

**A BETTER UNDERSTANDING OF DUAL OWNERSHIP OF TRUST PROPERTY AND
ITS INTRODUCTION IN CHINA THROUGH COMPARATIVE STUDIES**

by

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ABSTRACT

A main characteristic of the common law trust is the concept of dual ownership. This concept establishes a distinction between a trustee's legal ownership of the assets of the trust and a beneficiary's equitable title to those same assets. In civilian systems, however, because ownership is considered absolute and indivisible, no similar division of legal and equitable title is possible. This difference in the conception of ownership between the civilian and common law systems raises great challenges in fitting the concept of trusts, into civilian systems such as China's.

This thesis attempts to provide readers with a better understanding of the system of dual ownership of trust property. Through comparative studies, it discusses the best way that the trust can be incorporated in China. It argues that the concept of dual ownership is not an obstacle to the introduction of the trust in civilian jurisdictions. Using an analysis that focuses on comparing function, rather than form, the thesis argues that the key to understanding the interpretations of dual ownership in China is through an explanation that can be called the 'binary system of real rights and personal claims'. On this approach, the common law's legal ownership corresponds to a civilian trustee's unitary ownership in real rights, and the common law's equitable ownership corresponds to a special kind of personal claim.

RÉSUMÉ

L'une des caractéristiques principales de la fiducie en Common Law est le concept de double propriété, à savoir la propriété juridique du fiduciaire et la propriété effective du bénéficiaire. Cela dit, puisque la propriété est considérée comme absolue et indivisible dans les systèmes de droit civil, la notion de fiducie, venant de la Common Law, demeure problématique d'un point de vue civiliste. En particulier, la différence entre la conception de la notion de propriété en droit civil et en Common Law demeure comme un énorme défi, surtout pour ceux qui cherchent d'adapter le concept de fiducie, à des systèmes civiliste tel que celui de la Chine.

Cette thèse offre une meilleure compréhension de la double propriété en fiducie, et par le biais d'études comparatives, débat du meilleur moyen d'implanter la fiducie en Chine. Elle affirme que le concept de double propriété, souvent rencontré dans les études comparées, ne constitue pas un obstacle à l'introduction de la fiducie dans les systèmes civilistes. En prenant la notion des études comparatives actuelles, qui visent à « comparer la fonction, plutôt que la forme » des concepts juridiques, cette thèse avance une interprétation de la double propriété en Chine, basée sur le « système binaire des droits réels et personnels. » Il effectue cela en aménageant la notion de propriété des systèmes de Common Law, qui attribue au fiduciaire la propriété juridique, et en introduisant un équivalent fonctionnel de la propriété réelle, par le biais d'une catégorie particulière de droits personnels.

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INTRODUCTION

As a product of equity jurisprudence under the common law, a key component to understanding the operation of the common law trust is an appreciation of dual ownership, i.e. legal ownership and equitable ownership in the historically separate jurisdictions of common law and equity respectively. However, this split ownership understanding of the trust is significantly different from civilian property systems where ownership has been considered absolute and indivisible. The difference in the conception of ownership raises the greatest challenges in fitting the trust into a civilian system, without damaging either the trust concept or the civil law framework.

As one of the first socialist and civil law jurisdictions to introduce a domestic law of trusts, China's legislation and practice of the ownership of trust property has important research significance. It could help to modernize China's financial infrastructure, and will also shed light on the legislation of trusts in civil law jurisdictions where dual ownership is not recognized. Thus, this thesis considers Chinese law as a case study. In China the study of trusts has a short history. China promulgated the *Trust Law of People's Republic of China* (hereinafter referred to as *Trust Law of China*)¹ in 2001. However, in contrast to the concept of the trust under common law, the Chinese trust is more similar to a contractual relationship between a securities investment company and its clients. This causes a number of problems with Chinese trust law. Therefore,

¹ *Trust Law of the People's Republic of China*, (Adopted at the Twenty-First Session of the Ninth National People's Congress, promulgated by Order No. 50 of the President of the People's Republic of China on April 28, 2001, and effective as of October 1, 2001). The governmental English translation of the *Trust Law of China* (<http://english.gov.cn/laws/2005-09/12/content_31194.htm>) is set out as an annex to this thesis.

this thesis proposes a better understanding of the dual ownership of trust property in Chinese law, and proposes amendments to Chinese trust law.

The objective of this thesis is to provide a better understanding of the dual ownership of trust property and to develop the best way the trust can be incorporated into Chinese law. In order to achieve this objective, this thesis is divided into four chapters. Chapter I discusses the well-known common law trust and its dual ownership in common law. Chapter II analyses the introduction of trusts into civilian jurisdictions. Chapter III examines the regulations of the Chinese trust law and points out its uncertainties. Finally, Chapter IV proposes amendments to Chinese law and a proposal for the best way of introducing the trust in China. Based on a comparative study of ownership of trust property between common law and civil law, this thesis states that their definitions of ownership are not exactly the same and it consequently leads to the difference in owners' rights and obligations. Therefore the terminology for comparative studies is potentially misleading. In other words, this thesis supports Professor Lionel Smith's claim that dual ownership is a misunderstanding of common law trusts by civilian jurists.² Characterizing the nature of the trust in the concept of dual ownership does not depend upon using the terms 'legal' and 'equitable', "although of course [they] are convenient labels. It depends upon properly elaborating the various personal and proprietary rights, powers and duties that make up this relationship. There is no reason on earth to think that it is impossible to do this without maintaining two divided 'systems' of property law or property rights."³ Therefore, dual ownership is not an obstacle to the introduction of trust law in China.

² Lionel Smith, "Trust and Patrimony" (2009) 28 *Estates, Trusts & Pensions Journal* 332 at 332.

³ J E Penner, *The Law of Trusts*, 8th ed (Oxford: Oxford University Press, 2012) at 41.

After recognizing the possibility of introducing trusts to China without dual ownership, questions arise as to how this change should be implemented, especially with regards to the design of China's ownership of trust property. For instance, whether Chinese trusts should use the notion of patrimony, like Quebec law, or accommodate the binary system of personal claims and real rights. This leads to further questions: to whom the unitary ownership should be granted, trustees, beneficiaries or the trust itself? And, how to explain the nature of a beneficiary's right in a trust? This thesis indicates that the key to understanding dual ownership in China is to apply 'the binary system of real rights and personal claims' to achieve the functions of financial management and beneficiary security of trusts. Therefore, China should maintain its indivisible ownership while accommodating common law ownership as a trustee's unitary ownership in real rights, and introduce a functional equivalent to equitable ownership as a special kind of personal claim. This manner of introducing the trust is proposed by this thesis because it best fits with the Chinese legal system and without doing damage to the intended functions of a trust as developed under the common law.

In developing this thesis, the author plans to employ comparative, critical/reformist, theoretical, and interdisciplinary methodologies. Firstly, comparative studies of trusts and the ownership of trust property are shown to be necessary by the differences in the concept of ownership between common law and civil law. These comparative studies can help provide a better understanding of the ownership of trust property. Moreover, the necessity of comparative studies is underlined by the current problems of Chinese trust law. Comparative studies will help China integrate into international markets and learn some advanced regulations from industrialized countries. They will also help China identify the innovations that may assist further

reform efforts.

Secondly, criticism of the current problems with Chinese trust law, both on theoretical and doctrinal grounds, will feature prominently in my project. Furthermore, based on the premise that a better understanding of dual ownership and a well-functioning trust system are required in China, the thesis will propose reformist solutions to solve the problems identified. Moreover, taking advantage of comparative studies, this thesis explores the use of legal transplants as means of law reform and develops the best way that the trust can be introduced in China. Thirdly, the thesis will employ theoretical methodology to explore the underlying principles, reasons and broad context of my research, such as the main principle of comparative law that focuses on comparing function rather than form. Last, but not least, my theoretical methods will involve aspects of interdisciplinary study, for example, the proposed design of China's ownership of trust property needs to draw on work in economics.

I COMMON LAW TRUST AND ITS DUAL OWNERSHIP

In the first chapter, the author examines the common law trust, particularly focusing on its dual ownership. This chapter consists of four parts: definitions and the nature of the common law trust, the concept of dual ownership in common law, the legal ownership of trust property, and the equitable title to trust property.

1. Definitions and the Nature of the Common Law Trust

In the first section, the author indicates various definitions of the common law trust and deduce the nature of the trust from its definitions.

A. Definitions of the Common Law Trust

It is difficult to have a unified definition of the trust. The concept of trusts has grown gradually over the centuries, adapting with marked flexibility to the demands that society has made upon it. The trust has been defined as a method of wealth management, a relationship, a segregated fund, and an equitable obligation.

From the perspective of contemporary tax-planners, the trust in broad terms is a method of managing wealth for the benefit of one or more persons. But this definition “does not reflect the various ways in which a trust may come into existence, and it fails to mention the possibly surprising fact that one person can be settlor, trustee, and a beneficiary of the same trust”.⁴ Among common lawyers, the best definition of the trust is “the relationship which arises

⁴ Donovan W.M. Waters, Mark Gillen & Lionel Smith, *Waters’ Law of Trusts in Canada*, 4th ed (Toronto: Carswell, 2012) at 3.

whenever a person (called the trustee) is compelled in equity to hold property, whether real or personal, and whether by legal or equitable title, for the benefit of some persons (of whom he may be one, and who are termed beneficiaries) or for some object permitted by law, in such a way that the real benefit of the property accrues, not to the trustees, but to the beneficiaries or other objects of the trust.”⁵

Professor Donovan W.M. Waters characterizes the common law trust as segregated property. He states that the trust is “a segregated fund comprising an asset or a number of assets, a person or purpose as the object of the trust with exclusive right to the enjoyment of the fund or its dedication, and a person holding title to the asset or assets held in the trust and in some instances administering or managing the fund”.⁶ The term ‘fund’ emphasizes that the original assets held in the trust may be disposed of and others acquired in their place. The fund is the on-going asset holding at any one time subject to trust terms.

In addition, another well-known definition that has been cited with judicial approval states: “[a] trust is an equitable obligation, binding a person (called a trustee) to deal with property (called trust property) owned by him as a separate fund, distinct from his own private property, for the benefit of persons (called beneficiaries or, in old cases, *cestuis que trust*), of whom he may himself be one, and any one of whom may enforce the obligation.”⁷ This definition has been completed by adding the clause that a trustee may hold property, not for the benefit of persons, but for the furtherance of certain purposes: namely “or for a charitable

⁵ L.A. Sheridan, *The Law of Trusts*, 12th ed (Chichester: Barry Rose Law Publishers Ltd, 1993) at 3.

⁶ Waters, Gillen & Smith, *supra* note 4 at 3.

⁷ David Hayton, Paul Matthews & Charles Mitchell, eds, *Underhill and Hayton Law of Trusts and Trustees*, 18th ed (London: LexisNexis, 2010) at 2.

purpose, which may be enforced at the instance of the Attorney-General, or for some other purpose permitted by law, although unenforceable.”⁸ Accordingly, trusts can be classified into trusts for persons, charitable trusts, and private purpose trusts.

B. The Nature of the Common Law Trust

From the above definitions of trusts, it is not hard to find that the nature of common law trusts is a property holding and management device where the property in question constitutes a segregated fund. This nature involves three aspects: a fiduciary relationship, the independence of the trust property and dual ownership of the trust property. This section briefly analyses the first two aspects and leaves the third one, dual ownership, to be specifically examined in the next section.

Firstly, a fiduciary relationship exists between trustees and beneficiaries because the trustees hold the trust property for the benefit of the beneficiaries or for a purpose. In the trust, settlors transfer their assets to trustees to manage and administer based on their faith in the trustees. The trustee holds the title to the property for the benefit of all the beneficiaries. When the trustee is one of the beneficiaries, he may manage the property partially for his own benefit. However, even in such a case, a fiduciary relationship remains between the trustee and all the beneficiaries. As Professor Waters said: “the trustee may indeed have two hats, that of trustee and of beneficiary, but he is bound to wear only the hat of trustee when he carries out any duty of the trustee.”⁹ In other words, the trustee bears a fiduciary duty, an obligation rooted in the duty of

⁸ Philip H. Pettit, *Equity and the Law of Trusts*, 12th ed (Oxford: Oxford University Press, 2012) at 30.

⁹ Waters, Gillen & Smith, *supra* note 4 at 10.

loyalty, which requires him to hold and administer the property strictly in the best interests of all the beneficiaries. McLachlin J., of the Supreme Court of Canada, set out a classic statement of fiduciary relationship in *Canson Enterprises Ltd v Broughton & Co.*¹⁰:

The essence of the fiduciary relationship, by contrast, is that one party pledges herself to act in the best interest of the other. The fiduciary relationship has trust, not self-interest, as its core, and when breach occurs, the balance favours the person wronged. The freedom of the fiduciary is diminished by the nature of the obligation he or she has undertaken.

Secondly, trust property is independent from both the settlor's assets and the trustee's personal property. The settlor loses his ownership of the trust property when he transfers the property to the trustee, unless he retains the right to revoke. As a result, the creditors of the settlor have no claims on the trust property. Moreover, the trust property must be separated from the trustee's personal property. Therefore, the personal creditors of the trustee have no claim against the trust property but only against the trustee's personal assets. This is the result of the segregated nature of the trust property, i.e. the trustee's two hats of the fiduciary office and his personal affairs. "The two roles are distinct, as is the property concerned with each. Consequently, the trust beneficiary takes his interest in the trust property ahead of the trustee's personal creditors."¹¹ Moreover, it is noted that even trust creditors have no direct claims on the trust property in common law. Professor Smith states that the trust creditor, "just like a personal creditor of the trustee, has no direct access to the trust assets".¹² Nevertheless, Smith is careful to mention that "in some jurisdictions, the law has changed so as to give creditors direct access to the trust assets. The clearest example is in the United States".¹³

¹⁰ *Canson Enterprises Ltd v Broughton & Co*, [1991] 3 S.C.R. 534 at para 3.

¹¹ Waters, Gillen & Smith, *supra* note 4 at 13.

¹² Smith, "Trust and Patrimony", *supra* note 2 at 338.

¹³ Lionel Smith, "Scottish Trusts in the Common Law" (2013) 17 *Edinburgh Law Review* 283 at 305.

The success of the trust is due, in great part, to these two features. The independence of the trust property successfully immunizes the trust property from the claims of the trustee's personal creditors or spouse in the event of bankruptcy or divorce. The fiduciary relationship, on the other hand, ensures that the trustee's *prima facie* absolute ownership is exercised for the benefit of the beneficiary. These two characteristics combine to enable an effective splitting of the facets of ownership between different parties, which is known as the dual ownership of trust property. It keeps a balance between the trustee who has independent control over the trust property and the beneficiary who can enforce stringent duties against the trustee.

2. The Concept of Dual Ownership in Common Law

This section examines the basic principles of dual ownership of trust property in the common law. It focuses on the roots of the dual ownership in the separate common law and the Chancery courts, which were merged in 1875.

As opposed to civilian absolute and indivisible ownership, there is dual ownership of trustees and beneficiaries in common law. The concept of dual ownership resulted from the influence of the courts of equity and was rooted in two separate court systems that operated in tandem in England before the development of modern trust law. The two separate systems of courts were the King's Courts and the Court of Chancery. The law that was interpreted and moulded in the King's Courts is the common law in the strict sense and the law that was gradually established in the Lord Chancellor's Court is equity. Equity is "designed as an act of the King's residual justice to bring equity to bear in the application of the laws of the realm ... [It]

assumed the existence of the common law, assisting, modifying, and supplementing it.”¹⁴ But because equity is the King’s personal ruling concerning the application of his justice in the realm, it is superior in authority. Common law and Equity were therefore distinct, but complementary.

With regards to trusts, the common law courts recognized legal ownership in property and considered the *feoffees to uses*; the Chancellor, on the other hand, focused on the enjoyment to property by forcing *feoffees to uses* to hold the property for the benefit of the *cestui que uses* on the basis of conscience. As the Chancellor’s intervention became more regular, the Court of Chancery emerged. The common law courts recognized legal ownership in property, but did not admit the existence of equitable ownership. The Court of Chancery, on the other hand, sprang up to recognize situations where the legal owner of land ought not, in good conscience, be allowed unfettered enjoyment to property owned by him, but instead, ought to be subject to an overriding claim of some other person who had a claim in conscience to the use and enjoyment of the property. Equitable title exists whenever equity will require the legal owner of property to hold the property for the benefit of some other person or group of persons. In the eyes of equity, those for whom the property is held are the real owners of the property; whereas, they do not disturb the legal owner’s title to, or possession of, the property.¹⁵ The Court of Chancery protected the beneficiary’s rights to ensure the achievement of equity or justice. “If a man promised to hold his legal estate so that the property was to be enjoyed by another, the Chancellor saw to it that that duty was enforced.”¹⁶ In other words, “Chancery could not order that the legal ownership of the property change, but it could make orders against the person who holds that legal ownership.

¹⁴ Waters, Gillen & Smith, *supra* note 4 at 5.

¹⁵ Penner, *supra* note 3 at 14.

¹⁶ Waters, Gillen & Smith, *supra* note 4 at 10-11.

