust property against risks of loss by any event;
 - v. allowing professional trustees to receive remuneration for rendering services to charitable and non-charitable trusts;

- (b) Better protection of beneficiaries' interests
 - i. regulating the exemption clauses of professional trustees who receive remuneration for their services;
 - ii. providing a mechanism for beneficiaries to remove a trustee on fulfilling certain conditions;

- (c) Modernisation of trust law
 - i. clarifying that a trust is not invalid by reason only of a limited reservation of the settlor's power;
 - ii. abolishing the rule against perpetuities with respect to new trusts; and
 - iii. abolishing the rule against excessive accumulations of income with respect to new non-charitable trusts.

These proposals are discussed in detail in Chapters 2 and 3 and Annexes A to K to this document.

Other Related Issues

(a) Beneficiaries' right to information

- 1.14 There was a concern whether statutory provisions should be introduced to provide beneficiaries with a right to information. In view of the complexity of the issue, we have engaged a law professor of the University of Hong Kong⁶, who is an authority on trust law in Hong Kong, to conduct a dedicated consultancy study. A synopsis of the key findings is at Annex L.

⁶ Professor Lusina Ho, Harold Hsiao-Wo Lee Professor in Trust and Equity, the University of Hong Kong.

- 1.15 Under common law⁷, there are established rules governing beneficiaries' right to information. For example, a trustee must take reasonable steps to inform adult beneficiaries with interests vested in possession about the existence of the trust and general information relating to their beneficial entitlements. All beneficiaries have the right to apply to court to order the trustees to disclose all types of trust information, while disclosure in each particular case depends on the exercise of judicial discretion.
- 1.16 The study findings indicate that most onshore jurisdictions⁸ have not introduced legislation to replace or supplement common law rules, as there is a general consensus that the discretionary nature of the common law rules in this area is inevitable. Moreover, some offshore jurisdictions also rely on common law rules on disclosure (such as Bermuda, the Cayman Islands, the British Virgin Islands) whilst offshore jurisdictions⁹ that adopt statutory rules on disclosure tend to utilise them to restrict disclosure in order to incentivise settlors who usually favour secrecy. The study concludes that there are no imminent or compelling reasons to introduce legislation on beneficiaries' right to information in Hong Kong.
- 1.17 We concur with the conclusion of the study. Due to the divergent policies involved in disclosure and the versatile and evolving nature of trust, it is appropriate to treat each case individually rather than by hard-and-fast rules. Any attempt to provide statutory rules would only result in very general principles regarding the claims of disclosure. The lack of specific guidelines may also render such rules difficult to be enforced, hence defeating the purpose of making the rules.
- 1.18 We note that the common law in this area is evolving and far from settled. If we introduce statutory rules to replace common law rules, there is a risk that we may inadvertently deprive ourselves of the opportunity to take account of the development of new rules that suit the needs of modern-day trusts. On the other hand, if the statutory rules are in addition to common law rules, the trustees may face additional burden in tackling not just one set of rules, but two. This may create compliance problem for trustees because it is possible that an unwary trustee may be lulled into a false sense of security by

⁷ *Schmidt v Rosewood Trust Ltd* [2003] UKPC 26. Applied recently in Hong Kong in *Tam Mei Kam v HSBC International Trustee Ltd*, July 2, 2010 ([2011] HKCFA 34; affirming sub nom. *Re Estate of Mui Yim Fong* [2010] HKCA 197; [2010] 4 HKLRD 69.

⁸ These onshore jurisdictions include England, Scotland, Australia and Singapore.

⁹ These offshore jurisdictions include Jersey, Guernsey, Mauritius and Bahamas.

following the statutory rules and overlooking their common law counterparts.

1.19 In the light of the above, we are of the view that the issue of disclosure is better tackled on a case-by-case basis rather than by hard-and-fast rules. We will monitor the evolution of the common law and overseas practices in this area and keep under review the need and appropriateness to introduce any statutory requirement.

(b) Provisions against forced heirship rules

1.20 We have also considered the issue of whether there should be statutory provisions to the effect that forced heirship rules will not affect the validity of trusts or the transfer of property into trusts that are governed by the Hong Kong law (“provisions against forced heirship”). By way of background, forced heirship rights are the rights conferred by the laws of foreign jurisdictions (mainly civil law jurisdictions) on a testator’s heirs irrespective of the provisions of the testator’s will. Under forced heirship rules, the heirs will be entitled to claw back part of the trust assets or to recover money judgments for a similar amount.

1.21 We indicated our intention, in the 2010 consultation conclusions, to introduce provisions against forced heirship rules modeled on the Singapore approach. Subsequent research shows that there is a need to further examine the interaction of such provisions with overseas legislation and rules. We are conducting further study on this subject having regard to the experience of relevant overseas jurisdictions. We will consider incorporating such provisions in the amendment bill in the light of the study findings.

(c) Authorised investments

1.22 The Second Schedule to the TO sets out the “default” authorised investments in the absence of express provisions in a trust instrument. In response to some comments that the Schedule should be amended to allow more flexibility and choices for trustees to invest, we are reviewing the Schedule to see if there is scope to update the list of authorised investments. We will consult the relevant regulators, market practitioners and other stakeholders when conducting the review.

Seeking Comments

- 1.23 We would like to invite comments on our legislative proposals. The comments received will help us to ensure that the relevant proposals will meet the needs of modern-day trust administration and balance the interests of parties to a trust.
- 1.24 Subject to the outcome of the consultation, the Government plans to introduce an amendment bill into the Legislative Council in 2012-13 to take forward the reform.

CHAPTER 2

AMENDMENTS TO THE TRUSTEE ORDINANCE

2.1 The major proposals in relation to the TO are set out below. These proposals are based on the consultation conclusions issued in February 2010.

A. Statutory Duty of Care

Background

- 2.2 Case law has established that, in the investment of trust funds, appointment of agents and administration of trust property, trustees owe beneficiaries a duty of care and the standard of care expected is that of an ordinary prudent man of business acting in the management of his own affairs.¹⁰ In the selection of investments, the duty of trustees is to take such care as an ordinary prudent man would take if he were minded to make an investment for the benefit of other people for whom he felt morally bound to provide.¹¹ The English courts have further expressed the view that a higher standard should be owed by professional trustees or paid trustees. A professional trustee is expected to exercise the special care and skill that it professes to have.¹²
- 2.3 It is to be noted that the above duty of care under the general law can be excluded or modified by the trust instrument.
- 2.4 The TO also contains provisions pertaining to the standard of care expected of trustees in the appointment of agents.¹³
- 2.5 As set out in paragraphs 2.18, 2.19, 2.24 and 2.30 below, we recommend giving trustees wider default powers to facilitate effective trust administration. In parallel, we need to provide appropriate checks and balances so that trustees will exercise those powers properly. We therefore recommend introducing a trustee's statutory duty of care

¹⁰ *Speight v Gaunt* (1883-84) L.R. 9 App.Cas.1. at page 19.

¹¹ *Re Whiteley* (1886) L.R. 33 ChD 347, at page 355.

¹² *Bartlett v Barclays Bank Trust Co. Ltd.* [1980] 2 W.L.R. 430, at page 534.

¹³ Sections 25 of the TO.

along the lines of UK Trustee Act 2000 (“UKTA 2000”) and Singapore Trustee Act (“STA”).

Proposal

- 2.6 We will introduce provisions on the new statutory duty of care for trustees, i.e. a trustee must exercise such care and skill as is reasonable in the circumstances, having regard in particular to any special knowledge or experience that the trustee has or holds out as having, and if the trustee is acting in the course of a business or profession, to any special knowledge or experience that it is reasonable to expect of a person acting in the course of that kind of business or profession. The statutory duty of care will provide a clear and accessible statement of the standard of care to be expected of trustees.
- 2.7 The statutory duty of care will apply to trusts whether created before or after the commencement date of the amendment bill, but does not affect the legality or validity of anything done before the commencement date. It also does not apply where a trust instrument indicates that the statutory duty of care is not meant to apply.
- 2.8 We will provide that the statutory duty of care should apply to trustees when they are carrying out certain prescribed functions, including exercising the power of investment, appointing agents, nominees and custodians, taking out insurance, etc.
- 2.9 We will also amend sections 7, 11, 16 and 24 of the TO to make it clear that a trustee will not be responsible for loss under those sections if a trustee has discharged the statutory duty of care.
- 2.10 A draft of the major provisions seeking to codify the above proposals is at Annex A.

B. Power to Delegate

Background

- 2.11 Section 27 of the TO recognises that a trustee might be temporarily unable to exercise his powers and discretions. While the section empowers a trustee to delegate the exercise of his powers and discretions by a power of attorney, it also provides several safeguards,

including that the attorney must not be the trustee's sole co-trustee except for a trust corporation. The original purpose for making this restriction was probably to ensure that the number of trustees would not be reduced to one against the settlor's wish. However, the provision as it is may not be an effective safeguard because all the trustees may appoint the same attorney or all but one trustees delegate to the remaining trustee as the co-trustee. There are also concerns about the overlap and inconsistency between the Enduring Powers of Attorney Ordinance (Cap. 501) ("EPAO") and the TO regarding trustees' power of delegation.

