



## A REVIEW OF THE TRUST REGIME IN HONG KONG SAR RECOMMENDATIONS AND PROPOSALS

### INTRODUCTION

1. The Law Society of Hong Kong has reviewed a number of issues regarding the law and regulation on trust arrangements and the conduct of trustee business in Hong Kong. We put forward the following proposals and recommendations, for consideration by the HKSAR Government and the relevant organizations.

### BACKGROUND

2. Hong Kong is home to a robust private wealth management (“**PWM**”) industry.
3. The PWM industry in Hong Kong (“**HK**”) is closely linked to the HK legal profession. In recent years the demand for sophisticated legal advices (both contentious and non-contentious) on personal and family wealth has been on the increase. This demand translated to a significant growth in the number of law firms (international, local and foreign law firms) and the number of legal practitioners specialising and offering advice in these areas.
4. Much of the private wealth are internationally tied up in trust structures established in different jurisdictions. On the other hand the private wealth of high-net-worth clients are often managed by family offices (“**FOs**”). The trustees in these FOs play a very active role in the PWM industry. According to the Securities and Futures Commission (“**SFC**”)’s 2019 Asset and Wealth Management Activities Survey, assets held by FOs and private trusts, charities and other corporates accounted for HK\$849 billion as at the end of 2019. This sector of the trust industry showed the biggest year-on-year increase (of 31%)<sup>1</sup>.

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<sup>1</sup> Securities and Futures Commission, “Asset and Wealth Management Activities Survey 2019”, August 2020, [https://www.sfc.hk/web/files/ER/Reports/AWMAS\\_2019\\_EN.pdf](https://www.sfc.hk/web/files/ER/Reports/AWMAS_2019_EN.pdf)

5. FOs are (largely) corporate vehicles; globally many single-family offices (“**SFOs**”) are owned by trust structures as part of the family's governance and succession structure. There are also other FOs which manage wealth held in trust structures.
6. Trusts<sup>2</sup> are an integral part of the PWM industry and consistently favoured by clients as viable arrangements for intergenerational wealth succession, asset protection, tax, or to achieve other specific objectives.
7. According to some industry reports, and views of stakeholders and practitioners who practise in this area, offshore trusts and/or offshore trustees are usually preferred over HK trusts<sup>3</sup> and/or HK trustees<sup>4</sup>. *Prima facie*, there is a trend for clients to “redomicile” their HK trust structures in other offshore jurisdictions, and the trend has been on the increase. This is so even for clients who are themselves based in HK or mainland China, or whose bankers or investment activities are based in HK or mainland China.
8. The above needs to be addressed by a comprehensive review on the law and regulation of trusts and the conduct of trustee business in HK. This review, in our views, are most relevant and important, as that would enhance the marketability of HK trusts and HK trustees over competing jurisdictions. This review is in line with the HKSAR government's policy of positioning and developing HK as a “PWM hub”<sup>5</sup>. HK legal practitioners who are practising and advising in these areas could assist in the review.
9. In the course of the review, the choice of jurisdiction (i.e. HK trusts vs offshore trusts) and the choice of the location / domicile of the trustees (i.e. HK trustees vs offshore trustees) need to be carefully but separately examined.
10. The choices of jurisdictions (see para 11 to para 39 below) and choice of locations / domicile (para 40 to para 55 below) merit different deliberations, as the two involve different legal and policy considerations.

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<sup>2</sup> In this submission, “**trusts**” means express trusts (whether discretionary or fixed interest), and does not include trusts implied by law, corporate trusts, pension trusts where the legal structure and regulatory environment are significantly different

<sup>3</sup> In this submission, “**HK trusts**” means trusts governed by HK law

<sup>4</sup> In this submission, “**HK trustees**” means professional trust companies which are established under and/or regulated by Hong Kong law

<sup>5</sup> See, for example, Hon Paul MP Chan, the Financial Secretary, “The 2020-21 Budget” (Speech by the Financial Secretary on 26 February 2020), para 61-62, 106; Financial Services Development Council (“**FSDC**”), *Family Wisdom: A Family Office Hub in Hong Kong* (Jul 2020), FSDC, *Hong Kong as the Regional Wealth Management Hub* (Feb 2020) FSDC, *Hong Kong: The Smart Choice for your Family Office* (Dec 2019)