Thus, a Court of Chancery could order that the legal owner was personally obliged to deal with the property or sale proceeds in a way that benefited the equitable owner.”¹⁷ The concept of dual ownership under the two separate court systems is illustrated by the following example, given in *Water’s Law of Trusts in Canada*:

In the eyes of the common law courts if T held the legal title to land or chattels, he had the rights of disposition, management and enjoyment of that property. But, if T had earlier promised the transferor to hold the property for the enjoyment of a person other than T himself, the Court of Chancery was asked and finally agreed to enforce the moral obligation. At law, T might be owner in the fullest sense that the common law recognized ownership, but in equity – which T could not avoid if he were summoned to account – B, the intended beneficiary, could compel T to yield up the enjoyment in the property and indeed administer it on B’s behalf.¹⁸

Although the two types of courts were later merged in 1875 and equitable interests are now recognized by all branches of the court, and may therefore in a sense be considered legal, the distinction in law between legal and equitable ownership lives on as a primary tenet of trust law. The distinction is fundamental and ineradicable even though the separate jurisdictions have been abolished. The difference between legal and equitable interest is not merely of theoretical interest. A legal title prevails against the whole world unless statute-barred¹⁹ whilst an equitable title prevails against third parties except where there is a *bona fide* legal interest for value without notice of the equitable interest.²⁰ “Indeed, in a sense the whole point of the trust is to separate the benefit of property from the right to exercise the powers that go with having legal title. This is true even in a case where the terms of the trust allow the beneficiary to enjoy the

¹⁷ John E. S. Poyser, Larry H. Frostiak & Grace Chow. *Taxation Of Trusts and Estates: A Practitioner’s Guide 2014* (Toronto: Carswell, 2014) at 12.

¹⁸ Waters, Gillen & Smith, *supra* note 4 at 6.

¹⁹ See *Wylde v Silver*, [1963] Ch 243, [1962] 3 All ER 309; *Benn v Hardinge* (1992) 66 P & CR 246, CA.

²⁰ Hayton, Matthews & Mitchell, *supra* note 7 at 74-75.

trust property *in specie*, i.e. possess the trust property.”²¹ Therefore, the dual ownership, the segregation of control and the benefits of trust property, together are the base upon which the modern trust is built. As will be discussed, many scholars argue that the essence of trusts should not be dual ownership.²² However, in order to address the challenges of incorporating the trust into a civil law system, this thesis adopts the traditional language of dual ownership.

3. The Legal Ownership of Trust Property

After examining the basic principles of dual ownership, this section and the next respectively discuss the trustee’s legal ownership and the beneficiary’s equitable title in detail. It argues that an analysis of the trustee’s powers and obligations, and that of beneficiary rights, helps explain how dual ownership in the common law, i.e. the separation of the right to manage trust property and the right to its enjoyment, actually functions.

The legal ownership of the trust property authorizes the trustee to have the legal rights and powers associated with the property. However, the trustee must act upon these rights and powers in accordance with his personal obligation, i.e. to exercise his ownership of the property according to the trust terms and thus to ensure the benefit of the beneficiaries.²³ Therefore, the trustee’s legal ownership includes two aspects: the trustee’s legal title to the trust property and his duties to the beneficiaries. The first aspect entails that, on the one hand, the trustee enjoys a *prima facie* absolute title *vis-à-vis* the outside world to deal with the property in a way an absolute owner might enjoy; on the other hand, the trust assets are separated from the trustee’s

²¹ Penner, *supra* note 3 at 26.

²² This will be discussed in Chapter IV 1 A (1).

²³ Penner, *supra* note 3 at 21.

personal assets, and are thus immune from his creditors, successors, or spouses in the event of bankruptcy, death, or divorce. The second aspect, a series of default duties, in particular fiduciary duties, is adopted to ensure that the trustee's *prima facie* absolute title is exercised only for the benefit of the beneficiaries or certain purposes. This section examines the two aspects of the legal ownership of trust property in subsections B and C, but before discussing the powers and obligations of trustees, it is necessary to first clarify that a trust does not fail for want of a trustee in subsection A.

A. A Trust Does Not Fail for Want of a Trustee

A trustee can be either a single person or a group of people in the form of joint trustees, in which case the trustees are requested to act together and be jointly and severally liable for breach of trust.²⁴ Moreover, both natural persons and legal persons can act as trustees. Even though a trustee is essential to a trust, a trust does not fail simply “because no trustee is designated or because the designated trustee declines, is unable, or ceases to act, unless the trust’s creation or continuation depends on a specific person serving as trustee”.²⁵ In English law, for example, according to section 36(1) of the Trustee Act 1925, one or more new trustees may be appointed, by writing, “in the place of the trustee so deceased remaining out of the United Kingdom, desiring to be discharged, refusing, or being unfit or being incapable, or being an infant, as aforesaid.”²⁶ On the death of a sole or last surviving trustee, the trust property devolves upon his personal representatives.²⁷ If nobody can be found who is willing to carry out the trust,

²⁴ D.W.M. Waters, “The Institution of the Trust in Civil and Common Law” (1995) 252 *Recueil de Cours* 113 at 225.

²⁵ *Restatement (Third) of the Law of Trusts*, § 31 (2001).

²⁶ *Trustee Act 1925* (UK), 1925, c 19, s 36(1).

²⁷ John Mowbray et al, *Lewin on Trusts*, 18th ed (London: Sweet & Maxwell Ltd, 2008) at 441.

the court can in certain circumstances appoint the Public Trustee or a judicial trustee to discharge the trust. As a last resort, the court can even act as a trustee itself on an *ad hoc* basis.²⁸

This rule, a trust does not fail for want of a trustee, has exceptions. Some trusts require specific trustees. In this unusual case, it is a prerequisite to the existence of the trusts that only a specific, named trustee shall hold the office. As Buckley J said in *Re Lysaght*²⁹, in such a case, it is of the essence of a trust that the trustees selected by the settlor, and no one else, shall act as the trustees of it. If those trustees cannot or will not undertake the office, the trust must fail. Moreover, in such a case, a trust will fail where the potential trustee disclaims the trusteeship. In those rare situations, the trust is treated as never having come into effect. This is said to have been void *ab initio*.³⁰

B. The Trustee's Title to the Trust Property

Knowing that a trust does not fail for want of a trustee, we can now discuss the powers of the trustee. Subject to the terms of the trust, trustees have two main types of powers: administrative powers and dispositive powers. “Administrative powers enable trustees to manage the trust property. Dispositive powers enable the trustees to transfer trust assets to the beneficiaries.”³¹ These two powers can look remarkably similar. For instance, when trustees transfer a trust asset, if the transfer is made to a beneficiary, it is an exercise of a dispositive power, whereas if the transfer is made to a third party, it is an exercise of an administrative

²⁸ Gary Watt, *Equity and Trusts Law*, 3rd ed (Oxford: Oxford University Press, 2012) at 234.

²⁹ *Re Lysaght: Hill v Royal College of Surgeons*, [1966] Ch 191 at 194.

³⁰ Watt, *Equity and Trusts Law*, *supra* note 28 at 228.

³¹ A.H. Oosterhoff et al, *Oosterhoff on Trusts: Text, Commentary and Materials*, 7th ed (Toronto: Carswell, 2009) at 1115.

power.³²

(1) A trustee's administrative powers

The administrative power is granted to trustees to enable them to manage the trust property so they can best fulfill the terms of the trust,³³ such as the power to maintain the value of the trust property, the power to make contracts, and the power of investment.³⁴ In addition, the trustees have the power of appropriation, that is “trustees may require to appropriate particular assets in full or partial satisfaction of some interest under the trusts, whether fixed by reference to a fraction or by reference to a value in money, and whether there is a beneficiary absolutely entitled or whether the appropriated assets will continue to be held on the trusts affecting the particular interest”.³⁵ The trustees also have powers in relation to mortgages. They “may hold an equity of redemption or a mortgage as trust property, though the latter is not nowadays a common form of trustee investment”.³⁶

The trustee's administrative power is primarily from two sources: the trust instrument and legislation. Prior to the 19th century, all the powers entitled to the trustees were written into the trust instrument by settlors, and often this required great detail. During this time, efforts were made in England to reduce the necessary length of trust deeds and wills by making the most familiar of the administrative powers statutory, namely the settlor need not make any specific reference to them unless the trust instrument exclude them. These statutory powers have been

³² *Ibid.*

³³ Waters, Gillen & Smith, *supra* note 4 at 1135.

³⁴ Penner, *supra* note 3 at 21.

³⁵ Mowbray, *supra* note 27 at 1361.

³⁶ *Ibid* at 1372.

developed in England and were adopted early on by Canadian law.³⁷ Examples of these statutory powers found in contemporary Trustee Acts are the powers to insure trust property, to issue receipts for assets transferred to the trustees, and to compound debts and compromise claims brought by or against the trustees. A number of standard, general, and more basic powers necessary for the proper functioning of the trust are conferred upon trustees by legislation.³⁸

The legislative powers can be excluded or amended by the trust instrument. The administrative powers created by the trust instrument, known as express powers, should be specific and tailored to achieve the purpose of the trust. The express powers stipulated in the instrument offer the trustee incentive or freedom that can encourage the trustees to enter into agreements or conduct transactions for the benefit of the trust.³⁹ With respect to the express powers, the most difficult question is how far the trustees should be given freedom of action. It is believed that “[t]he state of the investment market and the volatile character of the taxing statutes encourage a testator or settlor to give his trustees the widest possible powers compatible with the nature of a trust, and modern trustee investment legislation leans in this direction.”⁴⁰ In addition to the powers given by the trust instrument and granted by legislation, if additional administrative powers are required, the trustee can make application to the court in Canada.

(2) A trustee’s dispositive powers

In contrast with the administrative powers that are concerned with the management of the trust property, a dispositive power is “an authorization to the trustee to allocate or distribute

³⁷ Waters, Gillen & Smith, *supra* note 4 at 1136.

³⁸ Oosterhoff, *supra* note 31 at 1116-17.

³⁹ Waters, Gillen & Smith, *supra* note 4 at 1138.

⁴⁰ *Ibid* at 1139.

trust property to a beneficiary of the trust”.⁴¹ Familiar examples of dispositive powers are the power of maintenance, the power of advancement, the power of appointment, and powers of selection under discretionary trusts. A trustee may have one or all of these powers, though the latter would be unusual. Powers of maintenance and advancement are described by the purpose for which the power is given and they will usually be granted to trustees by the settlor’s *inter vivos* or a testamentary instrument under the family trust in favour of minors and young adult beneficiaries entering marriages or starting careers. Conversely, in this situation the trustee will not be conferred a power of appointment, which is a power to transfer property, without any *a priori* fetter as to the purpose of the transfer, except in the situation of where the trustee is also a beneficiary of the trust and a member of the family.⁴² With respect to the discretionary trust, it is “sometimes referred to as a power of selection: the trustee is required to distribute property among persons but may choose who gets what... Any of these rights can be over income or capital or both”.⁴³

(a) The power of maintenance

A power of maintenance is the authority to apply income, or capital in certain circumstances, for the immediate and recurring needs of a beneficiary.⁴⁴ This power is normally used to provide for basic needs such as food, shelter, clothing, and medical care. In Canada, the legislation of some provinces also allows the power of maintenance to be used to provide for the

⁴¹ *Ibid* at 1171.

⁴² *Ibid* at 1171-72.

⁴³ *Ibid* at n 1.

⁴⁴ See *Crane v Craig* (1886) 11 P.R. 236 (Ont. H.C.); *Re Green* (1908) 9 W.L.R. 630 (Sask. Chambers).

education of beneficiaries, such as Alberta and British Colombia.⁴⁵

With respect to the express power of maintenance, a question arises as to its scope. First, it is evident from *Barclay v Zavitz*⁴⁶ and *Donald v Donald*⁴⁷ that the setting out of the interests to be transferred to beneficiaries should be kept distinct from the power of maintenance within the instrument. Second, like the situation which occurred in *Singer v Singer*⁴⁸, a clear distinction needs to be made between an instrument that creates a power of maintenance and a trust to maintain. Third, if a discretionary trust is created for the maintenance of a number of persons, the settlor has to ensure that the trustees can maintain individuals within the class to the exclusion of others whom they do not consider to be in need. With respect to the scope of the trustee's power of maintenance in this case, *Coy v Coy* addressed that the trustee "was not at liberty to select one child and give the whole proceeds to such one; the discretion vested in the trustee being as to the amount and mode of application – not as to the persons to be benefited."⁴⁹ In other words, "the trustee had no discretion as to, who, only as to how much, when, and in what form."⁵⁰

After analyzing the express power of maintenance, the author may now move to the subject of statutory powers of maintenance. The development of the statutory powers in England has gone through three distinct stages in 1860, 1881, and 1925. In 1860, *Lord Cranworth's Act* provided in section 26 that the statutory powers of maintenance would apply automatically unless the testator or settlor amended it in any way or declared it was not to apply. It also

⁴⁵ Oosterhoff, *supra* note 31 at 1119, n 26.

⁴⁶ *Barclay v Zavitz* (1885), 8 O.R. 663.

⁴⁷ *Donald v Donald* (1884), 7 O.R. 669.

⁴⁸ *Singer v Singer* (1916), 52 S.C.R. 447, 27 D.L.R. 220 (S.C.C.) at 461 [S.C.R.].

⁴⁹ *Coy v Coy* [1877], 25 Gr. 267 (Ont. Ch.) at 270.

⁵⁰ Waters, Gillen & Smith, *supra* note 4 at 1182.

stipulated that if the beneficiary is an infant, either absolutely, or contingently on his attaining the age of twenty-one or the occurrence of an event prior to his attaining that age, the trustees could pay income of that interest to the guardians, or on behalf of the child, for maintenance or education. However, this provision has failings. It did not apply to a defeasible interest but only to vested and indefeasible absolute interests. It would only apply if the contingency was attaining the age of twenty-one or a major event such as marriage occurred before that age was attained. As a result, when there was a double contingency or a sole contingency that happens after the attainment of majority, the intermediate income could not be used for maintenance. In order to revise these failings, the *Conveyancing Act* was introduced in 1881. It repealed the old section in *Lord Cranworth's Act*. One big improvement with the new section was that it included vested or contingent life interest and thus beneficiaries of such interests could now be maintained out of intermediate income. Nevertheless, beyond the introduction of the life tenancy, no other substantive changes were made in this new section except the improvement of language and arrangement.⁵¹ Therefore, in 1925 Parliament redesigned the section and as a result, section 31 of the *Trustee Act* was introduced, which remains the current law in England. With respect to maintenance rights, “the new section now applies to the vested, but defeasible, interest, and it does not matter if the payment date of a vested interest is postponed beyond the attainment of majority, or that the gift is contingent upon the attainment of an age greater than majority, or an event which may happen after the beneficiary’s majority.”⁵²

In Canada, the Trustee Acts in different provinces and territories complete the picture of

⁵¹ *Ibid* at 1184-85.

⁵² *Ibid* at 1185.

England's historical development and present an array of approaches to the subject of statutory powers of maintenance. Alone among all the other provisions and territories, Ontario has no statutory maintenance power stipulated in its Trustee Act. If the trust contains no express power, application has to be made to the court under its inherent jurisdiction. Section 36 of the Trustee Act⁵³ is of assistance in practice. It requires a personal representative, a guardian, or a trustee, on the passing of his final accounts, to pay into the Superior Court any money in his hands belonging to an infant. When the money is required for maintenance, the Children's Lawyer or the Public Guardian and Trustee may apply for payment out of the funds in court.⁵⁴

(b) The power of advancement

The power of advancement is a power granted to the trustee to pay a beneficiary part of the capital of a gift before the capital falls into the beneficiary's hands, so that the beneficiaries may take advantage of some opportunity that will further them in life.⁵⁵ Even if the settlor does not say, it may be granted by statute where the beneficiary is an infant and has an interest in capital that is vested in interest, where there is a vesting in interest but possession is postponed to a future date.

The term 'advancement' was used in the 18th century to describe the 'setting up in life' of a young person. It includes payments for the purposes of starting a person in business or in profession, paying apprenticeship fees, and supplying capital to enable an existing business to be

⁵³ *Trustee Act*, RSO 1990, c T-23, ss 36(4) and (6).

⁵⁴ *Ontario Rules of Civil Procedure*, RRO 1990, Reg 194, R. 72.03.

⁵⁵ See *Brooke v Brooke* (1911), 3 O.W.N. 52, 20 O.W.R. 27 (Ont. H.C.) 52 at 54; *Patterson v Royal Trust Co.*, 36 D.L.R. (3d) 590 (Q.B.).

carried on.⁵⁶ It also includes the payment of a debt if the debt is substantial and the payment is once-and-for-all.⁵⁷ The test to be applied is whether the payment is of a casual nature. If it is, it is not an advancement. Middleton J. adopted an American judicial statement described in *Bailey v Bailey* and said in *Brooke v Brooke* that:⁵⁸

it may not be easy to define with precision what is mean by “advancement in life” ... but it seems to us to point to some occasion out of the everyday course, when the beneficiary has in mind some new act or undertaking which calls for pecuniary outlay, and which, if properly conducted, holds out a prospect of something beyond a mere transient benefit or employment.

Canadian courts have recognized a more restricted view of the scope of this term. In *Re Hall*, Boyd C. stated that under Canadian law “an advancement is neither a loan or debt to be repaid”,⁵⁹ by which “he meant that ‘advancement’ connotes payments to start a person off on an activity, not the paying of existing debts which is part of the ongoing assistance one person, especially in a parental situation, might be expected to give to another, for instance, his child.”⁶⁰ Whereas, in recent years, both English courts and some Canadian courts have tended to give a broad meaning to the term. Therefore, the advancement power of the trustee means to set up a beneficiary in life, which may be accomplished by purchasing a business for the beneficiary or paying a substantial debt owed by the beneficiary.