Proposal

- 2.12 To better protect the interests of beneficiaries from excessive delegation under section 27 of TO, we recommend amending section 27(2) to provide that, if a trust has more than one trustee, the exercise of the power of delegation should not result in the trust having only one attorney or one trustee administering the trust, unless that trustee is a trust corporation.
- 2.13 Moreover, to avoid the overlap of section 27 of the TO with section 8(3)(a) of the EPAO in the area of delegation, we recommend repealing section 8(3)(a) of the EPAO so that the power of delegation by trustee is entirely governed by the TO and the inconsistency between the TO and EPAO will be removed. This would have the added benefit of making the TO more self-contained and provide beneficiaries with the additional safeguards under section 27 of the TO as outline above.
- 2.14 A draft of the major provisions seeking to codify the proposals in paragraphs 2.12 and 2.13 above is at Annex B.

C. Power to Employ Agents

Background

- 2.15 Under section 25 of the TO, trustees of a trust may collectively employ agents, such as solicitors, bankers and stockbrokers, to carry out administrative functions in relation to properties in Hong Kong (section 25(1)) and may employ agents to exercise all functions, including executing or exercising any discretion or trust or power, in relation to properties situated outside Hong Kong (by section 25(2)).

- 2.16 Trusteeship may require various professional skills that trustees may not possess. To enable trustees to effectively administer a trust, there is a need that trustees (other than trustees of a charitable trust) be given a general power to appoint agents to exercise any or all of their functions except for certain fundamental functions.
- 2.17 On the other hand, section 25 of the TO currently gives trustees the power to delegate a wide range of responsibilities to overseas agents for properties situated abroad. While it might be difficult for trustees to administer remote trust properties outside Hong Kong in the past and hence trustees need to employ agents to exercise broader functions related to such properties, advancement in communication technology has substantially reduced this difficulty. Retention of such a wide power by trustees is no longer justified. Therefore, we recommend repealing the trustees' power of delegation given under section 25(2) in relation to properties outside Hong Kong. The same set of rules will then apply for appointment of agents for both properties in and outside Hong Kong.

Proposal

- 2.18 Along the lines of the UKTA 2000 and STA, we will give trustees, other than those of a charitable trust, a general power to appoint agents to exercise any or all of their functions other than:
- (a) a function relating to distribution of trust assets;
 - (b) a power to decide whether a payment is to be made out of income or capital;
 - (c) a power to appoint a person to be a trustee; and
 - (d) a power to delegate their functions or to appoint nominees or custodians.
- 2.19 For trustees of charitable trusts, we recommend that agents should be allowed to carry out functions of generating income to finance a charitable trust's purposes, but not the execution of those purposes. This is in line with the UKTA 2000 and STA with one exception¹⁴.

¹⁴ Section 11(3)(d) of the UKTA 2000 provides that a charitable trust could appoint agents to carry out any other function prescribed by an order made by the Secretary of State. So far, we are not aware that any order to that effect has been made, nor are we aware of any function other than those set out in sections 11(3)(a) to (c) of the UKTA 2000 that a charitable trust could appoint agents to carry out. So we do not propose to introduce a provision similar to section 11(3)(d) of the UKTA 2000 in Hong Kong.

- 2.20 Section 25 of the TO will be repealed as it will be replaced by new provisions regarding the appointment of agents.
- 2.21 A draft of the major provisions seeking to codify the above proposals is at Annex C.

D. Trustee's Power to Employ Nominees and Custodians

Background

- 2.22 Under common law, trustees have a duty to take reasonable steps to secure and control trust assets unless the trust instrument otherwise provides. There are a number of limited exceptions to the common law rules provided for in the TO. The TO empowers trustees to deposit bearer securities with a banker or a banking company for safe custody and the collection of income.¹⁵ The TO also allows trustees to deposit trust documents with a banker or banking company or any company whose business includes the undertaking of safe custody of documents.¹⁶ There is no power to vest trust property in nominees.
- 2.23 To facilitate trustees to achieve effective trust administration, there is a case to provide trustees with a general power to employ nominees and custodians, and a power to vest trust properties in nominees following the approach in the UK and Singapore.

Proposal

- 2.24 We will give trustees a general power to employ nominees and custodians. Section 8 of the TO will be replaced by a new provision to make it clear that if trustees retain or invest in bearer securities payable to bearers, they must appoint a custodian for the securities, unless the trust instrument or any enactment permits the trustees to retain the securities without appointing a custodian, or the trustee is a sole trustee and is a trust corporation, or the trust has a custodian trustee.
- 2.25 A draft of the major provisions seeking to codify the above proposals is at Annex D.

¹⁵ See section 8(2) of TO.

¹⁶ See section 23 of TO.

E. Safeguards in relation to Appointment of Agents, Nominees and Custodians

Background

2.26 To protect the interests of the beneficiaries, the UKTA 2000 and STA provide certain safeguards to ensure that the power to employ agents, etc. would be subject to necessary checks and balances. The safeguards include:

- (a) applying the statutory duty of care to the exercise of the power to employ agents, nominees and custodians¹⁷;
- (b) requiring the trustees to provide an agent with a statement that gives guidance as to how the asset management function is to be exercised¹⁸;
- (c) restricting the choice of nominees and custodians to persons carrying on businesses that consist of or includes acting as nominees or custodians, or a body corporate controlled by the trustees¹⁹; and
- (d) imposing a duty on trustees to review the arrangements under which the agents, nominees and custodians act and how those arrangements are being put into effect.²⁰

Proposal

2.27 We consider these safeguards reasonable and necessary to ensure that the beneficiaries' interests would not be undermined as a result of the delegation of some of the trustees' duties to an agent, etc. We therefore recommend adopting these safeguards. Specifically, we will provide that the statutory duty of care should apply to appointment of agents, nominees and custodians (see paragraphs 2.8 above). Safeguards will also be provided to require the giving of a statement on the exercise of asset management functions (these functions relate to the investment of trust assets and the acquisition, disposal and management of trust property), restrict the choice of nominees and custodians, and impose a duty to review arrangements under which the agents, nominees and custodians act.

¹⁷ Paragraph 3 of Schedule 1 to the UKTA 2000.

¹⁸ Section 15 of the UK TA2000 and Section 41F of STA.

¹⁹ Section 19 of the UKTA 2000.

²⁰ Section 22 of the UKTA 2000.

2.28 A draft of the major provisions seeking to codify the above proposals is at Annex E.

F. Trustee's Power to Insure

Background

2.29 Trustees' power to insure trust property may be derived from the trust instrument or the TO. Section 21 of the TO provides trustees with a power to insure any building or other property against any loss or damage by fire and typhoon to any amount up to the full value of the building or property, and pay the premium for such insurance out of the income of the trust. The existing power is insufficient because it does not empower trustees to insure any loss or damage by events other than fire and typhoon, nor does it empower trustees to insure up to market value or full replacement value of the property. Moreover, as section 21 only empowers trustees to pay insurance premiums out of the income of trust properties, this will favour capital beneficiaries at the expense of the income beneficiaries, if they happen to be different people.

Proposal

2.30 We recommend empowering trustees with wider power to insure along the lines of the UKTA 2000 and STA. Trustees will be empowered to insure any trust property against risk of loss or damage by any event and pay the premiums out of the trust funds. The current restriction of insuring up to the full value of the property will be removed, so that the property can be insured up to its market value or full replacement value. A draft of the major provisions seeking to codify the above proposal is at Annex F.

G. Professional Trustees' Entitlement to Receive Remuneration

Background

2.31 Generally, trustees are not remunerated, because they have a duty not to profit from the trusts, and allowing trustees to receive remuneration may give rise to conflicts of their fiduciary duties and personal interests. The general rule is subject to the exceptions where the remuneration is

authorised expressly (a) by the trust instrument, (b) by the court under section 43 of the TO or by its inherent jurisdiction, or (c) by contracts between the trustees and beneficiaries.

- 2.32 To facilitate the employment of professional trustees to undertake the complex task of administering a modern-day trust, professional trustees (be it non-charitable trusts or charitable trusts) should have a right to receive remuneration for services rendered, even if they are services which are capable of being provided by lay trustees, subject to reasonable safeguards.

Proposal

Non-charitable trusts

- 2.33 We recommend adopting the UK approach²¹ by providing professional trustees with a right to receive remuneration. For non-charitable trusts, we will provide that:
- (a) if the trust instrument contains a provision entitling a trustee to receive remuneration, a trust corporation or a professional trustee is entitled to receive remuneration, even if such services provided are capable of being provided by lay trustees; and
 - (b) if the trust instrument is silent on remuneration, a trust corporation or a professional trustee (provided that he is not the sole trustee and each other trustee has agreed that he may be remunerated) is entitled to receive reasonable remuneration, even if such services are capable of being provided by lay trustees.