## **Choice of Hong Kong Trusts (the issue of jurisdictions)**

11. On the choice of HK trusts, one needs to study an important statute which is the HK Trustee Ordinance<sup>6</sup>. The HK Trustee Ordinance governs, amongst others, the rights, powers and duties of trustees. It was introduced in HK in 1928. A major modernisation took place in 2013<sup>7</sup> to “better cater for the need of modern-day trusts”<sup>8</sup> and “strengthen the competitiveness of HK’s trust services industry and further consolidate [its] status as an international asset management centre”<sup>9</sup>. Despite the ambition embraced in the statute, there has not been a major uptake in the choice of HK trusts.
12. One reason for the lack of enthusiasm for HK trusts is that the law of trusts in HK, as it currently stands, is not as versatile or well-suited for the needs of increasingly sophisticated clients in the context of international estate and succession planning, when compared to other more popular offshore jurisdictions (for example, the British Virgin Islands (“**BVI**”), the Cayman Islands, and the Channel Islands).
13. For international estate and succession planning, two factors underscore clients’ choice – retention of control (to the extent permitted by the governing law) and asset protection. These two factors determine to a significant extent the choice of the governing law of trusts to be established for and be chosen by clients. We have considered these two factors, and come to a view that the law of trusts in HK may not be as attractive as those in other jurisdictions in a number of aspects. We have examined the laws of a number of offshore jurisdictions and set out below a summary for consideration:

### *(A) Reservation of Powers*

14. The HK Trustee Ordinance currently only provides for the reservation of investment and asset management functions of a trust to the settlor and that the reservation of such powers will not invalidate the trust<sup>10</sup>.
15. This is unattractive for international estate and succession planning, because it does not address issues such as (i) whether it is permissible to reserve other

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<sup>6</sup> Trustee Ordinance (Chapter 29 of the Laws of Hong Kong) (the “**HK Trustee Ordinance**”)

<sup>7</sup> The Trust Law (Amendment) Ordinance 2013 (No 13 of 2013)

<sup>8</sup> Financial Services and the Treasury Bureau, “Detailed Legislative Proposals on Trust Law Reform – Consultation Paper” (March 2013), p 2

<sup>9</sup> *ibid*

<sup>10</sup> HK Trustee Ordinance, s 41X

types of powers, (ii) whether powers can be reserved to a person other than the settlor (such as, for example, a protector), (iii) what happens to such reserved powers when the settlor dies or becomes incapacitated, and (iv) the extent of a trustee's duties and liabilities in complying with the exercise of such reserved powers (in particular, as is commonly the case, a settlor making speculative or blatantly inappropriate decisions in investment and asset management).

16. Upon considering the law of trusts of various offshore jurisdictions, we note, for example, the following:

- The Cayman Islands Trusts Law<sup>11</sup> sets out a list of powers that a settlor of Cayman Islands trust may reserve to himself<sup>12</sup>. The range of powers which can be reserved goes beyond the powers relating to the asset and investment management functions (as in the case of HK) and include, for instance, the powers to amend the trust instrument, to appoint the trust fund, to give binding directions to the trustee in connection with dealings with trust property, to restrict the exercise of any powers or discretions of the trustee etc. However, the Cayman Islands Trusts Law does not specify whether such powers may be reserved in favour of a person other than the settlor.
- The BVI Trustee Act<sup>13</sup> similarly sets out a list of powers that can be reserved - and the range of powers which can be reserved goes beyond the powers relating to the asset and investment management functions (as in the case of HK). In addition, the BVI Trustee Act also sets out that such powers can be reserved not only to the settlor, but also to other power-holders (such as a protector, nominator, or committee<sup>14</sup>) as well.
- The Guernsey Trust Law<sup>15</sup>, (i) expressly set out a list of powers which may be reserved by the settlor or other persons designated by the settlor without invalidating the trust<sup>16</sup>, and (ii) clearly provide that the trustee will not be in breach of trust for acting in compliance with the valid exercise of such reserved powers whether by the settlor or other persons designated by the settlor<sup>17</sup>. These two features which we consider are important for international estate and succession planning are nowhere to be found in the HK trust law.

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<sup>11</sup> Trusts Law (2018 Revision) (the “**Cayman Islands Trusts Law**”)

<sup>12</sup> *ibid* at s 14(1)

<sup>13</sup> Trustee Act (as amended, up to and including the amendments made by the Trustee (Amendment) Act 2015 (the “**BVI Trustee Act**”)

<sup>14</sup> *ibid* at s 86(2)

<sup>15</sup> Trusts (Guernsey) Law 2007 (the “**Guernsey Trust Law**”)

<sup>16</sup> *ibid* at s 15(1)

<sup>17</sup> *ibid* at s 15(3)

**17. Following from the above study, we recommend the HK Trustee Ordinance be amended to:**

- (i) expand the scope of the powers that may be reserved;**
- (ii) provide for validity of reserving powers in favour of other power-holders (such as a protector) or persons designated by the settlor; and**
- (iii) clarify the trustee’s duties and liabilities where the trustees act in accordance with the instruction of a power-holder who has reserved the relevant power.**

**(B) Protectors and Other Power-holder**

18. The existence of the office of a “protector” has become an increasingly common feature of HK trusts but the legal status of a protector (or other power-holders with similar functions under a different name, such as an appointor, guardian, power-holder etc) under HK law is unclear”. There are no statutory provisions providing for the role of a “protector”<sup>18</sup> and there is no legal definition for the term “protector”. There is also a dearth of case-law or authorities from the HK courts on the subject matter. This cause uncertainty on what role, powers and liabilities such offices could have in a trust.