With respect to the express power of advancement, it is suggested that such power should be authorized to the trustee in the widest terms in determining whether a payment ought to be made because the term of advancement is a formula that is considerably more liberal. “If

⁵⁶ Waters, Gillen & Smith, *supra* note 4 at 1191.

⁵⁷ *Ibid* at n 94: *Re Scott*, [1903] 1 Ch. 1 (Eng. Ch. Div.).

⁵⁸ *Ibid* at n 95: (1911), 3 O.W.N. 52, 20 O.W.R. 27 (Ont. H.C.), citing a description of advancement given in *Bailey v Bailey* (1888), 14 Atl. R. 917.

⁵⁹ *Re Hall* (1887), 14 O.R. 557 at 559.

⁶⁰ Waters, Gillen & Smith, *supra* note 4 at 1191-92.

trustees are to be given the power to make capital payments for the purpose of advancement to beneficiaries whose interests are contingent or defeasible, the instrument should make this clear. Otherwise, the trustees may have to seek a construction of the instrument before it is wise for them to pay capital.”⁶¹ In *Re Finlayson*, it is stated by Drake J. that it is possible for the trustees to exercise the power of advancement during the lifetime of the life tenant (income beneficiary), but the construction of the instrument was based on the fact that to “hold otherwise would practically render the advancement of little value”.⁶² If the trustee’s power is to pay or apply his decision to make a payment for advancement purposes itself, it is sufficient to constitute an application. Neither payment to the beneficiary nor a guardian is necessary.⁶³ If the power of advancement is to be exercised for a class of beneficiaries among whom the fund is to be divided at some future time, the instrument should make the settlor’s purpose clear whether any payment of capital is to be taken into account in the ultimate determination of the shares of capital. If payments by way of advance are to be brought into hotchpot, the will must say so; the same applies to *inter vivos* trusts.⁶⁴

With regards to the issue of the statutory power of advancement, similar to the statutory power of maintenance, the English precedent directly inspired Canadian legislation. In England, the first statutory power was introduced in 1925 in the form of the *Trustee Act*. It is stipulated in section 32 that:

Trustees may at any time or times pay or apply any capital money subject to a trust, for the advancement or benefit, in such manner as they may, in their absolute discretion, think fit, of any person entitled to the capital of the trust property or of any share

⁶¹ *Ibid* at 1194.

⁶² *Re Finlayson* (1897), 5 B.C.R. 517 (B.C. Co. Ct.) at 520.

⁶³ *Lloyds Bank v O’Meara* [1950] 2 All E.R. 891 (Eng. C.A.) at 900-01.

⁶⁴ Waters, Gillen & Smith, *supra* note 4 at 1196, nn 115-16.

thereof, whether absolutely or contingently on his attaining any specified age or on the occurrence of any other event, or subject to a gift over on his death under any specified age or on the occurrence of any other event, and whether in possession or in remainder or reversion, and such payment or application may be made notwithstanding that the interest of such person is liable to be defeated by the exercise of a power of appointment or revocation, or to be diminished by the increase of the class to which he belongs: Provided that – (a) the money so paid or applied for the advancement or benefit of any person shall not exceed altogether in amount one-half of the presumptive or vested share or interest of that person in the trust property...⁶⁵

This section is based upon two central characteristics: first, the statutory power shall be implied in all trusts of personalty and apply to all beneficial interests unless there is provision to the contrary; and second, the power only applies to half the capital interest. The first characteristic makes it possible to apply the power to all beneficial interests regardless of the contingency, defeasibility or postponement of enjoyment, or whether the interest is immediate, in remainder or in reversion. In *Pilkington v Inland Revenue Commissioners*⁶⁶, the trustee was authorized to pay a considerable sum of capital to sub-trustees by way of advancement of Penelope, who was four years old when the trustees decided on this course of action, and whose family life was stable and comfortable. With regards to the second characteristic, a further limitation may arise as to any payment must be brought into hotchpot.

In Canada, “[o]nly Manitoba and Prince Edward Island have a statutory power of advancement.”⁶⁷ In 1968, Manitoba regulated its own statutory power of advancement based on a few amendments to the English provisions because it had no settled land legislation. First, it extended the power to include land or any interest therein as well as personalty. Moreover, in addition to advancement and benefit, it also explicitly covers maintenance and education.

⁶⁵ *Supra* note 26, s 32.

⁶⁶ *Pilkington v Inland Revenue Commissioners* (1962), [1964] A.C. 612.

⁶⁷ Waters, Gillen & Smith, *supra* note 4 at 1198.

Nevertheless, Manitoba still requires the trustees to obtain judicial consent every time they wish to exercise the power, whether for maintenance, education, advancement, or benefit.⁶⁸ With regards to Prince Edward Island, it adopted section 32 in 1956 with an addition made to apply this provision also to realty and personalty.⁶⁹

(c) The power of appointment

A power of appointment is sometimes defined as a power to create new trusts for the beneficiaries. It refers to the power of selection that a trustee has in the context of a discretionary trust: to choose which beneficiaries shall receive property and how much.⁷⁰ It is known that powers to be exercised by a trustee can be classified into pure powers and trust powers. When it is a trust power, the trustee must exercise it as an obligation; if he does not the court will. In contrast, if it is a pure power, the court cannot compel the exercise of the power and the trustee's intention for doing so is irrelevant. However, a trustee cannot release his power when it is a power *virtute officii*.⁷¹ A particular type of power of appointment is the power of encroachment. It applies when the settlor confers upon a designated individual the power to distribute capital to an income beneficiary. The designated individual is normally the trustee, but may also be another beneficiary, such as a life tenant.⁷²

(d) Powers of selection under discretionary trusts

Another example of the dispositive power is powers of selection under discretionary

⁶⁸ *Trustee Act*, CCSM, c T160, s 30.

⁶⁹ *Trustee Act*, RSPEI 1988, c T-8, s 40.

⁷⁰ Waters, Gillen & Smith, *supra* note 4 at 1200.

⁷¹ *Ibid.*

⁷² Oosterhoff, *supra* note 31 at 1126.

trusts. Discretionary trusts occur when the trustees are vested with property and are required to allocate it among a class of beneficiaries. Under trust law the trustees must exercise all their powers for the best fulfillment of the trust purposes and the interests of the beneficiaries. “Such discretions have their origins in an understandable desire to ensure that trustees will be able to respond to unforeseen developments.”⁷³ In a discretionary trust, the trustees have the discretion to determine the amount and time to dispose of trust property as they think fit. At times, they also have the discretion as to the form in which the disposition is to be made. Even when there is no express discretion as to the form of disposition, the trustees actually have an implied discretion stemming from the nature of the trust to make dispositions in the form of re-settlements on new trusts.⁷⁴ If the object of the trust is to provide maintenance for the members of the class of beneficiaries, the discretion will normally be over the income of the trust fund. If the object is to enable the trustees to make payments or transfers to the members, the discretion will normally be over both the income and the capital of the trust fund to be distributed.⁷⁵

However, it is noted that, due to the nature of dispositive powers, discretion must be exercised within the scope of the nature of the power, as well as determined by the settlor. This might cause a risk that the trustee will run the trust according to what he thinks the settlor would want; as a result, a trust with very wide dispositive discretions may appear at times to exist to benefit the settlor, rather than the beneficiaries.⁷⁶ Due to this, a court may sometimes interfere with the exercise of a trustees’ discretion, regardless of whether the discretion is coupled with a

⁷³ Lionel Smith, “Mistaking the Trust” (2010) 40 Hong Kong Law Journal 787 at 790.

⁷⁴ Waters, Gillen & Smith, *supra* note 4 at 1203.

⁷⁵ *Ibid* at 1203-04.

⁷⁶ Smith, “Mistaking the Trust”, *supra* note 73 at 791.

duty or not.⁷⁷ For example, a court may interfere to correct an error made by the trustees in the exercise of their discretion or where the trustees have misused their discretion. Moreover, a court will interfere when a trust holds shares in a private corporation and disputes arise over: (i) conflicts of interest between a trustee and classes of beneficiaries; (ii) the obligation of a trustee to provide information to the beneficiary about the corporation's affairs; and (iii) the resolution of a deadlock between trustees over how they should vote shares in the corporation.⁷⁸

In short, a trustee has two types of powers: the administrative powers to manage the trust property and the dispositive powers to allocate or distribute the trust property to his beneficiaries. Familiar examples of the administrative powers are the power to maintain the value of the trust property, the power to make contracts, the power of investment, the power of appropriation, and the powers in relation to mortgages. Familiar examples of dispositive powers, on the other hand, are the power of maintenance, the power of advancement, the power of appointment, and powers of selection under discretionary trusts.

C. The Trustee's Equitable Obligation

The second aspect of the legal ownership of common law is a trustee's equitable obligation. It is used to ensure that the trustee's legal title is exercised for the benefit of beneficiaries or a particular purpose. The general duty that all trustees must perform arises by virtue of the fact that they are fiduciaries. It underlies all the other duties taken by the trustees, such as the duty to exercise reasonable care, the obligation to act impartially, the duty to

⁷⁷ Oosterhoff, *supra* note 31 at 1126.

⁷⁸ Sheila M. Crummey, "Estates and Trusts Holding Shares of Private Corporations: Selected Issues" (2007) 26 E.T.P.J. 302 at 303.

safeguard and invest trust assets, and the duty to give account and provide information.

(1) A trustee's fiduciary duty

Trustees have title to, and control over, trust property. However, they hold it for the benefit of another person. This obligation is known as a fiduciary duty. "At the heart of the fiduciary relationship lies a particular notion of loyalty. In certain cases where a person is empowered to make decisions on behalf of another, equity will seek to ensure that these decisions are not taken *in conflict of interest*."⁷⁹ Therefore, this core liability of the trustee has several facets: the trustee "must act in good faith; he must not make a profit out of his trust; he must not place himself in a position where his duty and his interest may conflict; he may not act for his own benefit or the benefit of a third person without the informed consent of his principal".⁸⁰

The 'no conflict' rule is the basic rule governing fiduciaries. Under this rule, a fiduciary is liable to account for any profit he obtains in circumstance where his interests may conflict with his duty. This rule is exceptionally stringent, in that it is framed in terms of the possibility of conflict, not in terms of there being an actual conflict of interest.⁸¹ A rule derived from this basic rule is the self-dealing rule. The self-dealing rule makes voidable any transaction in which a trustee purchases the trust property or sells his own property to the trust, unless the transaction is

⁷⁹ Penner, *supra* note 3 at 19.

⁸⁰ *Ibid* at 412.

⁸¹ See *Keech v Sandford*, [1726] EWHC Ch J76; *Boardman v Phipps*, [1967] 2 AC 46; *Protheroe v Protheroe*, [1968] 1 All ER 1111; *Public Trustee v Cooper*, [2001] WTLR 901; *Hilton v Barker, Booth & Eastwood*, [2005] UKHL 8.

specifically authorized and explicit authorizations are strictly construed.⁸² The rationale is explained in *Movitex Ltd v Bulfield*⁸³: when the trustee acts both as vendor for the beneficiaries and purchaser or *vice versa*, he places himself in an obvious conflict of interest and it is impossible to determine whether he has served the beneficiaries' interests properly in securing the best price for them.⁸⁴ The fair-dealing rule applies to purchases not of the trust property itself, but of a beneficiary's interest in the trust property. In comparison to the self-dealing rule, this rule is less harsh, "for simple reason that the danger here is less: since there are two real parties to the transaction with their own interests at stake, not a trustee selling to himself, the bargain is much more likely to be a real one."⁸⁵

(2) A trustee's other duties

In addition to the fiduciary duties, the trustee has other duties upon his appointment and during the existence of the trust. Upon appointment, as Kekewich J held in *Hallows v Lloyd*, the trustees "are bound to inquire of what the property consists that is proposed to be handed over to them, and what are the trusts. They ought also to look into the trust documents and papers to ascertain what notices appear among them of incumbrances and other matters affecting the trust".⁸⁶ A trustee must obey and carry out the directions laid down in the trust. He cannot depart from the duties imposed on him or assume powers not conferred on him, even when he believes

⁸² *Tito v Waddell (No 2)* [1977] 3 All ER 129 at 241.

⁸³ *Movitex Ltd v Bulfield*, [1988] BCLC 104 at 117.

⁸⁴ A trustee, especially a sole trustee, cannot transact with the trust, i.e. himself, also because of the two-party rule, which states that, subject to statute, a person cannot contract with himself or convey property to himself and therefore a contract or conveyance purportedly entered into between a person and himself or between a person and himself and others is void.

⁸⁵ Penner, *supra* note 3 at 436-37.

⁸⁶ *Hallows v Lloyd* (1888) 39 Ch D 686 at 691.

it is for the benefit of the beneficiaries. The main initial duties are: “(a) [to] ascertain the terms of the trust; (b) acquaint themselves with the state of the trust property; (c) invest the trust property in accordance with the provisions of the trust instrument or statute; (d) ensure that the trust property is in proper custody; and, (e) if the appointment is of a replacement trustee, the new trustee must take all reasonable steps to ensure that there were no prior breaches of trust.”⁸⁷ In short, the trustee must collect the assets for the trust, ensure their safety, and then preserve and enhance their value. Failure to do any of these things would be considered a breach of trust.

During the existence of the trust, the main duties of the trustees are the duty to safeguard trust assets and invest trust funds, the duty to exercise reasonable care, the duty of impartiality, and the duty to give account and to provide information.

(a) Duty to safeguard trust assets and invest trust funds

A trustee must take all reasonable and practical steps to safeguard trust assets. Thus, he must ensure that the title to trust property is vested or registered in his name. When selling trust property, the trustee must use his best endeavours to obtain the best terms. He should not do anything that depreciates the value of the property and should ensure that trust property does not fall into decay.⁸⁸

In addition, trustees are under a duty to invest the trust funds in investments that are authorized by the trust instrument or by statute. The trustees should invest the trust property safely and so that it makes a reasonable return. They must not invest the trust property in a

⁸⁷ Oosterhoff, *supra* note 31 at 1049-50.

⁸⁸ Geraint Thomas & Alastair Hudson, *The Law of Trusts*, 2nd ed (Oxford: Oxford University Press, 2010) at 284-85.

dangerously speculative way.⁸⁹ Developed through case law, the trustees must perform this duty in compliance with the following principles: they must act prudently and safely; they must act fairly between beneficiaries; and they must act in the best interests of the beneficiaries. This best interest is generally taken to mean their financial interests⁹⁰.⁹¹ Failure to perform this duty will cause the trustee to be liable for any loss that the trust suffers.

In England, although the Trustee Act 2000⁹² allows trustees to invest in any property, it still requires the trustees to follow the standard investment criteria when exercising their investment powers. The trustees are required to consider: “(i) the suitability to the trust of investments of the same kind as any particular investment proposed to be made or retained and of that particular investment as an investment of that kind, and (ii) the need for diversification of investments of the trust, in so far as is appropriate to the circumstances of the trust.”⁹³ The first criterion demands the trustees examine whether or not the risk associated with a given investment is appropriated for making that investment and whether the trust fund of the investment would be dealt with in a suitable manner. The second criterion is bound up with a need to dilute the risk of investing in only a small number of investments. This is frequently referred to as portfolio theory, which express the notion that if an investor invests in a number of different investments across various markets then the impact of the loss in value suffered by any individual market or individual investment will be balanced out by the investments made in other

⁸⁹ Penner, *supra* note 3 at 21.

⁹⁰ Thomas & Hudson, *supra* note 88 at 303-04.

⁹¹ These duties are not restricted to trustee investment but apply more generally. Therefore, duty to exercise reasonable care is discussed separately in this section.

⁹² *Trustee Act 2000* (UK), 2000, c 29.

⁹³ *Ibid*, s 4(3).

markets that did not suffer a loss.⁹⁴ In Canada, in the absence of regulations of a trust instrument, the duty of investment is governed by statute. For example, section 26 and section 27 of the Ontario *Trustee Act* formerly made a statutory ‘legal list’ of investment. These provisions of the investment requirements imply another duty of the trustee – the duty of care.

(b) Duty to exercise reasonable care

A trustee’s duty of care, established in the late 19th century, was to take such care as an ordinary prudent man of business would take in managing another person’s affairs.⁹⁵ In the context of investment, the standard of care has been refined in *Learoyd v Whiteley*⁹⁶, which requires that a trustee use the same degree of diligence in managing the trust property as that which a person of ordinary prudence would use in managing the affairs of another person. Lord Watson said in this case that “[t]he courts of equity in England have indicated and given effect to certain general principles for the guidance of trustees in lending money upon the security or real estate”.⁹⁷ This modification allows for the fact that investment decisions affect both those persons entitled to present income and those who are to enjoy the capital at some future time.⁹⁸ In short, the duty of care requires trustees, whether in trust instruments or in statute, to act reasonably, or to take reasonable decisions in the exercise of their discretion. The reasonableness standard indicates that a trustee must be able to justify his conduct or decision on rational and relevant grounds.

⁹⁴ Thomas & Hudson, *supra* note 88 at 306-07.

⁹⁵ *Speight v Gaunt* (1883) 9 App Cas 1, 19 (affirming (1883) 22 Ch D 727, esp 736, 754).

⁹⁶ *Learoyd v Whiteley*, [1886-90] All ER Rep Ext 1806 at 1816.

⁹⁷ *Ibid.*

⁹⁸ Oosterhoff, *supra* note 31 at 1073-74.