Charitable trusts

- 2.34 For charitable trusts, we recommend adopting the UK approach to the extent when a trust instrument contains a charging clause. Specifically, if the trust instrument contains a provision entitling a trustee to receive remuneration, a trust corporation or a professional trustee is also entitled to receive remuneration. This entitlement is subject to the condition that the professional trustee is not the sole trustee and he has the agreement of the majority of the other trustees that he could so charge.

²¹ UKTA 2000 Sections 28 and 29.

- 2.35 In the case where the trust instrument is silent on remuneration, the UKTA 2000 does not give professional trustees a statutory right to receive remuneration. This is also the current position in the TO. As suggested in our consultation conclusions issued in February 2010, we recommend not following the UK approach.
- 2.36 In the absence of a charging clause in the trust instrument, a professional trustee will be automatically barred from receiving any remuneration. As a charitable trust grows in size and possesses more substantial assets, there may be an increasing need for it to engage the services of a professional trustee to properly manage the trust assets. The existing limitation creates a disincentive for professional trustees to provide the services. We therefore proposed to provide some flexibility for charitable trusts, whose instrument is silent on charging, to provide reasonable remuneration to professional trustees.
- 2.37 Specifically, we recommend providing in the TO that a trust corporation or a professional trustee is also entitled to receive reasonable remuneration, even if services provided are capable of being provided by lay trustees. To guard against any possible abuse by trustees in seeking this remuneration, we will include in the legislation collective scrutiny of trustees' remuneration similar to that mentioned in paragraph 2.33(b) above, i.e. a professional trustee (other than a trust corporation) is entitled to remuneration only if he is not the sole trustee and all other trustees have unanimously agreed that he may be remunerated. In practice, the disinterested trustees will need to exercise their duty of care in their scrutiny. The trustees will be subject to their paramount duty at common law to act in the best interests of the present and future beneficiaries of the trust. In so doing, they would need to determine whether it is appropriate to allow any one of them to be remunerated. They would need to consider all the circumstances of the case, including whether a settlor has conferred any benefit on a trustee, whether a trustee is the most appropriate person to provide the service to the trust, and whether allowing to charge is to the advantage of the trust. In addition, such remuneration has to be "reasonable".
- 2.38 In this regard, we welcome views, particularly from charitable trusts, on whether the safeguards under our proposal outlined in paragraph 2.37 above would be sufficient to prevent any potential abuse.

2.39 A draft of the major provisions seeking to codify the above proposals is at Annex G.

H. Statutory Control on Trustee's Exemption Clause

Background

2.40 A trustee's exemption clause is a clause in a trust instrument which purports to exclude or restrict the trustee's liability for failure to carry out properly the duties imposed on the trustee by the trust instrument or by law. If a trustee fails to carry out his duties, it is a breach of trust and the beneficiaries have a right to recover their losses from the trustee. The increasing use of wide trustee exemption clause by professional trustees tends to leave settlors hiring them with little choice but to accept exemption clause which would reduce the protection to beneficiaries in the event of breach of trust. It has been established under case law that a trustee's exemption clause can validly exempt trustees from liability of all breaches of trust except fraud.²²

Proposal

2.41 To better protect beneficiaries, we recommend subjecting certain trustee exemption clauses to statutory control if the clauses seek to exempt remunerated professional trustees from liability. We will provide that the terms of a trust must not (i) relieve, release or exonerate a trustee from liability for breach of trust arising from the trustee's own fraud, wilful misconduct or reckless act (including reckless omission), or (ii) grant the trustee any indemnity against the trust property in respect of the liability. Such control applies to professional trustees who receive remuneration.

2.42 The formulation is based on the relevant statutory provisions of Jersey and Guernsey²³ except that we have replaced "gross negligence" (as used in the legislations in these two jurisdictions) by "reckless act". Both Jersey and Guernsey regulate trustees' exemption clause on the basis of gross negligence. In *Midland Bank Trustee (Jersey) Ltd v*

²² *Armitage v Nurse* [1997] 2 All ER 705.

²³ Section 30(10) of the Trusts (Jersey) Law 1984 provides that "Nothing in the terms of a trust shall relieve, release or exonerate a trustee from liability for breach of trust arising from the trustee's own fraud, wilful misconduct or gross negligence".

Section 39(7) of the Trusts (Guernsey) Law 2007 provides that "The terms of a trust may not (a) relieve a trustee of liability for a breach of trust arising from the his own fraud, wilful misconduct or gross negligence, or (b) grant him any indemnity against the trust property in respect of any such liability."

*Federated Pension Services Ltd*²⁴, it was decided that “gross negligence” did not require any mens rea or an intentional disregard of danger or recklessness and that it meant no more than “a serious or flagrant degree of negligence”. However, this is relevant to Jersey and Guernsey only and “gross negligence” is not a concept recognized by English law. According to the *UK Law Commission Consultation Paper No. 171, Trustee Exemption Clause*²⁵, the definition is imprecise and the courts would be afforded an element of latitude in determining when a trustee’s misconduct is sufficiently severe as to be termed “gross negligence”. We therefore have not included “gross negligence” in our provisions. We however welcome views on whether “gross negligence” should still be included despite the above-stated problem, and if so, whether there should be a new definition for it or we should simply leave it to the court to interpret on a case by case basis.

2.43 Nonetheless, we see scope to include “reckless act” (which includes reckless omission²⁶) which is something between “negligence” and “wilful misconduct”. We believe that the interpretation of “recklessness” is clearly set out in *Sin Kam Wah v HKSAR*²⁷, where “recklessness” is defined as “...he acted recklessly in respect of a circumstance if he was aware of a risk which did or would exist, or in respect of a result if he was aware of a risk that it would occur, and it was, in the circumstances known to him, unreasonable to take the risk.” In view of the said interpretation, we consider it appropriate not to allow a professional trustee to be exempted from liability arising from the trustee’s own “reckless act” if such trustee receives remuneration.

2.44 We note that in the UK leading case *Armitage v Nurse*²⁸, the court takes the view that the term “actual fraud” “connotes at the minimum an intention on the part of the trustee to pursue a particular course of action, either knowing that it is contrary to the interests of the beneficiaries or being recklessly indifferent whether it is contrary to their interests or not”²⁹. The court also states that a trustee who is guilty of “wilful misconduct” either consciously takes a risk that loss will result, or is recklessly indifferent whether it will or not.³⁰

²⁴ [1996] PLR 179

²⁵ The Law Commission Consultation Paper No. 171, Trustee Exemption Clause at 4.77.

²⁶ Under section 3 of the Interpretation and General Clauses Ordinance (Cap.1), “act, when used with reference to an offence or civil wrong, includes a series of acts, an illegal omission and a series of illegal omissions.

²⁷ (2005) 8 HKCFAR 192 page 210 D-G

²⁸ [1997] 2 All ER 705.

²⁹ *Ibid* at 711b

³⁰ *Ibid* at 712b

However, for the sake of clarity and avoidance of doubt, we propose to include “reckless act” in regulating trustee’s exemption clause.

- 2.45 The proposed statutory control of trustees’ exemption clauses will apply to trusts whether created before or after the commencement date of the Bill. To allow trustees of existing trusts to prepare for the implementation of the statutory control, a transitional arrangement will be provided for existing trusts in that the statutory control will only apply one year after the commencement date of the amendment bill.
- 2.46 A draft of the major provisions seeking to codify the above proposals is at Annex H.

I. Beneficiaries’ Right to Remove Trustees

Background

- 2.47 There is no express provision in the TO giving beneficiaries the right to remove trustees. However, beneficiaries may remove a trustee if they are authorised by the trust instrument, or by the court, or when all the beneficiaries (all of full age and legal capacity and are absolutely entitled to the trust property) act together to terminate a trust and re-settle the trust property³¹.

Proposal

- 2.48 We recommend providing beneficiaries with the right to remove or retire trustees by way of a simple, time-saving and court-free process following the UK approach³².
- 2.49 We will provide for a court-free process for the appointment and retirement of trustees on beneficiaries’ directions. The pre-conditions for exercising such power are that all the beneficiaries under a trust should be of full age and legal capacity, and are absolutely entitled to the trust property.
- 2.50 That said, the new power does not affect the inherent jurisdiction of the court or its power under section 42 of the TO to remove a trustee for the benefit of the beneficiaries.

³¹ *Saunders v Vautier* 1841 Cr. & Ph. 240

³² See sections 19 and 20 of the Trust of Land and Trustees Act 1996 of UK.

2.51 A draft of the major provisions seeking to codify the above proposals is at Annex I.

J. Validity of Certain Trusts

Background

2.52 It is generally acceptable under the law for a settlor to reserve to himself some powers to control over the trust property. For example, a settlor may wish to reserve to himself a power to remove and appoint a trustee so as to ensure that his wishes will be fully carried out. However, if the settlor reserves to himself excessive powers, the court may consider that there is insufficient certainty as to the settlor's intention to create the trust and may treat the arrangement as a sham. In Hong Kong, the question of whether a settlor's reserved powers will affect the validity of a trust instrument remains to be governed by case law.