19. The roles of a protector are important, as he is the *“person occupying an office created by a trust instrument distinct from that of trustee, whether or not referred to as protector, upon which has been conferred power(s) or right(s) enabling the office-holder to participate in the administration of the trust or the disposition of trust assets”*<sup>19</sup>

20. The office of the protector may be held by family members of the settlor or independent advisors (or a committee of protectors comprising a mix of one or more of them).

21. Generally speaking, the role of the protector is to monitor the trustee of a trust in the discharge of its duties in the administration and management of the trust, as well as the investment and distribution of assets held by the trust fund of the trust.

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<sup>18</sup> Although we note that some legislations (such as the Inland Revenue Ordinance (Chapter 112 of the Laws of Hong Kong) and the Anti-Money Laundering and Counter-Terrorist Financing Ordinance (Chapter 615 of the Laws of Hong Kong)) refer to “protectors of trusts”, but who is or is not a protector of trust is not defined and the role, powers and liabilities of such offices are also not provided for

<sup>19</sup> Holden A, *Holden on Trust Protectors* (1st, Jordan Publishing, 2011) para 1.6

It would be difficult to set out an exhaustive list of powers that a protector may have because the exact scope of the powers of a protector would depend on the terms of the trust deed. The following sets out some of the more common powers usually conferred on a protector:

- the power to appoint new, additional or successor trustees;
- the power to remove existing trustees;
- the power to appoint new, additional or successor protectors,
- the power to remove existing protectors;
- the power to veto the exercise of powers by the trustees or the right to receive notice from the trustees for the exercise of powers;
- the power to approve the trustees' remuneration;
- the power to direct investments of the trust fund; and
- the power to appoint, pay or apply the income or capital of the trust fund.

22. After we have considered the law of trusts in various offshore jurisdictions, we note, for example, that the BVI Trustee Act gives statutory recognition to the role of a protector by expressly setting out that the trust deed establishing a BVI trust may contain provisions by virtue of which the exercise by the trustees of any of their powers and discretions shall be subject to the previous consent of the settlor or some other person, whether named as protector, nominator, committee or any other name, and if so provided in the trust deed the trustees shall not be liable for any loss caused by their actions if the previous consent was given<sup>20</sup>. In addition, the Act also states that a protector exercising his or her powers conferred under the trust deed in accordance with the BVI Trustee Act shall not by virtue of the exercise of such powers, be deemed to be a trustee and will not be liable to the beneficiaries for the bona fide exercise of these powers.

23. As mentioned above, the Guernsey Trust Law also recognises that the powers specified therein may be validly reserved not only by the settlor, but in favour of other persons designated by the settlor (such as a protector)<sup>21</sup>.

24. **It is obvious, and we recommend, that the HK Trustee Ordinance should be amended to provide for the role, powers and liabilities of the office of a protector (or other power-holders by a similar name).**

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<sup>20</sup> BVI Trustee Act s 86(1)

<sup>21</sup> Guernsey Trust Law, s 15(1)

(C) Firewall Provisions

25. The “firewall provision” in the HK Trustee Ordinance is currently limited to anti-forced heirship claims in relation to moveable property. It does not extend to other types of claims or foreign judgments in general<sup>22</sup>. As such, HK trust law protects the transfer of assets to a HK trust against claims by a forced heir, but does not protect against community of property claims by a divorcing spouse. The existence and effectiveness of firewall provisions in a particular jurisdiction is an important consideration for those clients having asset protection as one of their objectives in setting up a trust.
26. Upon considering the law of trusts in various offshore jurisdictions, we note, for example, that the Cayman Islands Trusts Law contains provisions dealing with the conflict of laws issues which can arise where claims are brought against a Cayman Islands trust by third parties, particularly forced heirs and creditors. It sets out that, subject to a number of exceptions<sup>23</sup>, all questions relating to a Cayman Islands trust are to be determined by reference to Cayman Islands laws only<sup>24</sup>. These include, but are not limited to, questions going to the capacity of the settlor, validity and administration of the trust, the existence and extent of powers conferred under the trust deed, etc. It also sets out that a Cayman Islands trust or a disposition of property to such trust shall not be invalidated or rendered void or defective because (a) the laws of a foreign jurisdiction prohibit or does not recognise the concept of a trust<sup>25</sup>, or (b) such trust or disposition avoids or defects the rights or interests of any person related to the settlor or any beneficiary under foreign law or contravenes foreign law or court orders<sup>26</sup>.
27. The Guernsey Trust Law also contains similar firewall provisions setting out that Guernsey law determines questions relating to a Guernsey trust and that a Guernsey trust (and a disposition of property to such trust) will not be affected by any foreign law on the basis that the foreign law does not recognise the notion of a trust or forced heirship claims.
28. Generally speaking, firewall provisions in the Cayman Islands and Guernsey considered in the above offer protection to assets held under trusts established in those jurisdictions against foreign judgments and divorce orders, making it more difficult for creditors or parties to a divorce to “pierce through” a trust with a view