The discharge of a trustee's duty to exercise reasonable care is flexible and changes with economic conditions and it is therefore judged applying the standards of the relevant period. Accordingly, it follows that in judging the past performance of trustees, one must avoid the "risk of applying the wisdom of hindsight and of passing judgment on the basis of modern-day standards".⁹⁹ In general, the standard of care requires a trustee to administer the trust in the way a person of ordinary prudence manages another person's affairs. A higher standard may apply to a professional trustee¹⁰⁰ and to a paid trustee in comparison with an unpaid one¹⁰¹. According to section 1(1) of the Trustee Act 2000, a trustee "must exercise such care and skill as is reasonable in the circumstances, having regard in particular – (a) to any special knowledge or experience that he has or holds himself out as having, and (b) if he acts as trustee 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".¹⁰² However, it is worth noting that "a trustee is not a surety, nor is he an insurer"¹⁰³. An ordinary prudent man is not necessarily liable for mere errors of judgment.¹⁰⁴

(c) Duties of impartiality

Another duty of the trustees is the duty of impartiality. It requires trustees to act impartially in dealing with beneficiaries; that is, they may not give preferential treatment to any one beneficiary or group of beneficiaries unless so authorized by the trust instrument. As Turner

⁹⁹ *Re Mulligan*, [1998] 1 NZLR 481 at 500.

¹⁰⁰ *Bartlett v Barclays Bank Trust Co Ltd*, [1980] Ch 515 at 534.

¹⁰¹ *Re Waterman's Will Trusts*, [1952] 2 All ER 1054 at 1055; *National Trustees Co of Australia v General Finance Co*, [1905] AC 373 at 381.

¹⁰² *Trustee Act 2000*, *supra* note 92, s 1(1).

¹⁰³ *Re Chapman. Cocks v Chapman.*, [1896] 2 Ch. 763 at 775.

¹⁰⁴ *Ibid* at 776, 778.

LJ stated in *Re Tempest*, “it is of the essence of the duty of every trustee to hold an even hand between the parties interested under the trust. Every trustee is in duty bound to look to the interests of all, and not of any particular member of class of members of his *cestuis que trust*.”¹⁰⁵ The beneficiaries of the same class are ought to be treated equally, on the basis that they enjoy equal rights, interests, or expectations.¹⁰⁶

In relation to investments, the impartiality duty aims to strike a balance between providing income for life-tenants and preserving capital for those with the remainder interest. “In order to maintain an even hand between successive beneficiaries, ideally all assets will be authorized investments. The trustees then can simply pay the income to the life-tenant and retain the capital for those entitled to the remainder.”¹⁰⁷ However, trust property often contains unauthorized investments. In this case, according to rules regulated in *Lottman v Stanford*¹⁰⁸, the trustee has to determine: whether a duty to convert a particular asset into an authorized investment exists; if so, whether the assets must be apportioned between income and capital; and if so, how the appointment is to be calculated.

In order to allow the trustee to better exercise the duty of impartiality, the trust instrument should specify the allocation of outgoings, that is, whose beneficial interest is to bear what expenses. In the absence of such express provisions, the trustee must look for the settlor’s implied intention. If even that is unclear, the trustee has to act pursuant to common law rules. The general rule is that expenses in relation to income of the trust, such as taxes and insurance,

¹⁰⁵ *Re Tempest* (1866) Ch App 485 at 487-88.

¹⁰⁶ Thomas & Hudson, *supra* note 88 at 286.

¹⁰⁷ Oosterhoff, *supra* note 31 at 1084.

¹⁰⁸ *Lottman v Stanford*, [1980] 1 S.C.R. 1065.

are borne by the income beneficiaries; whereas, the outgoings of capital, the costs of major improvements to trust property and administrative expenses, are borne by those with the remainder interest.¹⁰⁹

Nevertheless, “it is common practice today to exclude some or all of the rules governing appointment and allocation of outgoings in the trust instrument.”¹¹⁰ This is so for several reasons. First, “the rules may block trustees from making decisions that reflect tax considerations. [Second], the application of the rules often makes administration of the trust unjustifiably complicated.”¹¹¹ Therefore, the traditional formulation of the rule of this duty was modified by Hoffmann J in *Nestlé v National Westminster Bank plc*: “the trustee must act fairly in making investment decisions which may have different consequences for different classes of beneficiaries.”¹¹² This new formulation emphasizes fairness, the importance of discretion, and the width of competing considerations in any case.

(d) Duty to keep accounts and to provide information

Trustees must keep proper accounts of how they manage the trust property and must be ready to produce them for inspection and examination by the beneficiaries. A beneficiary has the right to require the accounts of the trust to be audited by any solicitor or accountant regardless of his suspicion of any improper administration.¹¹³ The trustee is allowed a reasonable time to assemble the accounts according to the beneficiary’s request. If a trustee causes expense due to

¹⁰⁹ Oosterhoff, *supra* note 31 at 1097.

¹¹⁰ *Ibid* at 1080-81.

¹¹¹ *Ibid*.

¹¹² *Nestlé v National Westminster Bank plc*, [1992] OPLR 85 at 92.

¹¹³ *Trustee Act 1925*, *supra* note 26, s 22(4); *Public Trustee Act 1906* (UK), 1906, c 55, s 13(5). (If audits are carried out more than once in every three years, the beneficiary will be ordered personally to pay the costs).

neglect or refusal to furnish accounts, he must bear the expense personally.

In addition, trustees must regularly give beneficiaries accurate and full information and explanations of the state of the trust. They must also make trust documents available for inspection by the beneficiaries. However, no beneficiary has the right to disclosure of anything that can be described as a trust document, in particular when there are issues as to personal or commercial confidentiality. Derived in part from a *dictum* of Lord Wrenbury in *O'Rourke v Darbishire*¹¹⁴, the basis upon which the beneficiaries are entitled to information and to inspect trust documents used to be that they are the actual owners of the trust property and therefore the documents belong to them. However, this proprietary theory has been disputed by modern cases as the basis for access to information, in particular in the case of instruments containing discretionary trusts or powers of appointment, where the beneficiaries have no property interest in the trust. As stated in *Schmidt v Rosewood Trust Ltd*, a beneficiary's right to seek disclosure of trust documents, although sometimes not inappropriately described as a proprietary right, is best approached as one aspect of the court's inherent jurisdiction to supervise (and where appropriate intervene in) the administration of trusts.¹¹⁵

As analyzed in this section, the legal ownership of trust property grants a trustee the legal title to trust property, which is mainly divided into administrative powers and dispositive powers. However, since the trustee holds the trust property for the benefit of beneficiaries or special purposes, he owes obligations to the beneficiaries. The obligation that lies at the base of trusteeship has resulted in there being fundamental duties applicable to all trustees. In addition to

¹¹⁴ *O'Rourke v Darbishire*, [1920] A.C. 581 (H.L.) at 626-27 [A.C.].

¹¹⁵ *Schmidt v Rosewood Trust Ltd*, [2003] 3 All ER 76 at 76.

the basic fiduciary duties that require him to act in good faith and avoid conflicts of interests, the trustee has other duties. For instance, duties to collect the assets for the trust and ensure their safety upon the appointment of the trustee, and the duty to invest trust funds, exercise reasonable care, provide information, and the duty of impartiality during the existence of the trust. The trustees have all the powers that the legal title confers vis-à-vis the outside world; whereas, only inside the trust are his powers limited to what is authorized by the trust terms, the court or the beneficiaries.¹¹⁶ Therefore, corresponding to the trustee's equitable obligations, an important issue to study at this point, is how to describe the beneficiaries' interests, i.e. how to understand the equitable ownership of the trust property.

4. The Equitable Title to Trust Property

While beneficiaries are granted equitable title by the nature of the trust in the common law, they nonetheless depend on the trust's terms in order to access either its capital, or the interest it generates. This is also true if the beneficiary wishes to access both the trust's capital and the interest the trust generates. They have this right regardless as to whether the income is immediate or deferred. This section first analyzes the nature of the beneficiary's right, namely whether it is a real right or only a personal claim. Following this, it will then indicate the specific rights of the beneficiary that are granted by his equitable title, which will provide a better understanding of the nature of a beneficiary's rights.

¹¹⁶ Rebecca Lee, "Convergence and Divergence in the Worlds of the Trust: Duties and Liabilities of Trustees under the Chinese Trust" in Lionel Smith, ed, *The Worlds of the Trust* (Cambridge: Cambridge University Press, 2010) 406 at 418.

A. The Nature of a Beneficiary's Rights

A significant issue regarding equitable title is the nature of the beneficiary's right. There has been some controversy over it. The majority opinion is held by Sir Frederick Maitland – English legal historian of the late 19th century. He believed that the right of the trust beneficiary is merely a personal right with *in rem* connections. Opposite this, Professor Austin Scott proposed that the beneficiaries have a direct proprietary interest in the trust property.¹¹⁷

It has often been said that legal ownership is a right *in rem* whilst equitable ownership is a right *in personam* because it is given only against persons and not things. The beneficiary's right is a personal claim, a right *in personam*, against the trustee in the event that the trustee should commit a breach of the trust.¹¹⁸ In such a circumstance, the trustee is obliged to effect a specific restitution of the property from the trust or to pay equitable compensation to the beneficiaries. Similarly, any third party who has knowingly received that property in breach of the trust,¹¹⁹ or who has acted as a dishonest assistant to the breach of the trust,¹²⁰ will bear personal obligations to account to the beneficiaries for any loss suffered by the trust.¹²¹

Unlike legal rights that prevail against persons generally, equitable rights only prevail against a limited group of persons.¹²² As Professor Smith states: “the beneficiary's interest never

¹¹⁷ D.W.M. Waters, “The Institution of the Trust in Civil and Common Law” (1995) 252 *Recueil de Cours* 113 at 351-52.

¹¹⁸ Oosterhoff, *supra* note 31 at 37.

¹¹⁹ See *Re Montagu*, [1987] Ch 264.

¹²⁰ See *Royal Brunei Airlines v Tan*, [1995] 2 AC 378; *Twinsectra Ltd v Yardley*, [2002] UKHL 12, [2002] 2 AC 164; *Dubai Aluminium v Salaam*, [2002] 3 WLR 1913.

¹²¹ Thomas & Hudson, *supra* note 88 at 26.

¹²² See Hayton, Matthews & Mitchell, *supra* note 7 at 76-77. In England, a limited group of persons was originally comprised persons who were not *bona fide* and now includes persons who were not able to take advantage of special protective provisions in the 1925 property legislation.

binds third parties except those whose rights derive from the rights of the trustee; this shows that the beneficiary's interest binds the *trustee's rights* in the trust property, not the trust property itself.”¹²³

Moreover, the beneficiary's right is considered a personal claim because its realization relies on another person's performance, i.e. the trustees' management of the assets. The beneficiary's right is “an indirect interest in the nature of an encumbrance on the trustee's rights in the trust property”.¹²⁴ Where a third party owns a common law obligation in relation to the trust property, it is the trustee who enforces it as a legal owner. “The beneficiary has no right in his own capacity to bring a common law action against the third party directly.”¹²⁵ Therefore, he has no full proprietary interest until the trustee's discretion is exercised in his favour. The beneficiary only has an expectation that the trustees will perform their duty to manage the assets and distribute income in favour of the beneficiary.

Although the execution of beneficiary's rights is based on the trustee's administration and disposal over the trust property, the beneficiary does not act simply like a personal creditor of the trustee for a few reasons. First, the fate of beneficiary's rights is tied up with the fate of the trust property. A beneficiary's rights will only be effective as long as the trust property exists. As Penner argues, “if the trust property is stolen or lost and cannot be recovered, or is destroyed, then the trust essentially evaporates, because there is no property to which the beneficiary's rights under a trust can attach ... Thus, if the property disappears, then so does the trust, and so

¹²³ Smith, “Scottish Trusts in the Common Law”, *supra* note 13 at 288.

¹²⁴ *Ibid* at 293.

¹²⁵ Gary Watt, *Todd & Watt's Cases & Materials on Equity and Trusts* (New York: Oxford University Press Inc., 2011) at 10.

does the beneficiary's right."¹²⁶ In this respect, the beneficiary's rights are different from those of a creditor. Moreover, the beneficiary's rights are capable of binding certain third parties except for 'equity's darling', who has an unanswerable defense, i.e. the *bona fide* purchaser for value of the trust property without actual or constructive notice of the equity. In other words, the beneficiary can exercise equitable proprietary remedies against certain third parties as the transferees of the trust property and trace the property so as to have the property or its product restored as an accrual to the trust fund.¹²⁷ When a trustee administers the trust property in breach of trust purposes, the trustee is personally accountable to the beneficiary. As Lord Collins SCJ observed in *Robert v Gill & Co*¹²⁸: in this case, the beneficiary has no personal right to sue a third party, and is suing on behalf of the estate or more accurately, the trustee. But when the trustee unreasonably refuses to, or fails to sue the third party, the beneficiary can proceed to trace the property and recover it from the third parties who are not equity's darling. Nevertheless, it is worth noting that a beneficiary's trace may only have the recovered property added back to the trust fund but not to the beneficiary's personal assets when it is a bare trust.

In short, the nature of the beneficiary's rights can be concluded as a personal claim against the trustee. While concerning the external relationship against certain third parties, the beneficiary's right involves an indirect interest in the trust property. The case of equity's darling is treated as a justifiable exception to the general *nemo dat* principle that protects security of title.¹²⁹

¹²⁶ Penner, *supra* note 3 at 28.

¹²⁷ Hayton, Matthews & Mitchell, *supra* note 7 at 77.

¹²⁸ *Robert v Gill & Co*, [2010] UKSC 22, [2010] 2 WLR 1227 at para 62.

¹²⁹ Penner, *supra* note 3 at 39.

B. The Beneficiary's Specific Rights

After examining the nature of the beneficiary's equitable title, this section indicates the major specific rights of the beneficiary that are granted by the equitable title: right to compel due administration, to bring a derivative action on behalf of the trust when the trust is not properly administered, and rights to terminate the trust.

(1) A beneficiary's right to compel due administration

In general, a beneficiary has no right to interfere in the administration of a trust, but has to wait passively to receive benefits to which he is entitled when the trusts are properly administered. However, when the trust is not properly administered, the beneficiary can take steps to compel its proper administration. As part of the right to compel due administration, a beneficiary is entitled to enforce claims, i.e. to apply to the court if the trustee fails to take any action necessary to preserve the trust assets.¹³⁰ If the improper administration is caused by a third person, the court may either direct the trustees to enforce that claim or allow the beneficiary to sue the third party directly for the benefit of the trust in the name of the trustees or to directly sue the trustees.¹³¹

The beneficiary can either issue an application to the court for the determination of a specific question or questions or issue proceedings for the general administration of the trust. The first method is preferable since it is the cheaper, quicker and simpler method in comparison with the second. However, when the administration of the trust involves third parties, or in any

¹³⁰ *Fletcher v Fletcher* (1844) 4 Hare 67.

¹³¹ A.J. Oakley, *Parker and Mellows: The Modern Law of Trusts*, 9th ed (London: Sweet & Maxwell, 2008) at 818.

action against trustees for breach of trust where the facts are in dispute, it is not appropriate for the beneficiaries to make an application to the court in this way.¹³² A beneficiary may employ the first method in the following circumstances: (a) applying to a court to approve a specific transaction that is for the interests of the beneficiaries as a whole but in the absence of general law and trust instrument;¹³³ (b) applying to a court to direct the trustees to do a particular act which they ought to do or to refrain from doing a particular act that they ought not to do;¹³⁴ (c) applying to a court to direct payment of money in the hands of the trustees to the court;¹³⁵ (d) applying to a court to construe the provisions of the trust instrument or to ascertain the classes of beneficiaries;¹³⁶ and (e) applying to a court to determine any other specific question which arises in the course of the administration of a trust. With respect to the second method – issuing proceedings for the general administration of the trust, because it is intended to lead to the court itself becoming responsible for the entire administration, it is usually only necessary in three situations: (a) where there have been constant disputes between the trustees; (b) where the circumstances of the trust give rise to recurring difficulties which would require frequent single applications to the court; and (c) where clear *prima facie* doubts exist as to the *bona fides* of the trustees.¹³⁷

(2) A beneficiary's right to bring a derivative action on behalf of the trust

Derived from the right to compel due administration, another right of the beneficiary is

¹³² *Ibid* at 817.

¹³³ *Phipps v Boardman*, [1967] 2 A.C. 46.

¹³⁴ *Syffolk v Lawrence* (1884) 32 W.R. 899.

¹³⁵ *Trustee Act 1925*, *supra* note 26, s 63.

¹³⁶ *Syffolk*, *supra* note 134 at para 14-122.

¹³⁷ *Oakley*, *supra* note 131 at 817-18.

the right to bring a derivative action on behalf of the trust. According to the general rule, a beneficiary can only sue his trustee or a person who is constructively treated as a trustee, but has no cause of action against a third party who commits a wrong act in respect of trust property or assists the trustee in breach of the trust. It is the trustee who has a cause of action and can bring proceedings on behalf of the trust against such a third party.¹³⁸

However, there are circumstances where it is appropriate to permit a beneficiary to bring an action against a third party. Firstly, as an act of tort law, “where the beneficiary is in possession of trust property, and may bring an action for interference with it, not by virtue of his equitable property rights, but by virtue of his possession alone.”¹³⁹ Secondly, where the trust is a bare trust¹⁴⁰, the beneficiary has the right, upon giving a proper indemnity, to require the trustee to lend his name to the action to vindicate the legal right.¹⁴¹ The beneficiary can also bring an action for the benefit of the trust under complex trusts and bare trusts where compelling the trustee to lend his name would have proved useless, for instance, when the trustee is disabled from suing or it is either difficult or inconvenient for him to sue. This was known as a derivative action. On the other hand, it is worth noting that the beneficiary cannot be in a better position than the trustee since they sue to enforce duties owed to the trustee.¹⁴²

(3) A beneficiary’s right to terminate the trust

Another right of the beneficiaries is the right to terminate the trust. A sole beneficiary

¹³⁸ Hayton, Matthews & Mitchell, *supra* note 7 at 970.