Proposal

2.53 In the interest of clarity, we recommend modeling on the STA to introduce a statutory provision to the effect that a trust is not invalid by reason only of the settlor reserving to himself powers of investment or asset management functions³³. It essentially means that a trust would not be invalidated by virtue of the mere fact that the settlor has kept to himself certain investment powers. It does not encroach upon the jurisdiction of the court to examine the validity of a trust in situations where the settlor reserves to himself such powers.

2.54 We will also provide in the law that, where an investment power or asset management function has been reserved by the settlor, a trustee who has acted in accordance with the exercise of the power is exempted from liability.

2.55 A draft of the major provisions seeking to codify the above proposals is at Annex J.

³³ Section 90(5) of the STA.

CHAPTER 3

AMENDMENTS TO THE

PERPETUITIES AND ACCUMULATIONS ORDINANCE

3.1 The major proposals in relation to the PAO are set out below. These proposals are based on the consultation conclusions issued in February 2010.

Abolition of the Rule Against Perpetuities and the Rule Against Excessive Accumulations of Income

Background

3.2 The rule against perpetuities (“RAP”) puts a time limit within which trust properties must vest in the beneficiaries. Under the common law rule, a future estate or interest in any property must vest not later than 21 years after the determination of a life in being at the time of the creation of such estate or interest (“perpetuities period”), and if there is any possibility that the interest may vest outside that period, then the interest fails from the time of the purported creation of such estate or interest.

3.3 In 1970, the RAP under the common law was varied by the PAO, an Ordinance which was modeled on the UK Perpetuities and Accumulations Act 1964. Under the PAO, trusts created after 13 March 1970, i.e. the commencement date of the PAO, 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.³⁴ For the purposes of the “wait and see” rule, the PAO also prescribes persons who could be regarded as lives in being.³⁵ On the other hand, settlors may choose a fixed perpetuity period of not exceeding 80 years.³⁶ Since the PAO does not have any retrospective effect, trusts created before the commencement of the PAO remain to be governed solely by RAP as formulated by case law.

³⁴ Section 8(1) of the PAO.

³⁵ Section 8(4) and (5) of the PAO.

³⁶ Section 6(1) of the PAO.

- 3.4 The RAP is complicated and difficult to apply in practice. The principal defect is the reliance on the concept of lives in being as a means to determine the perpetuity period. The statutory “wait and see” rule creates uncertainty for trustees administering the trust property. Non-observance of RAP may render a disposition void, which is a result not expected by settlors. In Hong Kong, the importance of RAP in ensuring that land would not be tied up for a certain outdated purpose has been reduced because almost all private land is leasehold land held from the Government with a fixed lease term and there are several Ordinances that govern resumption and compulsory sale of land.
- 3.5 Separately, a trust instrument may direct that the income of the trust be accumulated for a certain period of time and be distributed at the end of that period. Under the common law, the accumulation period must be confined within the perpetuity period, i.e. rule against excessive accumulations of income (“REA”), to disallow settlors from preventing the enjoyment of income of the trust property by the beneficiaries.
- 3.6 The common law position was modified by the PAO, which provides that settlors may choose one of the six statutory accumulation periods³⁷ for which the income of a trust may be accumulated. The REA is said to be archaic and overly complicated, and would also frustrate the wishes of a settlor to accumulate income.

Proposal

- 3.7 We recommend abolishing the RAP and REA (except for charitable trust) in respect of trust instruments taking effect on or after commencement of the amendment bill.
- 3.8 We will provide that a trust may continue in existence for an unlimited period unless the terms of the instrument creating the trust provide for the contrary. The RAP and REA do not apply in relation to an instrument that takes effect on or after the commencement date of the

³⁷ Under sections 17-20 of the PAO, the six periods are –

- a) the life of a settlor;
- b) 21 years from the death of the settlor;
- c) duration of minority of any person in existence at the death of a settlor;
- d) the duration of a minority of a person who is entitled to an income;
- e) 21 years from the date of making the disposition; and
- f) duration of minority of any person at the time of making the disposition.

amendment bill. We will also repeal sections 4 to 20 of the PAO as a consequential amendment.

- 3.9 The abolition of REA will not apply to charitable trust. We will provide that for charitable trust, except for limited exceptions, a direction to accumulate will cease to have effect 21 years after the first day on which the income of a charity may be accumulated. This would prevent the undesirable effect of accumulating income for a long period of time without applying the income to charitable purposes. The proposed amendment applies to instruments taking effect on or after the commencement date of the amendment bill.
- 3.10 A draft of the major provisions seeking to codify the above proposals is at Annex K.

A draft of the major provisions on statutory duty of care

Statutory duty of care

- A new provision will be added after section 3 of the TO to provide for the statutory duty of care and we will provide in a Schedule (the Third Schedule) when the statutory duty of care will apply. A draft of the major provisions is as follows –

3A. Statutory duty of care

- (1) When the statutory duty of care applies to a trustee as provided in the Third Schedule, the trustee must exercise the care and skill that is reasonable in the circumstances, having regard in particular –
 - (a) to any special knowledge or experience that the trustee has or holds out as having; and
 - (b) if the trustee is acting in the course of a business or profession, to any special knowledge or experience that is reasonably expected of a person acting in the course of that kind of business or profession.
- (2) This section and the Third Schedule do not affect the legality or validity of anything done before the commencement date of the amending Ordinance¹.
- (3) The statutory duty of care does not apply to a trustee if, or in so far as, it appears from the instrument creating the trust that the duty is not meant to apply.

Third Schedule

Division 1 – Investment

1. The statutory duty of care applies to a trustee –
 - (a) when exercising the power of investment under section 4(1) or any other power of investment, however conferred;
 - (b) when exercising the power under sections 5, 6, 11(1), (2), (3), (4) and (5), 12 and 41I.

¹ “amending Ordinance” refers to the amendment bill introducing the trust law reform proposals.

- (c) when continuing to hold an investment that has ceased to be an investment authorized by the instrument creating the trust or the general law under section 7.
2. For the purpose of section 1(a) of this Schedule, when investing any trust funds in any investment specified in the Second Schedule, the trustee must discharge the statutory duty of care in addition to complying with that Schedule.

Division 2 – Agents, Nominees and custodians

3. The statutory duty of care applies to a trustee –
- (a) when entering into arrangements under which a person is authorized, under section 41B or any other power (however conferred), to exercise functions as an agent;
 - (b) when entering into arrangements under which a person is appointed, under section 41G or any other power (however conferred), to act as a nominee;
 - (c) when entering into arrangements under which a person is appointed, under section 41H or any other power (however conferred), to act as a custodian;
 - (d) when carrying out a trustee’s duty under sections 41M (review of agents) and 41N (review of nominees and custodians) to review the arrangements referred to in paragraphs (a), (b) or (c).
4. For the purpose of section 3 of this Schedule, entering into arrangements under which a person is authorized to exercise functions as an agent or is appointed to act as a nominee or custodian includes, in particular –
- (a) selecting the person who is to act;
 - (b) determining any terms on which the person is to act; and
 - (c) if the person is being authorized to exercise asset management functions, the preparation of a policy statement under section 41F.

Division 3 – Power to Do Other Things

5. The statutory duty of care applies to a trustee –
- (a) when exercising powers relating to trust properties conferred by section 16;
 - (b) when exercising any corresponding power, however conferred;

Division 4 – Insurance

6. The statutory duty of care applies to a trustee –
 - (a) when exercising the power under section 21 to insure property;
 - (b) when exercising any corresponding power, however conferred.

Division 5 – Reversionary interests, Valuation and Audit

7. The statutory duty of care applies to a trustee –
 - (a) when exercising the power under section 24(1) or (3);
 - (b) when exercising any corresponding power, however conferred.

A draft of the major provisions on power to delegate

Power to delegate trusts

- New provisions will be added to section 27 of the TO such that the exercise of a trustee’s power of delegation should not result in the trust having only one attorney or one trustee administering the trust. The opportunity is also taken to clarify that an instrument creating the power of attorney is valid for 12 months (or any shorter period specified in the instrument). A draft of the major provisions is as follows –

27(1A) A delegation under this section –

- (a) commences as provided by the instrument creating the power of attorney or, if the instrument makes no provision as to commencement of the delegation, on the date of the execution of the instrument by the donor of the power; and
- (b) continues for a period of 12 months or, if a shorter period is provided by the instrument creating the power of attorney, the shorter period.

27(2A) If a trust has more than one trustee, the exercise of the power of delegation must not result in the trust having only one attorney or one trustee administering the trust, unless the attorney or trustee is a trust corporation.

27(9) This section –

- (a) as in force immediately before the commencement date of the amending Ordinance¹ continues to apply to a power of attorney created before the commencement date, as if this section has not been amended; and
- (b) as amended by the amending Ordinance does not affect the legality or validity of any power of attorney created before the commencement date.

¹ “amending Ordinance” refers to the amendment bill introducing the trust law reform proposals.