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<sup>22</sup> HK Trustee Ordinance s 41Y(2) and 41Y(3)

<sup>23</sup> Cayman Islands Trusts Law s 90(i) to 90(vi)

<sup>24</sup> *ibid* at s 90

<sup>25</sup> *ibid* at s 91(a)

<sup>26</sup> *ibid* at s 91(b)

to claiming the trust assets in satisfaction of debts or obligations owed to them. It is obvious that a set of comprehensive and robust firewall provisions are much desirable for HK trust law from an international estate and succession planning perspective.

29. **We recommend that comprehensive firewall provisions should be introduced to the HK Trustee Ordinance, providing (a) protection of trust assets from claims arising from the claimant’s personal relationship with the settlor/ beneficiaries of the trust, and potentially (b) non-recognition of foreign judgments. That said, we also recommend that at a policy level a careful balance needs to be struck between offering protection to personal and family wealth and the need to protect the interests of creditors in formulating any such firewall provisions for HK<sup>27</sup>.**

(D) Non-charitable Purpose Trusts

30. Under HK trust law, a trust cannot be created for non-charitable purposes (unless it falls under a limited category of case-law exceptions) because the “beneficiary principle” requires that there must be someone who can enforce the trust. In the context of estate and succession planning, purpose trusts<sup>28</sup> are often used for a variety of reasons, such as to hold shares in a private trust company or to further some “quasi-charitable purposes”.

31. We have looked into the law of trusts in various offshore jurisdictions and we note, for example, the following:

- In the BVI, common law restrictions in relation to purpose trusts are abrogated under the BVI Trustee Act<sup>29</sup>. The BVI Trustee Act sets out a number of conditions which must be satisfied in order to establish a valid BVI purpose trust. These include, but are not limited to, the condition that the stated purpose of the trust must “be specific, reasonable and possible”<sup>30</sup> and must not be “immoral, contrary to public policy or otherwise unlawful”<sup>31</sup>, there must be an enforcer of the trust, who must be a designated person<sup>32</sup>. The role of the enforcer is to enforce the purpose

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<sup>27</sup> And on this point, we do not propose for any changes to the Bankruptcy Ordinance or to the creditor protection rules under the Conveyancing and Property Ordinance for fraudulent transfer.

<sup>28</sup> In this submission, “**purpose trust**” means, broadly speaking, trusts which are established not for beneficiaries but for non-charitable purposes

<sup>29</sup> BVI Trustee Act s 84

<sup>30</sup> *ibid* at s 84A(3)(a)

<sup>31</sup> *ibid* at s 84A(3)(b)

<sup>32</sup> *ibid* at s 84A(3)(d) and (e)

trust<sup>33</sup> and the BVI Trustee Act also provides for the appointment and removal of the enforcer and certain powers and rights which an enforcer of a BVI purpose trust has<sup>34</sup>.

- The Guernsey Trust Law includes provisions for the recognition of the validity of purpose trusts. It makes it clear that trust may be validly established either for the benefit of beneficiaries (i.e. the traditional notion of trusts under common law) or for any purpose (i.e. including both charitable and purpose trusts)<sup>35</sup>. As a result, trusts holding property or exercising functions without conferring a benefit on any person are valid under Guernsey law. The Guernsey Trust Law also clarifies what is or what is not a non-charitable purpose, making it clear in the definition of “purpose” that it covers any purpose, whether or not involving the conferral of any benefit on any person, and includes, without limitation, the holding or ownership of property and the exercise of functions. Guernsey law permits a trust to have both a purpose and beneficiaries. Similar to the position in the BVI, a Guernsey purpose trust must have an enforcer<sup>36</sup>, and the Guernsey Trust Law also makes it clear that the enforcer has a fiduciary duty to enforce the trust in relation to its non-charitable purposes<sup>37</sup> to ensure that the trustees are accountable for their actions and should therefore be sufficiently independent from the trustees to be able to do this.