¹³⁹ *Ibid.*

¹⁴⁰ A bare trust, also called a simple trust, means a trust in which the settlor gives no active duties to the trustee; the trustee’s duty is merely to follow the instructions of the beneficiary.

¹⁴¹ *Foley v Burnell* (1793) 1 Bro CC 274.

¹⁴² *Hayim v Citibank NA*, [1987] AC 730.

who is *sui juris* (of the age of majority, and with full capacity) or beneficiaries who are all *sui juris* and all in agreement, can terminate trusts without reference to the wishes of the trustees or the settlor. This is known as the Rule in *Saunders v Vautier*.¹⁴³ The rationale of this Rule deems that the settlors make an outright gift of property to the beneficiaries upon the creation of the trust. Therefore, the settlor loses control over the property, and his provisions expressed in the trust instrument will not prevent the beneficiaries from bringing the trust to an end.¹⁴⁴ Although doubts arose that “beneficiaries had not become ‘absolutely’ entitled to the trust property when the property remained subject to a special power of appointment vested in trustees because the beneficiaries’ interests were defeasible”,¹⁴⁵ Lord Walker stated in *Schmidt* that a mere power of appointment had the negative ability to block the application of the Rule.¹⁴⁶ When it is not absolutely certain that no more beneficiaries can come into existence, the court may give leave to the trustees to distribute the trust property according to the directions of the existing beneficiaries.¹⁴⁷

According to the Rule in *Saunders v Vautier*, the beneficiaries are entitled to wind up the trust and to require the trustee to assign to them the subject matter of the trust in numerous situations: “(a) The beneficiaries of the trust can break it before they have all fulfilled a contingency provided that they are all *sui juris*; (b) Beneficiaries who are entitled by way of succession can also break the trust; and (c) The beneficiaries of a discretionary trust can also break the trust. Whenever the trust is terminated under the Rule, the beneficiary has the right to

¹⁴³ *Saunders v Vautier* (1841) 4 Beav. 115, 49 E.R. 282 (Rolls Ct.); affirmed (1841), 1 Cr. & Ph. 240, 41 E.R. 482 (Ch. Div.).

¹⁴⁴ Oakley, *supra* note 131 at 818-19.

¹⁴⁵ Hayton, Matthews & Mitchell, *supra* note 7 at 961.

¹⁴⁶ *Schmidt*, *supra* note 115.

¹⁴⁷ *Re White v Edmond*, [1901] Ch 570.

compel the trustee to convey the property to whoever they direct.”¹⁴⁸ Nevertheless, it is noted that the beneficiaries cannot terminate the trust as of right where there are legacies contingently charged on the trust fund.¹⁴⁹ Moreover, as Lightman J. held in *Don King Productions Inc. v Warren*¹⁵⁰, the trust cannot be terminated when the trustee has outstanding obligations under a contract which is held as a trustee and has no power to transfer the trust asset to the beneficiary or to his order.

With regards to the application of the right to terminate trusts, a question arises as to whether it is necessary to have an ascertained group of beneficiaries as a collective to terminate the trust. This would be true if the identity of all of the beneficiaries can be ascertained, i.e. if the *Broadway Cottages*¹⁵¹ test applies which requires the trustees to draw up a complete list of all the beneficiaries. However, there are situations where the identity of all the beneficiaries cannot be ascertained. As the House of Lords held in *McPhail v Doulton*¹⁵², the *Broadway Cottages* test was not appropriate, at least for discretionary trusts. “Instead, the majority affirmed that for discretionary trusts it was sufficient if the beneficial class was conceptually certain in the sense that it was possible for the trustees to say for any given individual that he or she either was or was not a member of the class.”¹⁵³ In fact, it is hard to list all the beneficiaries under discretionary trusts since the discretionary trust might be created for a large beneficial class, such

¹⁴⁸ Oakley, *supra* note 131 at 820.

¹⁴⁹ *Weatherall v Thornburgh* (1878) 8 Ch D 261, CA.

¹⁵⁰ *Don King Productions Inc. v Warren*, [2000] Ch. 291 at 321.

¹⁵¹ *Inland Revenue Commissioners v Broadway Cottages Trust*, [1995] Ch 20.

¹⁵² *McPhail v Doulton*, [1971] AC 424.

¹⁵³ Thomas Glyn Watkin, “Changing Concepts of Ownership in English Law During the Nineteenth and Twentieth Centuries: The Changing Idea of Beneficial Ownership Under the English Trust” in Martin Dixon & Gerwyn LL H Griffiths, eds, *Contemporary Perspectives on Property, Equity and Trusts Law* (New York: Oxford University Press Inc., 2007) 139 at 153.

as employees and ex-employees of a large, multi-national corporation. Likewise, it will in reality be impossible to claim that all the beneficiaries have agreed to terminate the trust. Therefore, the identity of all the beneficiaries is not required under discretionary trusts and thus allowing the existing trustees to terminate the trust.

It has been the purpose of this chapter to introduce the common law trust and its dual ownership, in particular focusing on the development or refurbishing of the concept of trust and dual ownership, and as a result to indicate the possibilities of introducing the trust into civilian jurisdictions. Concluding from all the above analyses in this chapter, dual ownership is simply a concept used as a result of the legal traditions of common law and equity. It does not require a strict duality of ownership under the trust and therefore does not prevent the trust from being introduced into civilian jurisdictions where ownership is absolute and indivisible. In fact, the legal history of England and those of its nearest European neighbours were not as different at this time as many have believed.¹⁵⁴

¹⁵⁴ *Ibid* at 158-59.

II THE INTRODUCTION OF TRUSTS INTO CIVIL LAW AND ITS OWNERSHIP OF TRUST PROPERTY

The trust in common law has been developed. It has more functions and is broadly used for tax purposes and commercial business. Precisely because of the value of the trust in commerce, a number of civilian jurisdictions have introduced the trust into their property systems. This chapter indicates the introduction of the trust into civilian jurisdictions, both mixed jurisdictions and pure civil law systems. It analyses the different ways adopted by these jurisdictions to transplant dual ownership of trust property under common law into their civilian property systems where ownership is absolute. This thesis argues that although the trust is considered a product of equity, it is possible and necessary to introduce the trust into civilian jurisdictions, in particular with the development of international finance and investment. The successful experiences of legislation and practice of those jurisdictions shed light on the amendments to the Chinese law of trust, especially with regards to the regulation of ownership of trust property.

1. Difficulties and Necessity of the Introduction of Trusts into Civil Law

Before delving into specific analyses of the introduction of trusts and its ownership of trust property in different jurisdictions, it is worth noting the difficulties of the introduction of trusts in general, and discussing the necessity and significance of doing so.

A. Difficulties with the Introduction of Trusts into Civil Law

Although the trust has been successfully introduced into a number of pure civil law

systems and mixed jurisdictions, there was a debate of over 100 years between civil and common law lawyers with respect to the difficulties or the possibility of civil law systems adopting the trust.¹⁵⁵ One opinion proposed in the long-past debate was that the trust cannot be introduced in civil law because splitting ownership is prohibited by the civilian jurisdictions. In other words, the trust “make those accustomed to Civilian property systems uncomfortable, given that they seem to rely on the peculiar Common Law separation of legal and equitable ownership.”¹⁵⁶

Ownership is both perpetual and exclusive under the civil law. According to article 544 of the French Civil Code (1804)¹⁵⁷, which is considered the most well-known model for a civil law system in modern times, ownership includes a complete power of three types of rights over the thing: *usus* – the right to use the thing, *fructus* – the right to take its fruits, and *abusus* – the right to destroy or alienate it.¹⁵⁸ All these rights should belong to a single person or group of persons in relation to any particular thing. “Only one person or group of persons could be the owner of an item of property at any one time.”¹⁵⁹ Therefore, the common law fragmentation or dismemberment of property into different estates or interests of different values, each belonging to a different person, finds no place in civil law systems.¹⁶⁰ As Pascal argued: because of its juridical structure – a division of legal and equitable titles, the trust does not fit into the

¹⁵⁵ Waters, “The Institution of the Trust”, *supra* note 117 at 341.

¹⁵⁶ James Chalmers, “Ownership of Trust Property in Scotland and Louisiana” in Vernon Valentine Palmer & Elspeth Christie Reid, eds, *Mixed Jurisdictions Compared: Private Law in Louisiana and Scotland* (Edinburgh: Edinburgh University Press, 2009) 132 at 132.

¹⁵⁷ *Code Napoléon* (1804).

¹⁵⁸ Paul Matthews, “The Compatibility of the Trust with the Civil Law Notion of Property” in Lionel Smith, ed, *The Worlds of the Trust* (Cambridge: Cambridge University Press, 2013) 313 at 319.

¹⁵⁹ T.G. Watkin, *An Historical Introduction to Modern Civil Law* (Aldershot: Ashgate, 1999) at 225.

¹⁶⁰ Matthews, “The Compatibility of the Trust”, *supra* note 158 at 320, n 32: Though see the second sentence of article 947 of the C.C.Q.: ‘Ownership may be in various modes and dismemberments.’ This refers on to the two modes of co-ownership and superficies (arts. 1009-1118), and the four dismemberments of usufruct, use, servitude and emphyteusis (arts. 1119-1211).

symmetry of a civil legal system.¹⁶¹ There was no room for dividing the legal and equitable ownership in property and it would have been a violation of the *ordre publique* to recognize the validity of a trust.¹⁶² Therefore, resistance was made at first to the introduction of the trust in civilian jurisdictions due to the acute awareness of the difficulties. As Professor Cantin Cumyn said: “Even if civil law countries that are interested in the trust do not intend to reproduce all its facets and ramifications, it is clear that its ubiquity is a cause of confusion for jurists who are not ‘common lawyers’”.¹⁶³

Another difficulty faced by the civil law system might lie in the effect of civilian jurisdictions of the *numerus clausus*. As opined by Professor Fratcher, this can be the greatest doctrinal barrier to the civilian reception of the common law trust. The *numerus clausus* is a basic principle in civil law jurisdictions. It is to the effect that the law knows only a definitive list of real rights. “The list of such rights and interests cannot be expanded beyond that closed list which appears in the Code, and therefore there can be no registration of interests in land or other property which do not conform or find themselves within the *numerus clausus* (the closed list of *in rem* rights).”¹⁶⁴ The principle of *numerus clausus* is uniformly accepted in a number of civil code systems based on Roman law, such as the French Civil Code (1804), the Austrian Code of 1811, the German Civil Code of 1901, and the Swiss Code of 1907. It is obvious that the fact of trustees and beneficiaries each having an interest would not fit into a *numerus clausus* based on ownership of property and rights over the property of another. As a result, the principle of

¹⁶¹ R A Pascal, “Some ABC’s about trusts and us” (1952-1953) 13 La LR 555 at 557.

¹⁶² *Ibid.*

¹⁶³ Medeleine Cantin Cumyn, “Reflections regarding the diversity of ways in which the trust has been received or adapted in civil law countries” in Lionel Smith, ed, *Re-imagining the Trust: Trusts in Civil Law* (Cambridge: Cambridge University Press, 2012) 6 at 10-11.

¹⁶⁴ Waters, “The Institution of the Trust”, *supra* note 117 at 344.

numerus clausus made it unclear for two centuries how the civil law courts should classify and deal with the position of the trustee and the beneficiary when they were confronted conflicts of trusts from foreign common law countries.¹⁶⁵

On the other hand, if a civilian jurisdiction decided to create a trust institution by legislation, then the *numerus clausus* principle would not present serious difficulties. The real problem is that it is hard to accept that one person controls assets which are not intended for that person's sole benefit or in some cases not for that person's benefit at all.¹⁶⁶ A notion which is deeply ingrained in the civil law system, is that since an owner must have absolute ownership, "there is an easy acceptance – or at least an enhanced tolerance – of the idea that a person who is the titleholder ('*titulaire*') of a thing must be able to deal with it as he or she wishes, and therefore for his or her own benefit."¹⁶⁷ As a result, an argument has arisen that the trust constitutes a restraint on alienation and is hard to be introduced into civil law. This argument of the difficulty of the introduction of trusts "is a debating point centered more in conceptual thinking and expression than anything else".¹⁶⁸

Lastly, it is difficult to introduce the trust into a civilian jurisdiction because of the traditional notion of patrimony in civil law. The notion of patrimony is a very old idea which is traceable back to Roman law. In *Private Law Dictionary and Bilingual Lexicons*, a patrimony has been defined as "the whole of the rights and obligations of a person having economic or

¹⁶⁵ *Ibid.*

¹⁶⁶ Matthews, "The Compatibility of the Trust", *supra* note 158 at 322.

¹⁶⁷ *Ibid.*

¹⁶⁸ Waters, "The Institution of the Trust", *supra* note 117 at 343.

pecuniary value”.¹⁶⁹ Since technically it must contain both assets and liabilities, the patrimony is also understood as “the totality of a person’s assets, and, in its broader sense, his liabilities also”.¹⁷⁰ A patrimony is, in a sense, a container. It may be empty, as in the case of the patrimony of a newborn baby.¹⁷¹ According to the classic French nineteenth century theory of Aubry and Rau, one person must correspond to one patrimony. Namely, the general rule of the patrimony is that a person can have one and only one patrimony.¹⁷² Therefore, the dual ownership of the common law finds no place in the civil law in relation to this notion.¹⁷³

B. Necessity and Significance of the Introduction of Trusts into Civil Law

The concern of those difficulties raises the question of what are the merits of the trust for civilian jurisdictions, namely whether it is necessary to introduce the trust into the civilian property system. In particular, in situations where it seems that most of what is done by way of trusts could be done by way of contracts instead. Indeed, Lord President Inglis once asserted in the Scottish court that “a trust is a contract made up of the two nominate contracts of deposit and mandate”.¹⁷⁴ However, it is worth noting that this explanation is inadequate when we notice that property held in trust cannot be seized by the personal creditors of the trustees¹⁷⁵; where a trustee,

¹⁶⁹ Smith, “Trust and Patrimony”, *supra* note 2 at 335, n 9; Quebec Research Centre of Private and Comparative Law, *Private Law Dictionary and Bilingual Lexicons* (Cowansville: LesÉditions Yvon Blais, 1991), s.v. “patrimony”.

¹⁷⁰ George L. Gretton, “Trusts Without Equity” (2000) 49 *International and Comparative Law Quarterly* 599 at 608.

¹⁷¹ Smith, “Trust and Patrimony”, *supra* note 2 at 335.

¹⁷² C. Aubry & F.C. Rau, *Cours de droit civil français d’après la méthode de Zachariae*, 4th ed (Paris: Marchal et Billard, 1873), vol. 6, bk. 2, div. 1, para 573. See the English translation by N. Kasirer, ‘Translating Part of France’s Legal Heritage: Aubry and Rau on the Patrimoine’ (2008) 38 *R.G.D.* 453.

¹⁷³ However, the traditional notion of patrimony has been developed and the theory of special patrimony has been accepted in civil law, which allows the introduction of trusts in civilian jurisdictions. This will be discussed in the following section, “2. Possibility of the Introduction of Trusts into Civil Law”.

¹⁷⁴ *Croskery v Gilmour’s Trs* (1890) 17 *R* 697 at 700.

¹⁷⁵ *Heritable Reversionary Co. Ltd v Millar*, [1892] *A.C.* 598 at 600.

the owner of trust property, becomes bankrupt, the trust property is not available to his creditors.¹⁷⁶ In other words, one thing that makes a trust distinct from a contract is that the trust can offer protection against creditors while the contract cannot. Therefore, as a result of this significant advantage over contractual arrangements, and of other merits of the trust, such as its flexibility and its value in commerce, despite the difficulties, it is necessary to introduce the trust into civilian jurisdictions.

Not only is the trust a necessary tool for civilian countries to attract international investment and financial business, but the trust also serves as a versatile legal device that has played a significant role in the international market. Its use for commercial purposes can be exercised in various forms, including investment vehicles, pensions trusts, securitization trusts and many others.¹⁷⁷ In recent years, there has been increasing competition among jurisdictions to attract investment and trust business on an international basis.¹⁷⁸ The increasing importance of cross-border transactions indicates that it has been significant to incept the trust into civilian jurisdictions and create legal institutions having even more of the characteristics of the trust. Indeed, the laws of trusts have been gradually liberalized over time to allow for a wider use of the trust.

2. Possibility of the Introduction of Trusts into Civil Law

After examining the difficulties and necessity of the introduction of trusts into civilian jurisdictions, now the question becomes whether it is possible in practice to introduce the trust

¹⁷⁶ *Sharp v Thomson* 1995 SC 455 at 479 per the Lord Presitdent (Hope).

¹⁷⁷ *Discussion Paper on Supplementary and Miscellaneous Issues relating to Trust Law*, Scottish Law Commission DP 148 (2011) at para 1.5.