- Corresponding amendments will be made to sections 27(1) and 27(2) of the TO and section 8(3)(a) of the EPAO (Cap. 501) as follows –
 - to repeal “for a period not exceeding 12 months” in section 27(1) of the TO;
 - to repeal “but not (unless a trust corporation) the only other co-trustee of the donor of the power” in section 27(2) of the TO;
 - to repeal section 8(3)(a) of the EPAO, so that the power of delegation by individual trustee is entirely governed by the TO. Suitable transitional provisions will be provided to cater for enduring power of attorney created before the commencement date of the amending Ordinance.

A draft of the major provisions on power to employ agents

Power to employ agents

- New provisions will be added after section 41 of the TO to provide for a power to appoint agents. A draft of the major provisions is as follows –

Part IVA (Appointment of Agents, Nominees and Custodians)

Division 1 – Agents

41A. Application of this Part

- (1) Except as otherwise provided in section 41I(6), this Part applies in relation to a trust having a sole trustee as it applies in relation to a trust that has more than one trustee, and references to trustees in this Part (except in section 41C(1) and section 41J(4)) include the sole trustee of a trust.
- (2) The powers conferred by this Part are exercisable by trustees jointly if there are more than one trustee.

41B. Power to employ agents

- (1) Subject to the provisions of this Part, the trustees of a trust may authorize a person to exercise any or all of their delegable functions as their agent.
- (2) For a trust that is not a charitable trust, the trustees' delegable functions are any function other than –
 - (a) a function relating to whether, or in what way, any assets of the trust are to be distributed;
 - (b) a power to decide whether any fees or other payment due to be made out of the trust funds¹ is to be made out of income or capital;
 - (c) a power to appoint a person to be a trustee of the trust; or
 - (d) a power conferred by the instrument creating the trust or any enactment that permits the trustees to delegate any of their functions or to appoint a person to act as a nominee or custodian.
- (3) For a charitable trust, the trustees' delegable functions are –
 - (a) a function relating to carrying out a decision that the trustees have taken;

¹ "trust funds" means any income or capital funds of a trust.

- (b) a function relating to the investment of assets subject to the trust (including, in the case of land held as an investment, managing the land and creating or disposing of an interest in the land); and
 - (c) a function relating to the raising of funds for the trust (otherwise than by means of profits of a trade which is an integral part of carrying out the trust's charitable purpose).
- (4) For the purposes of subsection (3)(c), a trade, whether carried on in Hong Kong or elsewhere, is an integral part of carrying out a trust's charitable purpose if the profits of the trade are applied solely to the purposes of the trust and either –
- (a) the trade is carried on in the course of the actual carrying out of a primary purpose of the trust; or
 - (b) the work in connection with the trade is mainly carried out by beneficiaries of the trust.
- (5) In this section, in relation to a trust, the reference to “function” includes powers and duties.

41C. Persons who may act as agents

- (1) Subject to subsection (2), a person whom the trustees may under section 41B authorize to exercise functions as the trustees' agent includes one or more of the trustees.
- (2) The trustees may not authorize 2 (or more) persons to exercise the same function unless the persons are to exercise the function jointly.
- (3) The trustees may not under section 41B authorize a beneficiary to exercise any function as their agent (even if the beneficiary is also a trustee).
- (4) The trustees may under section 41B authorize a person to exercise any function as their agent even though the person is also appointed to act as the trustees' nominee or custodian (whether under section 41G, 41H or 41I or any other power).

41D. Linked functions, etc.

- (1) Subject to subsection (2), a person who is authorized under section 41B to exercise a function as the trustees' agent is (whatever the terms of agency) subject to any specific duties or restrictions attached to the function.
- (2) A person who is authorized under section 41B to exercise a power which is subject to a requirement to obtain advice is not subject to the requirement, if the person is the kind of person from whom it would have been proper for the trustees, in compliance with the requirement, to obtain advice.

41E. Terms of agency

- (1) Subject to subsection (2) and section 41F(2) and Part IVB (Remuneration), the trustees may authorize a person to exercise functions as their agent on the terms as to remuneration and other matters as the trustees may determine.
 - (2) The trustees may not authorize a person to exercise functions as their agent on any of the terms mentioned in subsection (3) unless it is reasonably necessary for them to do so.
 - (3) The terms are –
 - (a) a term permitting the agent to appoint a substitute;
 - (b) a term restricting the liability of the agent or the substitute to the trustees or to any beneficiary; and
 - (c) a term permitting the agent to act in circumstances capable of giving rise to a conflict of interest.
- Section 25 of the TO will be repealed as it has been replaced by the new sections above regarding the power to appoint agents and a saving provision will be provided to cater for a person employed or appointed to act as an agent under section 25 of the TO before the commencement date of the amending Ordinance².

² “amending Ordinance” refers to the amendment bill introducing the trust law reform proposals.

**A draft of the major provisions on power to employ
nominees and custodians**

Power to appoint nominees and Custodians

- New provisions will be added after section 41 of the TO to give trustees a general power to employ nominees and custodians. There will also be a new section requiring trustees to appoint a custodian if they retain or invest in bearer securities unless otherwise provided by the trust instrument. A draft of the major provisions is as follows –

Part IVA (Appointment of Agents, Nominees and Custodians)

Division 2 – Nominees and Custodians

41G. Power to appoint nominees

- (1) Subject to the provisions of this Part, the trustees of a trust may –
 - (a) appoint a person to act as the trustees’ nominee in relation to any of the assets of the trust as they determine; and
 - (b) take the steps that are necessary to secure that those assets are vested in a person so appointed.
- (2) An appointment under this section must be made, or evidenced, in writing.
- (3) This section does not apply to any trust having a custodian trustee.

41H. Power to appoint custodians

- (1) Subject to the provisions of this Part, the trustees of a trust may appoint a person to act as a custodian in relation to any of the assets of the trust as they determine.
- (2) For the purposes of this Ordinance¹, a person is a custodian in relation to any assets if the person undertakes the safe custody of the assets or of any documents or records concerning the assets.
- (3) An appointment under this section must be made, or evidenced, in writing.
- (4) This section does not apply to any trust having a custodian trustee.

¹ “this Ordinance” refers to the Trustee Ordinance (Cap. 29).

41I. Investment in bearer securities

- (1) Trustees may, unless expressly prohibited by the instrument creating the trust, retain or invest in securities payable to bearers which, if not so payable, would have been authorized investments.
- (2) For the purpose of subsection (1), a direction that investments must be retained or made in the name of a trustee is not an express prohibition referred to in that subsection.
- (3) If trustees retain or invest in securities payable to bearer, the trustees must appoint a person to act as a custodian of the securities.
- (4) Subsection (3) does not apply if the instrument creating the trust or any enactment contains a provision that (however expressed) permits the trustees to retain or invest in securities payable to bearer without appointing a person as a custodian.
- (5) An appointment under this section must be made, or evidenced, in writing.
- (6) Subsections (3), (4) and (5) do not impose a duty on a sole trustee if that trustee is a trust corporation.
- (7) Subsections (3), (4) and (5) do not apply to any trust having a custodian trustee.

41K. Terms of appointment of nominees and custodians

- (1) Subject to subsection (2) and Part IVB (remuneration), the trustees may under section 41G, 41H or 41I appoint a person to act as a nominee or custodian on any terms as to remuneration and other matters that the trustees may determine.
 - (2) The trustees may not under section 41G, 41H or 41I appoint a person to act as a nominee or custodian on any of the terms mentioned in subsection (3) unless it is reasonably necessary for them to do so.
 - (3) The terms are –
 - (a) a term permitting the nominee or custodian to appoint a substitute;
 - (b) a term restricting the liability of the nominee or custodian or his, her or its substitute to the trustees or to any beneficiary; and
 - (c) a term permitting the nominee or custodian to act in circumstances capable of giving rise to a conflict of interest.
- Section 8 of the TO will be repealed as it has been replaced by the new section 41I above and a saving provision will be provided to cater for a banker or banking company holding any securities payable to bearer deposited with it under the repealed section 8 of the TO.

A draft of the major provisions on safeguards in relation to appointment of agents, nominees and custodians

Safeguards in relation to appointment of agents, nominees and custodians

- New provisions will be added after section 41 of the TO to introduce safeguards in relation to the appointment of agents, nominees and custodians. A draft of the major provisions is as follows –

Part IVA (Appointment of Agents, Nominees and Custodians)

Division 1 – Agents

41F. Special restrictions relating to asset management

- (1) The trustees may not authorize a person to exercise any of their asset management functions as their agent except by an agreement made, or evidenced, in writing.
- (2) The trustees may not authorize a person to exercise any of their asset management functions as their agent unless –
 - (a) the trustees have provided that person with a statement that gives guidance as to how the functions are to be exercised (a policy statement); and
 - (b) the agreement under which the agent is to act includes a term to the effect that the agent will secure compliance with –
 - (i) the policy statement; or
 - (ii) if the policy statement is revised or replaced under section 41M (review of agent), the revised or replaced policy statement.
- (3) The trustees must formulate any guidance given in the policy statement with a view to ensuring that the functions will be exercised in the best interest of the trust.
- (4) A policy statement must be made, or evidenced, in writing.
- (5) The asset management functions of trustees are their functions relating to –
 - (a) the investment of assets subject to the trust;
 - (b) the acquisition of property which is to be subject to the trust; and
 - (c) the management of property which is subject to the trust and the disposal of, or creation or disposal of an interest in, the property.