**32. We recommend that legislative provisions should be introduced to the HK Trustee Ordinance to recognise the validity of purpose trust established under HK trust law.**

*(E) Statutory Trusts*

33. The use of traditional types of trust for succession and estate planning may under certain circumstances cause concerns or difficulties to clients, especially to those who are not familiar with the concept of a “trust” or the idea of alienating his assets to a trustee (which is usually a professional corporate trustee). For example, in relation to trusts holding shares of operating entities, clients may not be comfortable with the idea of transferring their shareholding in such companies to a trust structure and wish to retain certain degree of control over the affairs of the company. The “prudent man of business rule” has also made the trust an unattractive vehicle to hold assets because it imposes an obligation on the trustee

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<sup>33</sup> *ibid* at s 84A(17)

<sup>34</sup> *ibid* at s 84A(9), (10), (11) and (15)

<sup>35</sup> Guernsey Trust Law, s 2

<sup>36</sup> *ibid* at s 12(1)

<sup>37</sup> *ibid* at s 12(2)

to monitor the conduct of the directors of such company and to intervene in the affairs and business of the company on some occasions. This poses significant difficulties for trustees and may not sit well with clients who want to retain control over the affairs of such companies.

34. These concerns are sometimes addressed through the choice of a purpose trust structure (in the manner discussed above), but some offshore jurisdictions (e.g. the BVI and the Cayman Islands) have introduced novel arrangements such as the VISTA trusts and STAR trusts to deal with these issues. The purpose of these novel arrangements are to essentially erase the problems traditionally associated with the “prudent man of business rule”. The following sets out a summary of the statutory provisions relating to VISTA trusts and STAR trusts:

- In the BVI, the BVI VISTA Act<sup>38</sup> introduces a novel type of statutory trust commonly known as “VISTA trusts”. Generally speaking, a VISTA trust in the BVI is a form of statutory trust specifically for trusts which are set up for holding shares in BVI companies. Under a VISTA trust, a trustee may retain shares in a BVI company irrespective of financial advantages of disposal or the value of the shares<sup>39</sup> and they are generally prohibited from intervening in the management of such companies<sup>40</sup> except in limited circumstances<sup>41</sup>. The trustees of a VISTA trust also have certain powers to appoint and remove directors of the BVI companies held under the VISTA trust in accordance with the terms of the instrument establishing such trust<sup>42</sup>. A VISTA trust arrangement therefore allows a shareholder to establish a trust of his BVI company that disengages the trustee from management responsibility and permits the BVI company and its business to be retained as long as the directors think fit. This is achieved in general terms by:
  - authorising the entire or partial removal of the trustee's monitoring and intervention obligations<sup>43</sup>;
  - permitting the settlor to confer on the trustee a role more suited to a trustee's abilities, namely a duty to intervene to resolve specific problems<sup>44</sup> (eg a deadlocked board);

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<sup>38</sup> Virgin Islands Special Trusts Act 2003 (the “BVI VISTA Act”)

<sup>39</sup> *ibid* at s 5

<sup>40</sup> *ibid* at s 6

<sup>41</sup> *ibid* at s 8

<sup>42</sup> *ibid* at s 7

<sup>43</sup> *ibid* at s 6

<sup>44</sup> *ibid* at s 8

- allowing the trust instrument to lay down rules for the appointment and removal of directors<sup>45</sup> (so reducing the trustee's ability to intervene in management by appointing directors of its own choice);
  - giving both beneficiaries and directors the right to apply to the court if the trustee fails to comply with the requirements for non-intervention or the requirements for director appointment and removal<sup>46</sup>; and
  - giving to the trustee, if required, the power to sell the shares with the consent of the directors<sup>47</sup>.
- In the Cayman Islands, the Cayman Islands Trusts Law introduces a novel type of statutory trust commonly known as “STAR trusts”. Generally speaking, a STAR trust is set up for the purpose of holding a specific asset regardless of the investment performance of that asset. It requires the settlor to expressly invoke the legislation within the trust instrument which avoids disputes as to how that particular trust should be interpreted. Unlike traditional types of trusts, a STAR trust:
    - has no maximum perpetuity period (it can go on forever);
    - can be created for non-charitable purposes (for example, to run a family business);
    - is enforced by an “enforcer”, rather than by the beneficiaries; and
    - trustees of a STAR trust (one of whom must be a Cayman Islands trust corporation) are only obliged to provide the beneficiaries with limited information.