¹⁷⁸ *Ibid* at para 1.3.

into civil law. If yes, how has the trust been incepted into civil codes and how has common law dual ownership been transplanted into the civilian property system where ownership is absolute. This paper opines that although distinctions between common law ownership and civil law ownership exist, it is possible to introduce the trust into the civil law; its evidence can be found both in theory and in practice.

A. Possibility of the Introduction of Trusts from a Theoretical Perspective and the Notion of Special Patrimony

(1) The possibility of the introduction of trusts from a theoretical perspective

From a purely theoretical perspective, identical characteristics of ownership are not required. The language, i.e. the concept of dual ownership or equitable remedies, does not matter.¹⁷⁹ It is generally accepted that as long as its effects are relatively similar in practice to those of the common law trust, a civilian “jurisdiction’s designation of a particular institution as a trust does not necessarily mean that this institution is identical or similar to the common law trust”¹⁸⁰. For instance, “the duties ascribed to trustees in Anglo-American and civilian systems are in fact remarkably similar ... [Thus], there is no need to postulate a special remedy confined to breaches of ‘equitable duties.’”¹⁸¹ In order to adapt trust law to a civilian system, the real question that needs to be asked is: which aspects of English trust law relating to property and obligations are essential to a trust. Tony Honoré believes that “[a] trust always involves a split

¹⁷⁹ More detailed analyses of the possibility of the introduction of trusts into civilian jurisdiction will be discussed in chapter IV, subsection 1, “Possibilities to Distill the Trust and Its Dual Ownership into China”.

¹⁸⁰ Guy Fortin, “How the Province of Quebec Absorbs the Concept of the Trust” (1999) 18 *Estates, Trusts & Pensions Journal* 285 at 286.

¹⁸¹ Tony Honoré, “Trusts: The Inessentials” in Joshua Getzler & Edward Hector Burn, eds, *Rationalizing Property, Equity, and Trusts: Essays in Honour of Edward Burn* (London: LexisNexis UK, 2003) 1 at 17.

between management/administration and benefit/enjoyment”.¹⁸² The idea of separate funds and a split between administration and enjoyment is not confined to common law systems. It has also been admitted by other legal systems, for example, “the *peculium* of Roman law, the *patrimoine d’affectation* of French law, [and] the *Sondervermögen* of German law”.¹⁸³

(2) The notion of special patrimony

Taking the patrimony theory as a specific instance, the difficulty in introducing the trust due to the traditional notion of patrimony has no longer been a problem. Qualifications to the traditional rule have been admitted and the notion of special patrimony, which plays the same role as dual ownership, has been proposed by the civilian tradition. It proves that as long as the effects of the legal instruments in common law and civil law are relatively similar, their distinctive concepts or languages do not matter.

The theory of special patrimony, i.e. that a person could sometimes have a special patrimony, was usefully applied to the trust by the French comparatist Pierre Lepaulle in his *Traité Théorique et Pratique des Trusts* in 1932. He stated that although patrimony was unknown to the common law, the trust could nonetheless be explained as a special patrimony, a *patrimoine d’affectation*.¹⁸⁴ This idea has particular importance in relation to the rights of creditors and the rights of heirs. “When civil lawyers are trying to understand why it is that the beneficiaries can make claims against third parties for the return of trust assets, or that personal

¹⁸² Honoré, “Trusts: The Inessentials”, *supra* note 181 at 11.

¹⁸³ Tony Honoré, “Obstacles to the Reception of Trust Law? The Example of South Africa and Scotland” in Alfredo Mordechai Rabello, ed, *Aequitas and Equity: Equity in Civil Law and Mixed Jurisdictions* (Jerusalem: The Harry and Michael Sacher Institute for Legislative Research and Comparative Law, The Hebrew University of Jerusalem, 1997) 793 at 812.

¹⁸⁴ Gretton, “Trusts Without Equity”, *supra* note 170 at 610, n 61.

creditors of the trustee cannot seize trust assets in satisfaction of their claims, they often see an analogy with the patrimony idea.”¹⁸⁵

Some systems have used the concept of special patrimony to describe the trust. One version of LePauille’s concept has been adopted in Quebec law, interpreted as patrimony by appropriation; another version has been adopted in Scots law, interpreted as multiple patrimonies. Under the Scottish notion of special patrimony, the trustee may have segregated patrimonies of assets and liabilities: his own general or private patrimony and a special patrimony dedicated to a special purpose of trust at the same time. Likewise, one patrimony may belong to more than one person, these are called joint trustees. The private patrimony is the aggregate of the trustee’s legal rights and liabilities, including the property he owns. Upon the insolvency of the trustee, all the property in his private patrimony is *prima facie* vulnerable to the claims of his personal creditors. On the contrary, a trust patrimony consists of the trust property owned by the trustee or joint trustees as a whole and any obligations he or they incurred in the property administration of the trust. Although owned by the same person, the civilian tradition accepted that the assets and liabilities of a special patrimony, which is viewed as the trust, are separated from a general patrimony. “The two patrimonies are distinct in law, and should also be kept distinct in practice, by proper labeling and accounting.”¹⁸⁶

The special patrimony theory explains why the trust can continue when all trustees are dead or become insolvent on the ground of the separate fund of the trust. In other words, any

¹⁸⁵ Matthews, “The Compatibility of the Trust”, *supra* note 158 at 324.

¹⁸⁶ Kenneth G C Reid, “Patrimony Not Equity: the Trust in Scotland” (2000) 8 *European Review of Private Law* 427 at 432.

sales or exchanges of the trust property are allocated to the trust patrimony, without affecting the trustee's personal assets, and vice versa. Therefore, the bankruptcy of the trustee's private patrimony cannot cause the termination of the trust.

In addition, the notion of special patrimony also explains why the trust property is immune from the claims of the trustee's personal creditors. That is because a trustee, the holder and manager of the trust property, has two separated patrimonies, his private patrimony and the trust patrimony, and each patrimony has its own creditors. As explained by Professor Reid: "[a] private creditor must claim from the private patrimony and a trust creditor from the trust patrimony. If that patrimony is empty, he must go without, for the other patrimony is not available."¹⁸⁷ In other words, the rights of beneficiaries are rights against trustees, enforceable against the special patrimony. Whereas, personal rights enforceable against the trustee in his personal capacity are not enforceable against the special patrimony. This explains why the beneficiary's right prevails over the claims of the trustee's personal creditors. It is simply because these two claims fall into different patrimonies and the trustee's personal creditors are restricted to the property in the trustee's private patrimony. The reason shall not be explained because the beneficiary, as opposed to the trustee, is the real owner of the trust property.

Furthermore, the dual patrimony theory helps to understand why value received by the trustee automatically becomes part of the trust fund if the trust property is transferred in breach of the trust. This is because "when the trust property is transferred, the trustee is deemed to receive any proceeds into his trust – as opposed to private patrimony. This is also the case in

¹⁸⁷ *Ibid.*

respect of any profits that a trustee makes in breach of the principle that he must not act as *auctor in rem suam*.”¹⁸⁸ Therefore, without adopting dual ownership, the dual patrimony theory can provide a convincing explanation of the nature of the trust and a theoretical basis for the rules of trust law.

It is not hard to find that the notion of special patrimony, in particular the *patrimoine d'affectation* theory, has promoted the integration of trusts into civilian jurisdictions.¹⁸⁹ It shows that, from a theoretical perspective, it is possible for civil law countries to introduce the trust into their legal systems by adopting a legal instrument playing the same role as dual ownership, in spite of differences in concepts. The possibility of the introduction of trusts into civil law exists not only in theory but also in practice.

B. The Possibility of the Introduction of Trusts from a Practical Perspective

In practice, trusts and trust legislation can be found in a number of jurisdictions, including both mixed jurisdictions and pure civil law systems.¹⁹⁰ Dating back to the 17th century, the oldest mixed jurisdiction that adopted the term ‘trust’ was Scotland.¹⁹¹ In the 19th century, trusts gradually appeared in other mixed jurisdictions, such as South Africa, Quebec and Sri

¹⁸⁸ *Discussion Paper on the Nature and the Constitution of Trusts*, Scottish Law Commission DP 133 (2006) at para 2.19.

¹⁸⁹ Kenneth G C Reid, “Conceptualising the Chinese Trust: Some Thoughts from Europe” in Remco van Rhee & Lei Chen, eds, *Towards a Chinese Civil Code: Historical and Comparative Perspectives* (Danvers: Martinus Nijhoff Publishers, 2012) 209 at 226.

¹⁹⁰ Smith, “Trust and Patrimony”, *supra* note 2 at 333.

¹⁹¹ George L. Gretton, “Trusts” in Kenneth Reid & Reinhard Zimmermann, eds, *A History of Private Law in Scotland* (Oxford: Oxford University Press, 2000) 480 at 482. It is noted that “the term ‘trust’ first appears in the seventeenth century does not mean that trusts first appeared in the seventeenth century. They might have existed earlier, without the name.”

Lanka. Louisiana followed the introduction of trusts in the 1920s and 1930s.¹⁹² At that time, the trust was also incorporated in several civil law countries, starting with Latin American countries; for instance, Columbia (1923), Panama (1925), Chile (1925), Mexico (1926), Bolivia (1928), Peru (1931), Costa Rica (1936), Venezuela (1940), Nicaragua (1940), Guatemala (1946), Ecuador (1948) and Honduras (1950).¹⁹³ In Asia, the trust was first transplanted into Japan in 1922. Afterwards, it was introduced in South Korea in 1961, and much later, in Taiwan in 1996 and mainland China in 2001.¹⁹⁴ Some civilian jurisdictions that introduced the trust in the 19th century were typically part of a larger political entity whose legal tradition derived from the law of England, in particular in the cases of South Africa and Louisiana. The first uses of trusts in those jurisdictions were in the context of property transmission within a family under the framework of succession or marriage law.¹⁹⁵ Whereas, “[t]he attractiveness of the family or succession trust is sharply diminished in the countries of Continental Europe by the mandatory limits within which these jurisdictions confine acts transferring patrimonial rights by gratuitous title.”¹⁹⁶ Thus, compared with Southern American and Asian countries, European jurisdictions seem more prudent and even hostile towards integrating the trust. The trust was largely ignored in Continental Europe until the early 21st century, except for Liechtenstein, which adopted the trust in 1926. After a long period of controversy, Luxembourg introduced a fiduciary contract in 1983 and France enacted legislation in 2007 to create the *fiducie*, a trust or at least a trust-like

¹⁹² Reid, “Conceptualising the Chinese Trust”, *supra* note 189 at 210.

¹⁹³ *Ibid* at 210, n 4: For details, see Rodolfo Batiza, “The Evolution of the Fideicomiso (Trust) Concept under Mexican Law,” *Miami Law Quarterly* 11 (1956-7): 478 at 479. See also Nicolas Malumian, *Trusts in Latin America* (Oxford: Oxford University Press, 2009).

¹⁹⁴ Lusina Ho, “The Reception of Trust in Asia: Emerging Asian Principles of Trust?” (2004) *Singapore Journal of Legal Studies* 287 at 287.

¹⁹⁵ Cantin Cumyn, “Reflections”, *supra* note 163 at 11-12.

¹⁹⁶ *Ibid* at 14.

institution albeit one which is subject to a number of limitations.¹⁹⁷ The trusts that best draw the interest of European civilians are those that occur in the context of business relations.

The civilian jurisdictions, whether pure or mixed, were anxious to improve their opportunity to trade with or even compete with common law jurisdictions. Without a doubt, in the modern global economic market, there is incentive for both common law systems and civil law systems to remove impediments and promote trust business. Indeed, both the United Nations¹⁹⁸ and the Hague Conference on Private International Law¹⁹⁹ have attempted to introduce the trust to civilian jurisdictions. In 1984, the delegates of some twenty-six member countries of the Hague Conference met in their fifteenth session and discussed the fashioning of a Convention to recognize the trust. As a product of the conference, the implementation of the *Hague Convention on the Law Applicable to Trusts and on their Recognition*²⁰⁰ (hereinafter referred to as *Hague Trust Convention*) was published. It is of particular interest to legal comparatists since it attempts to explain the trust in a more or less system-neutral manner: “[t]he term ‘trust’ refers to the legal relationship created – inter vivos or on death – by a person, the settlor, when assets have been placed under the control of a trustee for the benefit of a

¹⁹⁷ Reid, “Conceptualising the Chinese Trust”, *supra* note 189 at 210, n 8: See e.g. Paul Matthews, “The French fiducie: and now for something completely different”, *Trust Law International* (2007): 17. As well as offering an insightful analysis the author has included his own translation of the legislation. For more recent developments, including legislative amendments, see Pierre Crocq, “National Report for France,” in *Towards an EU Directive on Protected Funds*, ed. S. C. J. J. Kortmann et al. (Deventer: Kluwer Legal Publishers, 2009), 99-104.

¹⁹⁸ See Unidroit, International Institute for the Unification of Private Law, UPL 1957, Paper XL, Trust – Document 1, “Report on Possible Uses of Certain Principles of the Trust in Civil Law Countries”; UPL 1958, Paper XL, Trust – Document 2, “Memorandum Concerning the Introduction of Some Principles of Trust into the ‘Civil Law Legislations’”.

¹⁹⁹ See *Choice of Law Rules for Trusts*, 1982-1984.

²⁰⁰ *Hague Convention on the Law Applicable to Trusts and on their Recognition*, 1 July 1985, (entered into force 1 January 1992).

beneficiary or for a specified purpose.”²⁰¹ The *Hague Trust Convention*, to some extent, encouraged the introduction of trusts, at least to states which were considering the Convention’s ratification.²⁰²

The legislation of trusts in civilian jurisdictions and the rules in international practice show that it is possible to introduce the trust into civil law. In particular, with the development of international trade and commerce, the trust has been introduced into civilian jurisdictions that have no history of an equitable jurisdiction. There is no doubt that although ownership is viewed as absolute and indivisible in civilian property systems, the ‘dual ownership’ of common law should not constitute an *a priori* obstacle to the implementation of trusts in other legal systems.

3. Introduction of Trusts into Civilian Jurisdictions in General

A number of civil law countries have introduced trusts into their legal systems. However, different jurisdictions have adopted different methods to introducing the trust and to interpreting dual ownership, based on their own legislation and legal traditions. This section briefly introduces the practices of several jurisdictions, both mixed systems and pure civilian systems. They can demonstrate the main measures in introducing trusts broadly adopted by civil law systems, either in an open or relatively prudent attitude. In the next two sections, the author will focus on the two most typical cases: Scottish trust law and Quebec trust law, including a more detailed comparative study of these systems.

²⁰¹ *Ibid*, art. 2.

²⁰² Reid, “Conceptualising the Chinese Trust”, *supra* note 189 at 211. Nevertheless, in Europe, there are only four civilian jurisdictions have chosen to ratify, which are Italy, Luxembourg, The Netherlands and Switzerland.

A. Introduction of Trusts into a Pure Civil Law Jurisdiction

As discussed in section 2, the concept of trust has been introduced into a number of pure civilian jurisdictions. Here the author takes the German civil law tradition and Latin civil law tradition as two examples to analyze how the trust has been incorporated into pure civilian jurisdictions.

(1) Introduction of trusts in the German civil law tradition

As one example of jurisdiction under German civil law tradition, Liechtenstein is a small principality and has been a tax haven for many years. Therefore, it adopts legislation that encourages foreigners to invest within the principality. It became the first jurisdiction in Continental Europe to invite the concept of the trust so as to attract financial business. “The motivation to introduce the trust into Liechtenstein law was, on the one hand, to make available as many legally operative forms as possible for the investment, administration and commercial utilisation of assets, and on the other hand, to deal explicitly and specifically with the fiduciary transactions already in existence in civil law.”²⁰³ In 1926, article 897-932 of the Law of Persons and Associations first provided the term of *Treuhanderschaft* that is modelled precisely upon the common law trust. The trust relationship is defined in article 897 by way of the function of participants. “According to this, the essence of the trust is the transfer of assets from the settlor to the trustee on the strength of a trust agreement, so that the trustee may hold, manage and apply these assets in his own name, in accordance with the agreement and in favour of the

²⁰³ Guido Meier & Oliver Schmidt, “Liechtenstein” in Alon Kaplan, ed, *Trusts in Prime Jurisdictions* (London: Globe Law and Business, 2010) 275 at 275.

beneficiaries.”²⁰⁴ And then in 1928, a second chapter was added to the Law of Persons and Associations in the form of article 932(a). This article introduced the concept of *Treuunternehmen*, that is strictly translated as a ‘trust enterprise’ – a form of incorporation that was modeled upon the Massachusetts business trust.²⁰⁵ In order to make the concept of trust compatible with the civil law environment, the Law of Persons and Associations avoids any reference to legal and equitable interests.

However, the Law of Persons and Associations did not regulate the rule against perpetuities and trusts can therefore be formed for an indefinite period.²⁰⁶ Moreover, it did not regulate the nature of a trustee’s ownership although it excludes the right of enjoyment from the trustee’s ownership. The Law of Persons and Associations simply stipulated in article 897 that the trustee is a person, firm or corporate entity to whom or to which assets of any kind have been transferred with the obligation to administer or use that trust property that is vested in the trustee’s own name as independent owner but for the benefit of another.²⁰⁷

Despite these problems, the Liechtenstein *Treuhanderschaft* is a relatively successful case study, in particular given the special nature of Liechtenstein as a tax heaven. It regulates the assignments of rights and obligations between the trustee and beneficiary. The trustee is entitled to preserve and administer the trust property with the care of a prudent businessman and is authorized to follow the instructions of the instrument upon the creation of the trust and reject

²⁰⁴ *Ibid* at 277.