Division 2 – Nominees and Custodians

41J. Persons who may be appointed as nominees or custodians

- (1) A person may not be appointed under section 41G, 41H or 41I as a nominee or custodian unless one of the conditions mentioned in subsection (2) is satisfied.
- (2) The conditions are that –
 - (a) the person carries on a business that consists of, or includes, acting as a nominee or custodian; or
 - (b) the person is a body corporate that is controlled by the trustees.
- (3) For the purpose of subsection (2)(b), a body corporate is controlled by the trustees if the trustees have power to secure –
 - (a) by means of the holding of shares or the possession of voting power in, or in relation to, that body corporate or any other body corporate; or
 - (b) by virtue of any powers conferred by the articles of association or other document regulating that body corporate or any other body corporate,
that the affairs of the first-mentioned body corporate are conducted in accordance with the wishes of the trustees.
- (4) Subject to subsection (1), the person whom the trustees may appoint as a nominee or custodian include –
 - (a) one of the trustees, if that one is a trust corporation; or
 - (b) 2 or more of the trustees, if they are to act as joint nominees or joint custodians.
- (5) The trustees may under section 41G appoint a person to act as their nominee even though the person is also –
 - (a) authorized to exercise functions as the trustees' agent (whether under section 41B or any other power); or
 - (b) appointed to act as the trustees' custodian (whether under section 41H or 41I or any other power).
- (6) The trustees may under section 41H or 41I appoint a person to act as their custodian even though the person is also –
 - (a) authorized to exercise functions as the trustees' agent (whether under section 41B or any other power); or
 - (b) appointed to act as the trustees' nominee (whether under section 41G or any other power).

Division 3 – Review of and Liability for Agents, Nominees and Custodians

41L. Application of sections 41M, 41N and 41O

- (1) Sections 41M, 41N and 41O apply in a case where trustees have, under section 41B, 41G, 41H or 41I –
 - (a) authorized a person to exercise functions as their agent; or
 - (b) appointed a person to act as a nominee or custodian.
- (2) Subject to subsection (3), sections 41M, 41N and 41O also apply in a case where trustees have, under any power conferred on them by the instrument creating the trust or by any enactment –
 - (a) authorized a person to exercise functions as their agent; or
 - (b) appointed a person to act as a nominee or custodian.
- (3) If the application of section 41M, 41N or 41O in a case is inconsistent with the terms of the instrument creating the trust or any enactment, that section does not apply to that case.

41M. Review of agent

- (1) When an agent continues to act for a trust, the trustees of the trust –
 - (a) must keep under review the arrangements under which the agent acts and how those arrangements are being put into effect;
 - (b) if circumstances make it appropriate to do so, must consider whether there is a need to exercise any power of intervention that the trustees have; and
 - (c) if the trustees consider that there is a need to do so, must exercise the power of intervention.
- (2) If an agent has been authorized to exercise asset management functions, the duty to review under subsection (1) includes, in particular –
 - (a) a duty to consider whether there is a need to revise or replace the policy statement made for the purposes of section 41F;
 - (b) if the trustees consider that there is a need to revise or replace the policy statement, a duty to do so; and
 - (c) a duty to assess whether the policy statement (as it has effect for the time being) is being complied with.
- (3) Section 41F(3) and (4) applies to the revision or replacement of a policy statement under this section as it applies to the making of a policy statement under that section.
- (4) For the purposes of subsection (1), a “power of intervention” includes –

- (a) a power to give directions to the agent; and
- (b) a power to revoke the authorization or appointment of the agent.

41N. Review of nominees and custodians

- (1) When a nominee or custodian continues to act for a trust, the trustees of the trust –
 - (a) must keep under review the arrangements under which the nominee or custodian acts and how those arrangements are being put into effect;
 - (b) if circumstances make it appropriate to do so, must consider whether there is a need to exercise any power of intervention that the trustees have; and
 - (c) if the trustees consider that there is a need to do so, must exercise the power of intervention.
- (2) For the purposes of subsection (1), a “power of intervention” includes –
 - (a) a power to give directions to the nominee or custodian; and
 - (b) a power to revoke the appointment of the nominee or custodian.

41O. Liability of agents, nominees and custodians

- (1) A trustee is not liable for any act or default of the agent, nominee or custodian if the trustee has discharged the statutory duty of care applicable to the trustee under section 2 of the Third Schedule –
 - (a) when entering into the arrangements under which the person acts as the agent, nominee or custodian; or
 - (b) when carrying out the duties to review under section 41M or 41N.
- (2) If a trustee has agreed to a term under which the agent, nominee or custodian is permitted to appoint a substitute, the trustee is not liable for any act or default of the substitute if the trustee has discharged the statutory duty of care applicable to the trustee under section 2 of the Third Schedule –
 - (a) when agreeing to that term; or
 - (b) when carrying out the duties to review under section 41M or 41N as far as the duties relate to the use of the substitute.

41P. Effect of trustees exceeding their powers

A failure by the trustees to act within the limits of the powers conferred by this Part –

- (a) in authorizing a person to exercise a function of the trustees as an agent; or
 - (b) in appointing a person to act as a nominee or custodian,
- does not invalidate the authorization or appointment.

A draft of the major provision on power to insure

Power to insure

- Section 21 of the TO will be replaced by a new provision empowering the trustee to insure any trust property against risk of loss or damage. A draft of the major provision is as follows –

21. Power to insure

- (1) A trustee may –
 - (a) insure any property that is subject to the trust against loss or damage due to any event; and
 - (b) pay the premiums out of the trust funds¹.
- (2) If a property is held on a bare trust, the power to insure the property is subject to any direction given by the sole beneficiary or (if more than one beneficiary) each of the beneficiaries that –
 - (a) the property is not to be insured; or
 - (b) the property is not to be insured except on the conditions specified in the direction.
- (3) For the purpose of subsection (2), a property is held on a bare trust if it is held on trust for –
 - (a) a sole beneficiary who is of full age and capacity and is absolutely entitled to the property subject to the trust; or
 - (b) more than one beneficiary and each of the beneficiaries is of full age and capacity and who (taken together) are absolutely entitled to the property subject to the trust.
- (4) If a direction under subsection (2) is given, the power to insure, so far as it is subject to the direction, ceases to be a delegable function for the purpose of section 41B (power to employ agents).

¹ “trust funds” means any income or capital funds of a trust.

A draft of the major provisions on professional trustees' entitlement to receive remuneration

Professional trustees' entitlement to receive remuneration

- New provisions will be added after section 41 of the TO entitling professional trustees (both trustees of charitable and non-charitable trusts) to receive remuneration under different situations. New provisions will also be added on reimbursement of trustee's expenses and remuneration of agents, nominees and custodians. A draft of the major provisions is as follows –

Part IVB

Remuneration

41Q. Application of Part IVB

This Part applies in respect of –

- (a) services provided to, or on behalf of, a trust (whenever created); or
- (b) expenses incurred on behalf of a trust (whenever created),

on or after the commencement date of this Part.

41R. Interpretation of Part IVB

- (1) For the purposes of this Part, a trustee acts in a professional capacity if –
 - (a) the trustee acts in the course of a profession or business which consists of, or includes, the provision of services in connection with –
 - (i) the management or administration of trusts generally or a particular kind of trust; or
 - (ii) any particular aspect of the management or administration of trusts generally or a particular kind of trust, and
 - (b) the services that the trustee provides to, or on behalf of, the trusts falls within the description of paragraph (a).
- (2) For the purposes of this Part, a person acts as a lay trustee if the person –
 - (a) is not a trust corporation; and
 - (b) does not act in a professional capacity.

41S. Remuneration of professional trustees under instrument creating the trust

- (1) Subsections (3) and (4) apply to a trustee if –
 - (a) there is a provision in the instrument creating the trust entitling the trustee to receive payment out of trust funds in respect of services provided by the trustee to, or on behalf of, the trust; and
 - (b) the trustee –
 - (i) is a trust corporation;
 - (ii) is not a trust corporation, but is acting in a professional capacity as a trustee of a non-charitable trust; or
 - (iii) is not a trust corporation, but is acting in a professional capacity as a trustee, other than the sole trustee, of a charitable trust;
- (2) Despite subsection (1) –
 - (a) the application of subsections (3) and (4) to a trustee is subject to any inconsistent provision made in the instrument creating the trust; and
 - (b) Subject to any inconsistent provision made in the instrument creating the trust, in the case of a trustee referred to in subsection (1)(b)(iii), subsections (3) and (4) apply to the trustee only to the extent that a majority of the other trustees of the charitable trust have agreed as applicable to the trustee.
- (3) A trustee is to be treated as entitled under the instrument creating the trust to receive payment in respect of services provided even if the services are capable of being provided by a lay trustee.
- (4) Any payment to which a trustee is entitled in respect of services provided is to be treated as remuneration for services (but not as a disposition of property) for the purposes of section 10 of the Wills Ordinance (Cap. 30) (avoidance of gifts to attesting witnesses and their spouses).