**35. We recommend that legislative provisions should be considered for the introduction of a statutory trust regime similar to a VISTA trust or STAR trust arrangement to HK. The introduction of such arrangements would, as it has been observed, increase HK’s ability to compete with other offshore jurisdictions and would also cater well for clients who are relatively new to the concept of trusts and who would generally prefer to have greater control over their assets<sup>48</sup>.**

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<sup>45</sup> *ibid* at s 7(1)

<sup>46</sup> *ibid* at s 10

<sup>47</sup> *ibid* at s 9

<sup>48</sup> “Hong Kong Trust Industry Spotlight: Enhancing its competitive Edge” (October 2017)

(F) Right to Trust Information and Documents

36. In HK, the right to information under a trust arrangement is currently governed by case law as it was rejected as a proposal on trust law reform back in 2013. The leading authority in this area is the case of *Schmidt v Rosewood Trust Ltd*<sup>49</sup>, which established that the right to the disclosure of trust information is one aspect of the court's inherent jurisdiction to supervise, and if necessary to intervene in, the administration of trusts. No beneficiary had any entitlement as of right to disclosure of a "trust document", and especially when there were issues as to personal or commercial confidentiality, the court might have to balance the competing interests of beneficiaries, the trustees themselves, and third parties, with the result that disclosure might have to be limited and safeguards might have to be put in place.
37. As the matter now stands, there are uncertainty on (i) what is or is not trust information and documents, (ii) who has a right to disclosure (e.g. whether a settlor or a protector is entitled to the disclosure of trust information and documents), and (iii) the extent of such obligation for disclosure (if it exists). This is not ideal from a trustee's perspective. On one hand, the unlawful disclosure of any trust information or documents puts the trustee in breach of trust, but on the other hand, the non-disclosure of such information and documents where it is in fact required to do so might put the trustee under the threat of legal proceedings for the compulsory disclosure of such information and documents.
38. We note that some offshore jurisdictions have introduced legislations to clarify this area. By way of illustration,
- The Bahamas Trustee Act<sup>50</sup> imposes a statutory obligation of a trustee of a Bahamas trust to take reasonable steps to inform each beneficiary who has, but may not be aware of having, a vested interest under the trusts of the existence of the trusts and of the general nature of that interest, and if there are no beneficiaries entitled to a vested interest (as in the case of a discretionary trust), then the trustee is to take reasonable steps to ensure that there is at least one person who is capable of enforcing the trust (e.g. one of the discretionary beneficiaries) to be made aware of such matters<sup>51</sup>. This removes a trustee's obligation to inform beneficiaries of their rights if they have no vested interests but are only interested as contingent beneficiaries or under discretionary trusts. The Bahamas Trustee Act also provides for how disclosure is to be made under a number of specific

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<sup>49</sup> [2003] 3 All ER 76

<sup>50</sup> Trustee Act 1998 (the "Bahamas Trustee Act")

<sup>51</sup> *ibid* at s 83(1)

circumstances (e.g. if the beneficiary in question is a minor or a mentally incapacitated person<sup>52</sup>), and the type of documents and documents that may be disclosed<sup>53</sup>.

- In New Zealand (“NZ”), the NZ Trusts Act<sup>54</sup> provides extensively for the trustee's duties and liabilities in the context of disclosure of trust information and documents. It distinguishes between “basic trust information” and “trust information”. For “basic trust information”, there is a general presumption that they must be disclosed to beneficiaries<sup>55</sup>. The basic trust information includes the fact that a person is a beneficiary of the trust, the name and contact details of the trustee, the details of appointment and removal of trustees, and the right to copies of the trust deed and other trust information<sup>56</sup>. On the other hand, for “trust information”, there is a presumption for disclosure within a reasonable period of time upon receiving a request from a beneficiary<sup>57</sup> but the trustee at the same time has discretion on whether or not such disclosure should be made after considering a list of factors set out in the NZ Trusts Act<sup>58</sup>. The list of factors which the trustee is required to consider includes, for instance, the nature of interests held by the beneficiary requesting for disclosure, whether such information is confidential, the purpose of such disclosure, etc<sup>59</sup>. If the trustee ultimately decides to withhold all or any of the basic trust information from beneficiaries or refuse a request for disclosure of trust information, then the NZ Trusts Act provides that it must apply to the NZ courts for directions<sup>60</sup>.