²⁰⁵ Waters, “The Institution of the Trust”, *supra* note 117 at 379.

²⁰⁶ Dietmar Loretz, “Liechtenstein Trusts and Foundations: Creation and Operation” in Alon Kaplan, ed, *Trusts in Prime Jurisdictions* (London: Globe Law and Business, 2010) 301 at 301.

²⁰⁷ Waters, “The Institution of the Trust”, *supra* at 379-80.

any subsequent instructions received from either the creator or the beneficiary.²⁰⁸ The beneficiary, on the other hand, has a right to proceed against the trustee when the trustee wrongfully transfers the trust property and to draw benefits from the trust, “either at the present or in the future, whether as an actual holder and recipient of beneficial interest or simply as a reversioner.”²⁰⁹ The beneficiary is also entitled to claim against the third party if the third party had notice of the breach of the trust or paid no consideration for the transfer of the property. Article 912 of the Law on Persons and Companies recognizes the power to trace.²¹⁰ Additionally, the trust property is free from the claims of the personal creditors of the trustee. The notion of *Treuhanderschaft* has been widely used for many years and continues to be used extensively by foreign investors today.

In comparison to Liechtenstein, German law has been relatively prudent with its introduction of trusts. Germany did not transplant Anglo-American trust law immediately into its jurisdiction and it has no systematic regulation of the trust. As F. Weiser stated: “[t]he codified law of Germany knows nothing of Trusts.”²¹¹ The reason for this is that the rules of German civil law are flexible enough to solve the practical problems of trusts.²¹²

Nevertheless, a trust-like device does exist and courts have developed specific rules applicable to fiduciary relationships. The method of one person being able to administer property

²⁰⁸ Loretz, *supra* note 206 at 305-06.

²⁰⁹ Meier & Schmidt, *supra* note 203 at 287.

²¹⁰ *Ibid* at 291.

²¹¹ F. Weiser, *Trusts on the Continent of Europe: A Study in Comparative Law with an Annex Containing Suggestions for the Drafting of General Bonds of International Government Loans* (London: Sweet & Maxwell, 1936) at 15.

²¹² Hein Kötz, “National Report for Germany [G]” in D.J. Hayton, ed, *Principles of European Trust Law* (Hague: Kluwer Law International, 1999) 85 at 97.

for the benefit of another is more closely reflected in the German concept of the *testamentsvollstrecker*.²¹³ Different from a trustee who has full title to the deceased's assets for the purpose of the administration, the testamentary executor under German law is essentially an agent of the heirs. However, the executor plays a similar role as a trustee. He has the power and discretion in relation to disposition of property and he alone has the right to convey legal title of the property.²¹⁴

An heir, who is in the same position of a beneficiary under trusts, only enjoys a claim as a party to a contract. He can ask for a recovery of the property that the testamentary executor has transferred to a third party only when the third parties are not *bona fide* purchasers for value without notice. The legal basis for this claim is a breach of the duties that the trustee owes the settlor-beneficiary, i.e. the abuse of agency (*Mißbrauch der Vertretungsmacht*).²¹⁵ As to the issue of the position of the settlor-beneficiary against the trustee's personal creditors, German scholars address this by allowing the settlor-beneficiary to be granted the right to require that the assets be released to him by means of a third party complaint (*Drittsiderspruchsklage*), seen in section 771 of the Code of Civil Procedure. The settlor-beneficiary also has the right to release the trust assets in the case of the trustee's insolvency pursuant to section 43 of the German Bankruptcy Act of 1877.²¹⁶ The Imperial Court of Justice clearly expressed that according to the inner truth

²¹³ See Hein Kötz, "The Modern Development of Trust Law in Germany" in David Hayton, ed, *Modern International Developments in Trust Law* (The Hague/London/Boston: Kluwer Law International, 1999) 49 at 50-54. "The notion of trust relationship in German law is given an extraordinarily wide definition. It includes various specific types of trust relationships: trust relationship for the purpose of tying-up the estate (*nachlaßbindung*); trust relationship for the purpose of dedicating assets for charitable purposes; administrative trust; and investment companies (*Kapitalanlagegesellschaften*), which is a particularly important type of administrative trust".

²¹⁴ Waters, "The Institution of the Trust", *supra* note 117 at 387.

²¹⁵ Kötz, "The Modern Development", *supra* note 213 at 60-61.

²¹⁶ *Constant Case Law*, Cf. only BGH 7 April 1959, NJW 1959, 1223.

of the matter the assets still belong to the settlor-beneficiary because the transfer of property is only “in a legal sense, but not from a substantive and economic viewpoint”.²¹⁷ Therefore, the difference between the German *testamentsvollstrecher* and a trust lies not so much in the conceptual character of that device as an agency, given that the testamentary executor operates very much in the manner of the trustee based on the design of a binary system of the heir’s personal claims and the executor’s real rights.

(2) Introduction of trusts in the Latin American civil law tradition

Another example of the introduction of trusts in a pure civil law jurisdiction is Latin America, the Hispanic civil law countries. The introduction of the trust in these countries lies in the trading and financial interests they have in North America, in particular for the purpose of investing in and attracting capital from North America. In some jurisdictions, the trust is in the form of trusts for bondholders while the primary interests of these Latin American countries are in investment trusts. Therefore, it is not surprising to find that widespread permission is given in these countries to banks to accept confidential commissions. In other words, “the creator of the *comisionis* gives the bank an agency status (*mandato*) to carry out the task of investment, and deposits securities and cash with the bank as the intended initial investment fund.”²¹⁸ These *comisiones* have a similar nature to the deposit and mandate approach in European civil law and is known in common law as agency and bailment in which the bank is entitled to trade securities.

As a result, a legislative movement promoted by the United States was implemented in

²¹⁷ RG 23 December 1899, RGZ 45, 80, 85.

²¹⁸ Waters, “The Institution of the Trust”, *supra* note 117 at 382.

Latin America in 1921 and a significant number of Central and South American countries have adopted the *fideicomiso*, the most familiar investment fund, by introducing the trust.²¹⁹ The *fideicomiso* in Latin America is “seen almost exclusively as a trusteeship on the part of a bank or financial institution which is holding funds as private investment. [It] grant[s] loans at interest, hold[s] land as security and manage[s] mortgage repayment, or manage[s] developed real estate, though in this last instance seldom holding title to the real estate.”²²⁰ The first example of the *fideicomiso* is Colombia which adopted the concept in 1923. Panama also took immediate action with a 1925 law on the *fideicomiso*.²²¹ In Mexico and Venezuela, *fideicomisos* can be created for members of the family and for charitable and business purposes, but banks can only act as trustees and a trustee cannot be a beneficiary as well. This clearly proves that the trust is essentially used for financial investment, which is also true with Bolivian trusts and Guatemalan trusts. Nevertheless, natural persons are also accepted as trustees in some Latin American countries such as Panama, Costa Rica, El Salvador and Venezuela.²²²

In order to attract American investors to Latin American jurisdictions, the trustee is the owner of the trust property and “the creditors of the trustee shall succeed only if they are creditors in the administration of the trust”.²²³ For the beneficiary, he or she has the right to follow the trust property when the trustee transfers the property improperly and when required to trace the property in the hand of a third party unless the third party was a *bona fide* purchaser for consideration without notice. The trustee and creditor’s positions are broadly adopted, but with

²¹⁹ Maurizio Lupoi, *Trusts: A Comparative Study* (Cambridge: Cambridge University Press, 2000) at 269.

²²⁰ Waters, “The Institution of the Trust”, *supra* note 117 at 382.

²²¹ Lupoi, *Trusts: A Comparative Study*, *supra* note 219 at 269.

²²² Waters, “The Institution of the Trust”, *supra* note 117 at 382.

²²³ *Ibid* at 383.

respect to the status of the beneficiary in pursuing *in rem* actions, the situation is less clear. For instance, in Panama and Puerto Rico, there is some doubt as to whether a beneficiary can bring an *in rem* action against a transferee on the part of the trustee. With respect to the settlor's right of intervention in the administration of the *fideicomiso*, it is not infrequently found in Latin American countries.²²⁴

In general, Latin American countries found it uncomfortable to adopt the trust since the trust was originally a product of equity and to some extent is alien to their Hispanic civilian jurisdictions. However, the concept of a trust is known in varying degrees throughout Latin American. "Unlike the situation in Scotland and in South Africa, the *fideicomiso* has made its way into Central and South America by means only of express legislation."²²⁵ The introduction of trusts in these countries are interesting cases for comparative studies because their trust legislation might be considered as a product of the development of international investment, a main incentive for the introduction of trusts in modern times. Also, it is interesting to see whether the involvement of Mexico and North America as a result of the North America Free Trade Association (NAFTA) will further the move of the *fideicomiso* in Mexico.

B. Introduction of Trusts in Mixed Jurisdictions

Not only has the trust been introduced in pure civilian jurisdictions, but also in a number of mixed jurisdictions. For instance, the legal system of Louisiana in the United States and South Africa, as well as Scots law and Quebec law as will be discussed in detail in the following

²²⁴ *Ibid.*

²²⁵ *Ibid* at 385.

sections.

(1) Introduction of trusts in Louisiana

Louisiana is a mixed jurisdiction with private law drawn from the civil law tradition and public law derived from the common law tradition.²²⁶ Its experience of the introduction of trusts is one of the most interesting cases for comparative studies. This State was governed by a civil code that was closely connected to the Napoleonic code. It was only in 1964 that a special law covering all aspects of trusts was passed.²²⁷

Since 1882, Louisiana has recognized the trust for particular purposes by statute; and in 1938 it, for the first time, introduced a generalized statute permitting the trust for any purpose. The 1938 Act defined the trust in largely the same terms as the First Restatement.²²⁸ It stated that “[t]he ‘trust’ refers to an express private trust, and means a fiduciary relationship with respect to property, subjecting the person by whom the property is held, to deal with the property for the benefit of another person, which arises as a result of a manifestation of an intention to create it”.²²⁹ This Act stipulated the trustee as the person holding property in trust. Nevertheless the 1938 Act created both practical and conceptual problems and it did not integrate the trust into the civil law of Louisiana. As a result, it was soon ultimately replaced by a comprehensive coverage of the whole field of trusts in the codification of 1964, which is the statute that remains in force today. The main purpose of the Trust Code of 1964 “was to allow attorneys in the state to take

²²⁶ Michael McAuley, “Truth and reconciliation: Notions of property in Louisiana’s Civil and Trust Codes” in Lionel Smith, ed, *Re-imagining the Trust: Trusts in Civil Law* (Cambridge: Cambridge University Press, 2012) 119 at 119.

²²⁷ Lupoi, *Trusts: A Comparative Study*, *supra* note 219 at 281-82.

²²⁸ McAuley, *supra* note 226 at 156.

²²⁹ *Louisiana Trust Estates Act*, Act 81 of 1938; La. R.S. 1950, Title 9, as amended., 9:1792(16).

advantage of techniques for providing generational family asset management and enjoyment, and of federal tax concessions for trusts that were available elsewhere in the United States”.²³⁰ It is stated in the 1964 Code that Louisiana required a trust law for the state and to which the state’s judges could turn, if necessary, in interpreting and applying the Code.

The 1964 Code solved numerous fundamental problems. A key problem that has been faced by every civilian jurisdiction recognizing absolute ownership is that of the split between legal and equitable titles under common law. Louisiana had faced this problem ever since its first trust statute of 1882. Due to long discussions, the code stipulated that the title to the trust property remain with the trustee in consideration of the tax difficulties that would result if Louisiana adopted a different rule from the system in the rest of the United States (where the trustee takes legal title). It is stated in section 1781 that “[a] trustee is a person to whom title to the trust property is transferred to be administered by him as a fiduciary”.²³¹ In order to localize this anomaly in civil law terms, the Code carefully defines a trust as a “relationship resulting from the transfer of title to property to a person to be administered by him as a fiduciary for the benefit of another”.²³²

The 1964 Code regulated that the fiduciary holds the legal title of the trust property so as to fit the state law into the rest of the United States. Nevertheless, a further question remains concerning characteristics of the beneficiary’s right, i.e. whether it is a real right or personal right since the beneficiary not only has “a right of action against the trustee personally for breach, but

²³⁰ Waters, “The Institution of the Trust”, *supra* note 117 at 372.

²³¹ *Louisiana Trust Code*, Act 338 of 1964, La. R.S. 9:1721-2252 (Supp. 1964), s 1781.

²³² *Ibid*, s 1731.

also the proprietary right to recover trust property, whether converted or not, from the trustee's hands or from the hands of a third party who took with notice or gratuitously".²³³ With regards to this question, Louisiana chose to leave open the conceptual side of how the beneficiary might enforce his right, and instead delineate the remedies available to the beneficiary. "Part VIII of the Trust Code retains the personal right of action against the trustee which had been a part of the 1938 Law, and otherwise follows the American Law Institute *Restatement (Second) of Trusts* in permitting the beneficiary to enforce a right of the trust estate against a trustee who acts improperly with trust property and any third party who receives with knowledge of the breach or gratuitously."²³⁴ In other words, the Trust Code follows the conceptual structure of the common law trust as it is set out in the American Restatement, and concerns itself with translating that Code into a doctrinal expression that is considered compatible with Louisiana's civil law.²³⁵

(2) Introduction of trusts in South Africa

Another case of the introduction of trusts is South Africa. Different from Louisiana, which is a civilian jurisdiction in a common law country, the South African legal system is characterized by its mixed nature occasioned by the coalescence of Roman-Dutch law with English law. That makes it of great interest for comparative studies.

South Africa adopted the old uncoded Roman Dutch legal tradition at the Cape of Good Hope in the middle of the 17th century²³⁶. This legal system has been maintained by the

²³³ Waters, "The Institution of the Trust", *supra* note 117 at 373.

²³⁴ *Ibid* at 373-74.

²³⁵ In addition to the Restatement First and Restatement Second, the Restatement Third indicates the current understanding of the trust device in the Anglo-American world though it is not a direct source for the Trust Code.

²³⁶ Francois du Toit, "Jurisprudential Milestones in the Development of Trust Law in South Africa's Mixed Legal

Africans and the new and later English settlers throughout the whole country. The trust of English law was only introduced deliberately during the British conquest of the Dutch settlers.²³⁷ Moreover, as the Appellate Division stated in its seminal judgment in *Braun v Blann and Botha*²³⁸: English law's notion of dual ownership is foreign to South African law's adherence in a typically civilian tradition to single or unitary ownership in the form of a dominium.²³⁹ As a consequence, very little of the rules of English trust law have been imported into South Africa. Nevertheless, it cannot be denied that English law remains an important source of comparative jurisprudence for the development of South African trust law, especially when courts and scholars in South Africa address novel trust problems.²⁴⁰ Furthermore, the English law was set up for business as part of African law; the trust is used intensively for investment purposes and plays an active estate-planning role outside pure common law jurisdictions.²⁴¹

The laws, including the trust law, in South Africa, are uncoded. The courts have inevitably attempted to define the trust in terms of Roman Dutch conceptual thinking. "The *inter vivos* trust was analogized with *fiducia*, being a pact or agreement between the settlor and the trustee for the administration of property by the trustee for the benefit of the transferor (the settlor). [The testamentary trust, for many years], was conceived of as a type of *fideicommissum*, the trustee being the fiduciary and the trust beneficiary being the sole party with a beneficial interest."²⁴² However, the definition of the testament trust was rejected by the Appellate Division

System" in Lionel Smith, ed, *The Worlds of the Trust* (Cambridge: Cambridge University Press, 2013) 257 at 257.

²³⁷ Waters, "The Institution of the Trust", *supra* note 117 at 353.

²³⁸ *Braun v Blann and Botha*, 1984 (2) SA 850 (A) at 859E-F.

²³⁹ Du Toit, *supra* note 236 at 258.

²⁴⁰ *Ibid.*

²⁴¹ Waters, "The Institution of the Trust", *supra* note 117 at 356.

²⁴² *Ibid* at 354.

in the *Braun* case. The court stated that it would be both historically and jurisprudentially wrong to identify the trust with the *fideicommissum* and to equate a trustee with a fiduciary.²⁴³ Instead, it labeled the testamentary trust as a legal institution *sui generis*, namely an independent institution of its own kind²⁴⁴.

In comparison to the efforts made by the courts, legislation in South Africa has made a relatively limited contribution to the development of trust law. The first statute regulating the trust was the Trust Moneys Protection Act 34 of 1934, which is significant principally for its directives regarding the furnishing of security by trustees. The most important and most recent legislation is the Trust Property Control Act 57 of 1988. Although it is not a legislative attempt at codification of the body of South African trust law, the Act seeks to establish firmer control over trustees and their stewardship of trusts by the Master of the High Court²⁴⁵. It legislatively codified a trustee's duty of care in section 9(1) and defined the trust in section 1:

[T]he arrangement through which the ownership of property of one person is by virtue of a trust instrument made over or bequeathed

(a) to another person, the trustee, in whole or in part, to be administered or disposed of according to the provisions of the trust instrument for the benefit of the person or class of persons designated in the trust instrument or for the achievement of the object stated in the trust instrument, or

(b) to the beneficiaries designated in the trust instrument, which property is placed under the control of another person, the trustee, to be administered or disposed of according to the provisions of the trust instrument for the benefit of the person or class of persons designated in the trust instrument or for the achievement of the object stated in the trust instrument.²⁴⁶

From this definition it is not hard to find that “the Act recognizes two forms of the so-

²⁴³ *Braun*, *supra* note 238 at 859C, 866B.