41T. Remuneration of professional trustees other than under instrument creating the trust

- (1) This section applies to a trustee of a charitable or non-charitable trust if –
 - (a) the trustee's entitlement to remuneration –
 - (i) is not provided by the instrument creating the trust; or
 - (ii) is not expressly prohibited by any term in the instrument creating the trust; or
 - (iii) is not provided by any other enactment; and
 - (b) the trustee –
 - (i) is a trust corporation; or

- (ii) is not a trust corporation, but is acting in a professional capacity as trustee, other than the sole trustee, of a trust.
- (2) Despite subsection (1), in the case of a trustee referred to in subsection (1)(b)(ii), subsections (4) and (5) apply to the trustee only if each of the other trustees of the trust have agreed in writing that the trustee may be remunerated for services provided by the trustee to, or on behalf of, the trust.
- (3) This section applies to a trustee who has been authorized under a power conferred by Part IVA (appointment of agents, nominees and custodians) or the instrument creating the trust –
 - (a) to exercise functions as a trustee’s agent; or
 - (b) to act as a nominee or custodian,as it applies to any other trustee.
- (4) A trustee is entitled to receive reasonable remuneration out of the trust funds for any services that the trustee provides to, or on behalf of, the trust.
- (5) A trustee is to be treated as entitled under this section to receive remuneration in respect of the services provided even if the services are capable of being provided by a lay trustee.
- (6) For the purposes of this section –
 - reasonable remuneration***, in relation to the provision of services by a trustee of a trust –
 - (a) means the remuneration that is reasonable in the circumstances for the provision of those services by the trustee to, or on behalf of, the trust; and
 - (b) includes, in relation to the provision of services by a trustee who is an authorized institution under the Banking Ordinance (Cap. 155) and provides the services in that capacity, the institution’s reasonable charges for the provision of the services.

41U. Trustee’s expenses

- (1) This section applies to a trustee who has been authorized under a power conferred by Part IVA (appointment of agents, nominees and custodians) or the instrument creating the trust or any other enactment –
 - (a) to exercise functions as the trustee’s agent; or
 - (b) to act as a nominee or custodian,as it applies to any other trustee.
- (2) A trustee of a trust –
 - (a) is entitled to be reimbursed from the trust funds; or
 - (b) may pay out of the trust funds,

expenses properly incurred by the trustee when acting on behalf of the trust.

41V. Remuneration and expenses of agents, nominees and custodians

- (1) This section applies, if, under a power conferred by Part IVA (appointment of agents, nominees and custodians) or the instrument creating the trust or any other enactment, a person other than a trustee has been –
 - (a) authorized to exercise functions as the trustees' agent; or
 - (b) appointed to act as a nominee or custodian.
- (2) The trustees of the trust may remunerate the agent, nominee or custodian out of trust funds for services if –
 - (a) the agent, nominee or custodian is engaged on terms entitling the agent, nominee or custodian to be remunerated for those services; and
 - (b) the amount does not exceed the remuneration as is reasonable in the circumstances for the provision of those services by the agent, nominee or custodian to, or on behalf of, the trust.
- (3) The trustees may reimburse the agent, nominee or custodian out of trust funds for any expenses properly incurred by him, her or it in exercising the functions as the agent, nominee or custodian.

A draft of the major provision on statutory control on trustee's exemption clause

Trustee's exemption from liability

- A new provision will be added after section 41 of the TO to regulate trustee's exemption clause. A draft of the major provision is as follows –

Part IVC

Exemption from liability

41W. Professional trustee is not exempted from liability for breach of trust

- (1) This section applies to a trustee who –
 - (a) acts in a professional capacity; and
 - (b) receives remuneration for the trustee's services provided to, or on behalf of, the trust.
- (2) The terms of a trust must not –
 - (a) relieve, release or exonerate a trustee from liability for breach of trust arising from the trustee's own fraud, wilful misconduct or reckless act; or
 - (b) grant the trustee any indemnity against the trust property in respect of the liability.
- (3) A term of a trust is invalid to the extent that it purports to –
 - (a) relieve, release or exonerate a trustee from liability for breach of trust arising from the trustee's own fraud, wilful misconduct or reckless act; or
 - (b) grant the trustee any indemnity against the trust property in respect of the liability.
- (4) Subject to subsection (5), this section has effect in respect of a trust created on or after the commencement date of the amending Ordinance¹.
- (5) In respect of a trust created before the commencement date of the amending Ordinance, this section –
 - (a) has effect in respect of the trust one year after that date; and

¹ "amending Ordinance" refers to the amendment bill introducing the trust law reform proposals.

- (b) does not affect the legality or validity of anything done by a trustee of the trust before the expiry of the one year period.
- (6) To avoid doubt, this section applies to a trustee of a charitable trust who receives remuneration under section 41S or 41T.
- (7) In subsection (1), a *trustee who acts in a professional capacity* has the same meaning as in section 41R(1).

A draft of the major provisions on beneficiaries' right to remove trustees

Beneficiaries' right to remove trustees

- New provisions will be added after section 40 of the TO to provide for the appointment and retirement of trustees on beneficiaries' direction. A draft of the major provisions is as follows –

Division 2 – Appointment and Retirement of Trustees on Beneficiaries' directions

40A. Appointment and retirement of trustees

- (1) This section applies in relation to a trust if –
 - (a) no person is nominated for the purpose of appointing new trustees by the instrument, if any, creating the trust; and
 - (b) either –
 - (i) the sole beneficiary under the trust is of full age and capacity and is absolutely entitled to the property subject to the trust; or
 - (ii) all of the beneficiaries under the trust are of full age and capacity and (taken together) are absolutely entitled to the property subject to the trust.
- (2) The sole beneficiary or all of the beneficiaries (as the case may be) may give a written direction of either or both of the following descriptions –
 - (a) to a trustee directing the trustee to retire from the trust;
 - (b) to a sole trustee or all the trustees for the time being or, if there is none, to the personal representative of the last person who was a trustee, directing the sole trustee or trustees or the personal representative to appoint by writing a person specified in the direction as a trustee.
- (3) A trustee to whom a direction to retire has been given under subsection (2)(a) must make a deed declaring the trustee's retirement if –
 - (a) reasonable arrangements have been made for the protection of any rights of the trustee in connection with the trust;
 - (b) after the trustee has retired, there will be either a trust corporation or at least 2 persons to act as trustees to perform the trust; and
 - (c) either –

- (i) another person is to be appointed as a new trustee on the trustee's retirement (whether in compliance with a direction given under subsection (2)(b) or otherwise); or
 - (ii) the continuing trustees by deed consent to the retirement.
- (4) When a trustee makes a deed declaring the trustee's retirement under subsection (3), the retirement takes effect and the trustee is discharged from the trust.
- (5) When a trustee retires under subsection (3) as read with subsection (4), the trustee and the continuing trustees (together with any new trustee) must (subject to any arrangement for the protection of the rights of the retiring trustee) do anything necessary to vest the property subject to the trust in –
 - (a) the continuing trustees; or
 - (b) the continuing trustees and new trustees.
- (6) This section has effect subject to the restrictions imposed by sections 36 (limitation of the number of trustees) on the number of trustees.

40B. Appointment of substitute for incapacitated trustee

- (1) This section applies in relation to a trust if –
 - (a) a trustee, by reason of mental disorder as defined by section 2(1) of the Mental Health Ordinance (Cap. 136), is incapable of exercising the trustee's functions (*the incapacitated trustee*);
 - (b) no person is entitled and willing and able to appoint, under section 37(1), a new trustee in place of the incapacitated trustee; and
 - (c) either –
 - (i) the sole beneficiary under the trust is of full age and capacity and is absolutely entitled to the property subject to the trust; or
 - (ii) (if more than one beneficiary) all of the beneficiaries under the trust are of full age and capacity and (taken together) are absolutely entitled to the property subject to the trust.
- (2) The sole beneficiary or all of the beneficiaries (as the case may be) may give a written direction –
 - (a) to an attorney acting for the incapacitated trustee under an enduring power of attorney; or
 - (b) to a committee of the estate or other person acting for the incapacitated trustee appointed or authorized by the court under Part II of the Mental Health Ordinance (Cap. 136),
 to appoint a person specified in the direction to be a new trustee in place of the incapacitated trustee.

40C. Supplementary provision relating to directions

- (1) For the purposes of sections 40A and 40B, a direction is given by all of the beneficiaries if –
 - (a) a single direction is jointly given by all of them; or
 - (b) in compliance with subsection (2), a direction is given by each of them (whether solely or jointly with one or more, but not all, of the others),
and none of them by writing withdraws the direction given before it has been complied with.
- (2) If more than one direction is given, each beneficiary must specify for appointment or retirement the same person or persons.
- (3) Section 37(7) (providing for the powers, authorities and discretions of new trustees) applies to a trustee appointed under section 40A or 40B as if the trustee were appointed under section 37.
- (4) In sections 40A and 40B –
 - (a) *beneficiary*, in relation to a trust, means a person who under the trust has an interest in the property subject to the trust (including a person who has such an interest as a trustee or personal representative).