**39. We recommend that the HK Trustee Ordinance should be amended to provide for duty of a trustee in relation to the disclosure of information and documents of the trust. The amendments as proposed enhance clarity and provides certainty.**

### **Choice of Hong Kong Trustee (the issue of location / domicile)**

40. On the choice of HK trustees, we observe that the reservations on using HK trustees tend to be caused by:

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<sup>52</sup> *ibid* at s 83(2), see also s 83(3) to 83(5)

<sup>53</sup> *ibid* at s 83(5) and 83(7)

<sup>54</sup> Trusts Act 2019 (the “NZ Trusts Act”)

<sup>55</sup> *ibid* at s 51

<sup>56</sup> *ibid* at s 51(3)

<sup>57</sup> *ibid* at s 52(1)

<sup>58</sup> *ibid* at s 52(2)

<sup>59</sup> *ibid* at s 53

<sup>60</sup> *ibid* at s 54

- (i) Tax consideration – if the legal owner of the assets are in HK, would the structure be taxable in HK? The answer is often not clear, and would depend on the nature of the trusts (does it trade actively or passively holds its investments for long term?), the nature and location of the assets (are they assets that give rise to HK sourced profits). Prima facie, the only certainty one could have is that if the trustee is not in HK but in, say, the Cayman Islands, there would definitely not be a HK tax issue for the trust.
- (ii) Regulatory Consideration – it is perceived that HK does not have a comprehensive regulatory regime for trustees, especially for professional trustees. The current regulatory framework is fragmented and lacks industry specific regulations.
- (iii) Legal Consideration – regardless of the governing law of the trust, if the trustee is in HK, the legal owner of the assets (the trustee) would be subject to the laws and regulations of HK and the jurisdiction of the HK courts. This is particularly relevant when dealing with third parties, investigatory powers of regulators, applicable Anti-Money Laundering regimes, exchange of tax information regimes and jurisdictions of legal proceedings.
- (iv) Other Consideration – when people are moving assets and family members are relocating out of HK for whatever reasons, they would not want their trust or their trustee left behind and remain in HK.

41. **We suggest that the HKSAR Government to consider:**

- **promoting the use of HK trusts managed by HK trustees as part of the ecosystems of promoting FOs in HK**
- **clarifying the taxation treatment of trust structures and trust parties**
- **promoting investments**
- **carefully Review the Regulatory Regime for Professional Trustees.**

The above are elaborated in the paragraphs below.

(A) *Promoting the use of HK trusts managed by HK trustees as part of the ecosystems of promoting FOs in HK*

42. From the perspective of economic growth and job creation, we would rather see the wealth and the trusts managed by HK trustees rather than offshore trustees which seem to be the preferred locations presently.

43. From a regulatory perspective, the SFC should find much comfort if a fund managed by the FO, or the shareholder of the FO, or the investor of a limited partnership (“**LP**”) / an open-ended fund company (“**OFC**”) is a trust managed by a HK trustee that is registered under Part VIII of the Trustee Ordinance (Cap. 29 of the Laws of HK) rather than a structure or trustee that is outside of the jurisdiction of HK.

(B) Clarifying the taxation treatment of trust structures and trust parties

44. On regulation and tax, there is a need to study comparable jurisdictions (e.g. Singapore) to consider how clarity on the regulation and the taxation of trusts and trustees could be improved.

45. Departmental Interpretation and Practice Notices or similar guidance could be issued by the Inland Revenue Department (“**IRD**”) to clarify what a HK trustee should attend upon and handle the trust’s income or profits where prima facie the trust is not “carrying on business” but is “investing family wealth” which may or may not be actively managed.

46. The HKSAR Government can also consider tax exemption of income earned by a trust. The reality is that such exemption would not cause a decrease in revenue for HK but serve to attract clients setting up trusts in HK. To the extent that HK does not levy profits tax where the taxpayer is not carrying on business, or earning passive income, or offshore income, HK trusts would not bear any tax bill. However it takes time and money to draw up financial accounts, file tax returns, satisfy the IRD that there is no profits liability to tax, etc. The compliance burden, along with the IRD’s standard answer of “each case depends on its facts and circumstances”, lead people to choose structures and trustees that are not in HK.

47. Special tax regimes already apply to REITs, Collective Investment Schemes, MPF Trusts, trusts that fit within the unified funds regime. Measures are being introduced to exempt carried interests for PE industry. What remains to be taxed under general principles of the Inland Revenue Ordinance should only be private trust arrangements with a HK trustee.

(C) Promoting Investments

48. Practice guidelines should be issued and be put in place to confirm that trusts that are professionally managed in HK may invest in FOs, the Hong Kong-Shenzhen wealth connect investment opportunities, LLP and OFC without creating extra compliance burden or tax leakage for the users of our wealth management

industry. Where appropriate, the HKSAR Government should consider incentives to encourage wealth owners to use HK managed trusts as the preferred investment vehicle.

49. One could consider to relax the requirement for LP or OFC to appoint a licensed fund manager where the fund is purely holding family/ private wealth and there is a licensed trust and corporate services providers (TCSP) appointed to administer the trust/ fund.

(D) Carefully Review the Regulatory Regime for Professional Trustees

50. Currently the regulatory landscape for trustees is fragmented, especially for professional trustees offering trusts and fiduciary services in the ordinary course of business in HK. This leads to inconsistent approaches and confusing policy objectives laid in the regulation of professional trustees and that increases operating costs for professional trustees which then have to navigate through and comply with the various requirements across different applicable legislations and regulatory framework.
51. HK introduced the registration regime for the regulation of trust and corporate services providers (“**TCSPs**”) in 2018 – this is a wide-reaching legislation for the regulation trustees in HK because it applies to all TCSPs conducting trust business in HK. The introduction of the TCSP system is helpful in promoting HK’s rating to become “substantially effective” by the Financial Action Task Force peer review. Nevertheless, the legislation itself is largely a registration regime to deal with Anti-Money Laundering risks in the conduct of trust business in HK; it does not however regulate the other aspects in the operation of a trust business in HK.
52. Another key legal framework for the conduct of trust business in HK is found under Part 8 of the HK Trustee Ordinance. That provides for the registration as a trust company for trust companies conducting the following businesses:
  - to act as an executor, administrator, trustee, receiver, receiver and manager, assignee, liquidator, guardian of the property of infants, committee of the estates of lunatics, or other like office of a fiduciary nature;
  - to act as attorney or agent for the collection, receipt and payment of money and for winding up estates and for the sale or purchase of any movable or immovable property;

- to act as agent for the management and control of movable and immovable property for and on behalf of the owners thereof or for or on behalf of executors, administrators or trustees;
  - to act as investing and financial agent for and on behalf of executors, administrators, and trustees or any other persons and to receive money in trust for investment and to allow interest thereon until invested, and to undertake for and on behalf of executors, administrators and trustees or any other persons the negotiation of loans of all descriptions and the procuring and lending of money on the security of any description of property immovable or movable or without taking any security on such terms as may be arranged, and to advance and lend moneys to protect any estate, trust or property entrusted to the company as aforesaid and to charge interest upon any such advances.
53. The TCSP registration system, or the registration as a trust company under the HK Trustee Ordinance, have no fit and proper consideration as to the standards of professionalism of the trustees, or any consumer / investor protection elements. There are legal requirements for segregation of assets, requirements to be accountable to beneficiaries, etc. but no regulatory oversight, and no audit/ accountability.
54. In addition to the above, the Mandatory Provident Fund Schemes Authority also regulates MPF trustees. That is another regulatory regime for trustees.
55. The Hong Kong Monetary Authority in 2020 launched a public consultation to introduce a practice code for trust businesses but it would only be enforceable for trustees owned by financial institutions. Trust businesses owned by insurance companies are subject to Insurance Authority's oversight, whilst lawyers and accountants acting as trustees are subject to their professional conduct rules. Trustees who deal with private trusts and non-SFC regulated products are subject to the Companies Registry's TCSP regime under the Anti-Money Laundering and Counter-Terrorist Financing Ordinance. The conducts or professional standards of trustee companies under different ownership models but potentially all operating in the PWM industry in HK are not subjected to the same yardstick of a unified regulator or uniform regulatory framework. This fragmented regulatory framework potentially reduces consumer confidence when they are to select a trustee company.

## **Concluding Comments**

56. We have reviewed the legal and regulatory landscape in HK and propose three broad areas of recommendations and proposals for the HKSAR Government to consider:

- (i) **To amend the HK Trustee Ordinance to make HK trusts to be more competitive, attractive and versatile.**
- (ii) **To improve the regulatory framework for professional trustee companies in HK which are dealing with private wealth. The regulatory framework at the moment is fragmented.** This raises the market confidence in choosing HK trust companies.
- (iii) **To review the tax treatment of trusts, trustees, trust investment vehicles and trust distributions in HK,** with a view to providing greater clarity and to removing ambiguity in the relevant sections of the Inland Revenue Ordinance. Further, tax incentives (by way of tax exemptions) should be offered to attract wealth owners and FOs to structure their investment holdings through the use of HK trusts managed by HK based trustees.

57. Whilst HK has the potential to attract, and manage, a lot of investments and FOs, it needs to recognise that the wealth owning structures for Ultra High Net Worth and High Net Worth families are often tied up in family trusts. Unfortunately, the trend continues to be for these family trusts to set up their family trusts under offshore laws rather than HK laws, and often using overseas trustee companies rather than HK trustee companies. This means that it is offshore companies who are engaged to provide legal advice on the trust structures, to navigate the overseas regulatory requirements, and potentially to resolve conflicts and disputes under foreign laws or in courts of offshore jurisdictions.

58. There is huge potential to capitalise on HK as a globally leading Wealth Management hub. In the context of PWM, the use of trusts continue to be an essential tool to effect succession planning and intergenerational wealth transfer.

**The Law Society of Hong Kong  
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