40D. Application of sections 40A and 40B

- (1) Sections 40A and 40B do not apply in relation to a trust created by a disposition in so far as the disposition provides that those sections do not apply in relation to the trust.
- (2) Sections 40A and 40B do not apply in relation to a trust created by a disposition before the commencement date of those sections in so far as provision to the effect that those sections do not apply is made by a deed executed –
 - (a) if the trust was created by a person who is of full age and capacity, by that person; or
 - (b) if the trust was created by more than one person, by the persons who created the trust as they are alive and are of full age and capacity.
- (3) A deed executed for the purpose of subsection (2) is irrevocable.
- (4) If a deed is executed for the purpose of subsection (2) –
 - (a) the deed does not affect anything done before its execution to comply with a direction given under section 40A or 40B; but
 - (b) a direction given under section 40A or 40B that has not been complied with before execution of the deed ceases to have effect.

A draft of the major provision on validity of certain trust

Validity of certain trusts

- A new provision will be added after section 41 of the TO to provide that a trust is not invalid by reason only of the settlor reserving to himself powers of investment or asset management functions. A draft of the major provision is as follows –

Part IVD Validity of Trusts

41X. Reserve power not affect validity

- (1) A trust is not invalid by reason only of the person creating the trust (the settlor) reserving to the settlor any or all powers of investment or asset management functions under the trust.
- (2) If a power referred to in subsection (1) has been reserved by the settlor, a trustee who acts in accordance with the exercise of the power is not acting in breach of trust.
- (3) This section does not affect the legality or validity of anything done before the commencement date of the amending Ordinance¹.

¹ “amending Ordinance” refers to the amendment bill introducing the trust law reform proposals.

**A draft of the major provisions on amendments to Perpetuities
and Accumulations Ordinance (Cap. 257) (PAO)**

Abolition of the rule against perpetuities and rule against excessive accumulations of income

- To accompany the abolition of the rule against perpetuities (RAP) and rule against excessive accumulations of income (REA), there will be new provisions replacing section 6 of the PAO to allow a trust to continue in existence for an unlimited period of time and section 4 to 20 of the PAO will be repealed. A new provision will also be added after section 20 of the PAO to provide the maximum accumulation period for charitable trusts. A draft of the major provisions is as follows –

3A. Rule as to duration not affected

This Ordinance does not affect the rule of law which limits the duration of non-charitable purpose trusts.

6. Duration of a disposition

- (1) Subject to section 3A, a trust may continue in existence for an unlimited period unless the terms of the instrument creating the trust provide to the contrary.
- (2) The rule against perpetuities (or remoteness of vesting) and the rule against excessive accumulations do not apply –
 - (a) in relation to an instrument that takes effect on or after the commencement date of the Amending Provisions¹; and
 - (b) (if an instrument is made in the exercise of a special power of appointment) in relation to that instrument only if the instrument creating the power takes effect after on or after that commencement date.
- (3) In relation to an instrument creating a trust that takes effect before the commencement date of the Amending Provisions, unless the terms of the instrument creating the trust provide to the contrary, any advancement, appointment, payment or application of assets from that trust to another trust is valid even if that other trust may continue after the date by which the first-mentioned trust must terminate.

¹ “Amending Provisions” means the part of the amendment bill which contains amendments to the Perpetuities and Accumulations Ordinance (Cap. 257).

- (4) For the purposes of subsection (2), an instrument which is a will takes effect at the testator's death.

21. Restriction on accumulation for charitable trusts

- (1) This section applies to an instrument to the extent that it provides for property to be held on trust for charitable purposes, other than such a provision made by a court.
- (2) This section applies –
- (a) whether the settlor is an individual or a corporation; and
 - (b) whether or not the duty or power to accumulate income extends to income produced by the investment of income previously accumulated.
- (3) If an instrument imposes or confers on the trustees a duty or power to accumulate income, and apart from this section the duty or power would last beyond the end of a period of 21 years calculated in accordance with subsection (4), then subject to subsection (5), the duty or power ceases to have effect at the end of that period.
- (4) The period referred to in subsection (3) begins on the first day when the income must or may be accumulated.
- (5) Subsection (3) does not have effect in relation to the instrument if it provides for the duty or power to accumulate income to cease to have effect –
- (a) on the death of the settlor; or
 - (b) on the death of one of the settlors, determined by name or by the order of their deaths.
- (6) If a duty or power to accumulate income ceases to have effect under subsection (3), the income to which the duty or power would have applied apart from this section, must –
- (a) go to the person who would have been entitled to it if there had been no duty or power to accumulate income; or
 - (b) be applied for the purposes for which it would have had to be applied if there had been no such duty or power to accumulate income.
- Suitable transitional provisions will be provided to cater for the application of repealed provisions of the PAO to existing instruments.

- Corresponding amendments will be made to section 3 of the PAO. Section 3(1) and (2) will be repealed and substituted by a new section 3(2). The draft provision is as follows –

3(2) This Ordinance applies –

- (a) in relation to an instrument that takes effect on or after the commencement date of the Amending Provisions; and
- (b) (for an instrument made in the exercise of a special power of appointment) in relation to that instrument only if the instrument creating the power takes effect on or after that commencement date.

**Beneficiaries' Right to Information:
Should Hong Kong Introduce Statutory Rules?**

Synopsis of the Key Findings of the Consultancy Report

1. Following the publication of consultation conclusions in February 2010, the Financial Services and Treasury Bureau engaged an authority on trust law in Hong Kong¹ to conduct research on the subject of whether Hong Kong should introduce statutory rules regarding beneficiaries' right to information under a trust arrangement. The present synopsis outlines the key findings of the study.
2. The study examines the current legal position in Hong Kong and the approaches taken by overseas jurisdictions on beneficiaries' right to information. It analyses the advantages and limitations of statutory rules, and whether Hong Kong should introduce statutory rules in this respect.
3. Current legal position in Hong Kong
This area is governed by common law, which may be broadly summarised as follows.
 - (a) Previous case law has established the types of documents which are *prima facie* disclosable, e.g. beneficiaries (with a more than theoretical possibility of obtaining benefit) can inspect trust deeds, deeds of appointment to beneficiaries, deeds of appointment of trustees, trust accounts and information about trust property, etc. Nonetheless, such disclosure will be denied if overriding circumstances apply (e.g. commercial confidentiality).
 - (b) Trustees owe a duty to take reasonable steps to notify, without demand, a limited class of beneficiaries (i.e. adult beneficiaries with interests vested in possession) about the existence of the trust and their beneficial entitlements; however, it is unclear how far this duty extends to minor, future, or contingent beneficiaries.
 - (c) *Schmidt v Rosewood Trust Ltd* (2003) laid down the general principle governing discretionary beneficiaries' right to information, namely that all such beneficiaries have the right

¹ Professor Lusina Ho, Harold Hsiao-Wo Lee Professor in Trust and Equity, the University of Hong Kong.

to apply to court to order trustees to disclose all types of trust information, but disclosure in each particular case depends on the exercise of judicial discretion. Such a discretionary approach is considered by the courts to be necessary to accommodate conflicting issues arising in the wide gamut of trust arrangements.

- (d) As a result of the decision in *Schmidt*, it becomes unclear how the *prima facie* categories mentioned in (a) above will be applied.

4. Overseas experiences

- (a) Most onshore jurisdictions have not introduced legislation to replace or supplement common law rules as there is a general consensus that the discretionary nature of the common law rules in this area is inevitable.
- (b) Offshore jurisdictions that adopt statutory rules on disclosure tend to utilise them to restrict disclosure. Many of the studied offshore jurisdictions only provide that a beneficiary may request information about trust accounts, but not trust information revealing trustees' deliberations about the exercise of their discretion. Many of these statutes are also silent on the beneficiaries' right to be notified of the existence of the trust and their beneficial entitlements, as well as disclosure of documents like trust deed.
- (c) Some onshore jurisdictions like Canada and New Zealand are currently considering the issue of disclosure. In the US, some states have adopted rules on disclosure with limited scope.

5. Advantages and limitations of statutory rules

- (a) Statutory rules offer the advantage of providing concise, concrete, and easily accessible statements of law as well as guidelines for the exercise of judicial discretion.
- (b) However, such rules have their limitations. Because of the divergent policies at issue and the versatile and evolving nature of the trust, issues of disclosure are better tackled on a case-by-case basis rather than by hard-and-fast rules. Statutory rules can only achieve marginal effect in mitigating uncertainty in this area of law. Indeed, if statutory rules are introduced in addition to common law rules, there could be conflict between the two sets of rules.

6. The case of Hong Kong

- (a) The introduction of legislation will provide useful guidance, albeit the beneficial effects of such legislation are likely to be marginal.
- (b) There are no imminent or compelling reasons to introduce legislation on beneficiaries' rights to information in Hong Kong.