²⁴⁴ *Ibid* at 859E.

²⁴⁵ M.M. Corbett, “Trust Law in the 90’s: Challenges and Change” (1993) 56:2 *Journal of Contemporary Roman-Dutch Law* 262 at 267.

²⁴⁶ *Trust Property Control Act*, (S Afr), No 57 of 1988, s 1.

called trust in the strict sense: first, the arrangement where the trustee is vested with the ownership in trust property and, secondly, where the ownership in trust property vests in the trust beneficiaries with the trustee as mere administrator”.²⁴⁷ The former type of trust is generally known as the so-called ‘ownership trust’, which is the most common type of trust; while the latter is known as the *bewind* trust in South African and corresponds with the institution of *bewind* in modern Dutch law and that of *bewindhebber* in Roman-Dutch law.

In the ownership trust, the trustee is the owner of the trust property, however devoid of any beneficial interest in such ownership. Therefore, the trustee’s ownership is considered as bare since the trust property forms no part of the assets or estate of the trustee.²⁴⁸ Actually, in *Land and Agricultural Bank of South Africa v Parker*²⁴⁹, the court identified the core idea of the trust in South African law as the functional separation between a trustee’s ownership or control of trust property and the enjoyment derived by the beneficiaries from the trustee’s exercise of such ownership or control. It is best described by Professor Honoré as a doctrinal hybrid, a *jus tripartitum* of Roman Dutch, English and indigenous South African rules, but in its end-product a *jus civiles*.²⁵⁰

With respect to the issue of the trustee’s duty of care, section 9(1) of the Trust Property Control Act regulates that “[a] trustee shall in the performance of his duties and the exercise of his powers act with the care, diligence and skill which can reasonably be expected of a person

²⁴⁷ Du Toit, *supra* note 236 at 269.

²⁴⁸ *Ibid* at 271, n 57: W. Geach and J. Yeats, *Trusts: Law and Practice* (Cape Town: Juta & Co Ltd, 2007), p. 2. Section 12 of the Trust Property Control Act prescribes that trust property shall not form part of the personal estate of a trustee except insofar as such trustee is entitled to such property as a beneficiary under the trust.

²⁴⁹ *Land and Agricultural Bank of South Africa v Parker*, 2005 (2) SA 77 (SCA) at para 19.

²⁵⁰ Edwin Cameron et al. *Honoré’s South African Law of Trusts*, 5th ed (Cape Town: JUTA Law, 2002) at 17-18.

who manages the affairs of another.”²⁵¹ Failing to do so, the trustee can incur personal liability for breach of trust and can be sued in delict by the beneficiary.

As in other civil law countries, the trust law of South Africa faces a number of difficulties due to the fact of incepting a common law product into a civilian system. For instance, the difficulty of characterizing the nature of a beneficiary’s rights, namely whether the beneficiary has any right other than to claim against the trustee for breach of the trust. Additionally, creditors of the trustee have insisted that property transferred to the trustee is certainly subject to the claims of the personal creditors of the trustee, notwithstanding the debt incurred by the trustee or the obligation while acting as a trustee.²⁵² Despite such difficulties, the trust law of South Africa sets up a model and serves as a guide for other civilian systems. It is useful for comparative studies because South Africa “constitutes a real and necessary attempt to rationalize the trust in a civil law context by the courts of a country that found itself with the trust, whether it would have that trust or no ... [The] courts have preferred to make their way both with the rationalization and the development of the South African trust in the thought form of the civil law.”²⁵³ Professor Beinart described the practice in South Africa, i.e. the introduction of trusts in an uncoded civil law jurisdiction, as follows: “the recipe for absorption of a useful institution such as the trust into a civilian system appears to be avoidance of excessive conceptualism and legal purity or rigidity, and achievement of a judicious mixture of historical precedents and a conceptual appreciation with the demands of practice.”²⁵⁴

²⁵¹ *Trust Property Control Act*, *supra* note 246, s 9(1).

²⁵² Waters, “The Institution of the Trust”, *supra* note 117 at 355.

²⁵³ *Ibid.*

²⁵⁴ B. Beinart, “Trusts in Roman and Roman-Dutch Law” (1981) 6 *Trusts and Trust Like Devices* 167 at 208.

4. The Scottish Theory of Trusts

The Trust has been recognized in Scotland for a long time, at least since the 17th century.²⁵⁵ The introduction of the trust in Scots law is a very interesting case; similar to South Africa, Scotland also has a mixed legal system and its law has never been codified. Furthermore, what makes it more interesting than South African law is that the Scottish jurisdiction is very similar to the English system which is the place of origin of the trust. Indeed, Since 1707 England and Scotland have shared the House of Lords as a common final appellate court.²⁵⁶ As a result, at the end of the 18th century, English common law played a significant role in the development of the Scottish trust and some Scottish regulations are even derived from English common law.

In addition to the legal tradition of English common law, Scots law also has a civil law origin. Actually, property law in Scotland is particularly civilian. With respect to the trust, Scholars believe that it originates from the Roman *fideicommissum* which came from a feudal conveyancing procedure.²⁵⁷ Nevertheless, it is worth noting that Scots law has never been codified.²⁵⁸ There is nothing close to a code of trust law in Scotland. The trust was neither introduced nor prohibited by statute at the beginning. Practitioners have simply made use of the trust device and the courts and jurists have had to deal with it.²⁵⁹

Only by the 18th century, a form of trust called ‘fiduciary fee’ had been recognized,

²⁵⁵ Gretton, “Trusts Without Equity”, *supra* note 170 at 619.

²⁵⁶ Waters, “The Institution of the Trust”, *supra* note 117 at 348.

²⁵⁷ W.A. Wilson & A.G.M. Duncan, *Trusts, Trustees and Executors*, 2nd ed (Edinburgh: Scottish University Law Institute Ltd, 1995) at 3.

²⁵⁸ Waters, “The Institution of the Trust”, *supra* note 117 at 349.

²⁵⁹ Chalmers, *supra* note 156 at 140.

whereby a person would hold the property for himself in lifetime and his children in fee simple.²⁶⁰ This device was subsequently recognized by statute²⁶¹ and remains competent today.²⁶² The basic statute regulating trusts in Scotland is the *Trusts (Scotland) Act 1921*²⁶³. Nevertheless, it is quite outdated in both style and substance. Much of the Act deals with old trusts that were used to hold landed estates or, through the marriage contract trust, to manage weaknesses in the law regarding the property of married women. Nowadays, the trust is used more for the purposes of tax and estate planning, to regulate a family's business interests, or for commercial purposes.²⁶⁴ These changes are not reflected in the *Trusts (Scotland) Act 1921*. Nevertheless, a few regulations have been passed subsequently that amend the 1921 Act and provide further free-standing provisions. The main statutory provisions are the *Trustee Investments Act 1961*²⁶⁵, the *Trusts (Scotland) Act 1961*²⁶⁶, the *Law Reform (Miscellaneous Provisions) (Scotland) Act 1966*²⁶⁷ and the *Charities and Trustee Investment Act 2005*²⁶⁸.

A. Different Theories of Ownership Developed in Scotland

Although English common law plays a significant part in the development of the Scottish trust, “[t]here never was a time in Scots law when there was a distinction between courts concerned with the letter of the law and other courts concerned with unconscionability. As a result Scots law has never known, and does not know today, the distinction between the legal and

²⁶⁰ *Newlands v Newlands' Creditors* (1794) Mor 4289.

²⁶¹ *Trusts (Scotland) Act 1921* (UK), 1921, c 58, s 8.

²⁶² Chalmers, *supra* note 156 at 140.

²⁶³ *Trusts (Scotland) Act 1921*, *supra* note 261.

²⁶⁴ *Discussion Paper on Supplementary and Miscellaneous Issues*, *supra* note 177 at para 1.5.

²⁶⁵ *Trustee Investments Act 1961* (UK), 1961, c 62.

²⁶⁶ *Trusts (Scotland) Act 1961* (UK), 1961, c 57.

²⁶⁷ *Law Reform (Miscellaneous Provisions) (Scotland) Act 1966* (UK), 1966, c 19.

²⁶⁸ *Charities and Trustee Investment (Scotland) Act 2005* (UK), 2005, asp 10.

the equitable estate.”²⁶⁹ Therefore, with respect to the introduction of trusts in Scots law, the question that needs to be asked is how Scots law accommodates the common law notion of dual ownership in its own system where there is an absence of legal and equitable estates.

In response to this question, different theories with respect to the ownership of trust property have been raised in Scotland. These theories have caused considerable confusion over time; writers and the courts have vacillated between various positions.

(1) Legal person theory

One theory that has been discussed often to explain the ownership of trust property is the legal person theory. It considers the trust as a legal person and itself the owner of the trust property. As Lepaulle states: “I do not deny that this is an easy way out: instead of struggling with delicate concepts and bold creations, it settles for taking an old idea from our familiar armoury.”²⁷⁰ However, this theory has been strongly rejected by the Scottish Commission.

On March 1st 2005, the Scottish Law Commission hosted a seminar to stimulate discussion concerning the concept of legal personality for trusts; namely, whether the trust should be recognized as an artificial legal entity with its own juristic personality and therefore become the owner of the trust property. Twenty-four participants consisting of a mix of both academics and practitioners attended this seminar. The feasibility of recognizing a legal personality for trusts was discussed in the seminar; nevertheless, the participants felt that the

²⁶⁹ Waters, “The Institution of the Trust”, *supra* note 117 at 349.

²⁷⁰ Smith, “Trust and Patrimony”, *supra* note 2 at 354, n 93; Lepaulle, “La notion de ‘trust’”, *op. cit.*, footnote 72, at p. 207.

operational disadvantages of conferring legal personality on trusts far outweighed any presentational advantages.²⁷¹ Their concerns are mainly reflected in two aspects: (a) this method would complicate issues and (b) its uniqueness may cut Scotland off from other jurisdictions. As stated by the Commission, the value of the trust is its simplicity and therefore its adaptability for use in new economic and social environments. Giving the trust a legal personality would complicate matters. If the trust is a legal person,

[it] would have to exercise its active legal capacity through agents, presumably the trustees. Apart from issues of *vires*, the agency rules which would govern the relationships between the trust, the trustees and third parties would not be simple. It was accepted that even if a trust had separate juristic personality, trustees would continue to owe fiduciary obligations to the beneficiaries as well as the trust: difficult conflicts of interest could be envisaged.²⁷²

In addition, the legal person theory would cut Scotland off from future developments in trust law elsewhere because the concept of a legal device where property is owned by one person on behalf of another was being developed at European²⁷³ and international levels.²⁷⁴

Other arguments to support the Commission's position are: first, it is not necessary to introduce an extra juristic person – the trust. A distinction could be made between public and private trusts and a case might be made that the former should have juristic personality. However, there already exist several suitable routes for public trusts to obtain separate legal personality, which exist in the form of incorporation as a company limited by guarantee or as a Scottish Charitable Incorporated Organization, if the public trust is also charitable.²⁷⁵ Moreover, it is

²⁷¹ *Discussion Paper on the Nature and the Constitution of Trusts*, *supra* note 188 at paras 1.3-1.4.

²⁷² *Ibid* at para 2.41.

²⁷³ See for example the 1986 Hague Convention on the Recognition of Trusts and the work of the Coordinating Group on Trust Law.

²⁷⁴ *Discussion Paper on the Nature and the Constitution of Trusts*, *supra* note 188 at para 2.43.

²⁷⁵ *Ibid* at para 2.40.

argued that the trust can be granted a legal personality since there seems to be an analogy between the trust and the partnership that has its own legal personality. Nevertheless, the relationship between the partnership and its partners are distinct from the one between the trust and its trustees. The partnership is a profit-seeking enterprise and its partners intend to receive a share of any profits the partnership makes, i.e. acting as intended beneficiaries of the partnership. In contrast, the manager of the trust, the trustee, is not an intended beneficiary of the trust.²⁷⁶

Furthermore, not only is it unnecessary, but also wrong to characterize the trust as a legal person. Professor Lionel Smith criticized the theory of legal person and stated that “it would be a mistake for any legal system to conceptualize the trust as a legal person, since the result will only be to eliminate the trust as a fundamental legal institution.”²⁷⁷ In order to be a fundamental institution, the trust cannot be another institution such as a sub-category of legal persons or contracts.²⁷⁸ As a result, the legal person theory was also denied by Scots law because it requires statutory intervention and cannot explain the trust as it currently exists.²⁷⁹

(2) Theory of a beneficiary’s ownership

Negating the legal personality of the trust, the question now is to whom the ownership of trust property should be attributed. Before answering this question, one thing needs to be clarified; a trustee, not the owner of trust property, is the person who should be granted exclusive powers of management over the trust assets in order for a trust to function.²⁸⁰ So, if the settlor or

²⁷⁶ *Ibid* at para 2.42.

²⁷⁷ Smith, “Trust and Patrimony”, *supra* note 2 at 334.

²⁷⁸ *Ibid* at 349.

²⁷⁹ *Chalmers*, *supra* note 156 at 133, n 5.

²⁸⁰ Reid, “Conceptualising the Chinese Trust”, *supra* note 189 at 115.

beneficiaries are considered the owners of the trust property, the right of management will be taken away from them and conferred to trustees.

In the late 19th century, Lord McLaren stated that both the trustee and beneficiary are simultaneously the owners of the property and coined the phrase ‘personal right of property’ to explain the beneficiary’s right.²⁸¹ A few years later, Matters said that “the [beneficiary], to whom the whole beneficial interest belongs, is the true owner”.²⁸² This theory has now been rejected and it is clearly understood that under current Scots law the trustee is the owner of the trust property.²⁸³

One reason Scots law rejected the theory of a beneficiary’s ownership is that a beneficiary in a Scottish trust can be unascertained. For instance, a trust can be validly created for a person’s children even if this person has no offspring or may never have any offspring. Therefore, if the beneficiary were the owner of the property, the ownership of the trust property would be uncertain as well or might not ever exist. Furthermore, if the beneficiary, but not the trustee, were the owner of the trust property, it would be hard to explain why the trustee can transfer good title to a third party. It violates the principle of *nemo plus juris ad alium transferre potest quam ipse haberet* (no one can give what he does not have), which precludes the non-owner trustee from transferring title to the trust property. Although an agent can dispose properties on behalf of a principal, a trustee is distinct from an agent and their rights are different in nature. “The trustee simply does not have the relationship with a *beneficiary* which agency

²⁸¹ *Hay’s Trs v Hay* (1890) R 961 at 964.

²⁸² *Millar*, *supra* note 175 at 46-47.

²⁸³ *Chalmers*, *supra* note 156 at 141.

would require.”²⁸⁴ The trustee’s right is to make a claim on the trust property and not to pursue the beneficiary personally. “So where a trustee breaches trust at the request of a beneficiary, the Trust (Scotland) Act 1921 s 31 only goes so far as to allow the court to apply the beneficiary’s interest in the trust by way of indemnity to the trustee, not to create a right against the beneficiary.”²⁸⁵

B. Fiduciary Ownership in the Mixed Scottish Legal System

Negating the legal person theory and theory of a beneficiary’s ownership, Scots law adopts the theory of fiduciary ownership. It recognizes the absolute title of trust property in the trustee. In order to have a better understanding of the fiduciary ownership in Scots law, it is necessary to first study the classic notion of fiduciary ownership in French law.

(1) Fiduciary Ownership in French law

The concept of *Fiducia* was present within Roman law and then gradually disappeared from most civilian systems, at least as a nominate institution. Nevertheless, in recent decades, the civilian *Fiducie* has had a renaissance which draws inspiration more from the trust of the common law.²⁸⁶ In order to introduce the trust into civil law, Professor Emerich believes that the interpretation of common law dual ownership into the notion of fiduciary ownership is a

²⁸⁴ *Ibid* at 143.

²⁸⁵ *Ibid* at 143, n 72.

²⁸⁶ Yaëll Emerich, “The Civil Law Trust: A Modality of Ownership or An Interlude in Ownership?” in Lionel Smith, ed, *The Worlds of the Trust* (Cambridge: Cambridge University Press, 2013) 21 at 21-22.

possibility within civilian jurisdictions, both from a theoretical perspective and a practical perspective.²⁸⁷

From a theoretical perspective, fiduciary ownership has similar characteristics to dual ownership. Fiduciary ownership is an ownership that receives a specific alignment towards a purpose. This purpose of the *fiducie*, which is set up by the settlor, becomes a restriction on the trustee's administration and discretion. In other words, the trustee shall manage the property in line with the purpose of the *fiducie*. The fiduciary relationship is not a benefit for the trustee since he must act in the interest of the beneficiary; and the third party in good faith should take unchallengeable title in any *fiducie* assets that he requires through dealing with the fiduciary in the administration of the *fiducie*.²⁸⁸ Therefore, fiduciary ownership is only a presence of legal powers but not a subjective right of ownership.²⁸⁹ These characteristics are evident when considering the similarity between fiduciary ownership and dual ownership of the common law and make fiduciary ownership seem different from the absolute ownership of the civil law. Nevertheless, the differences, including the restrictions of the trustee's rights, do not negate the potential presence of attributes of the traditional absolute ownership. The traditional attributes, "namely *usus*, *fructus* and *abusus*, can be found within fiduciary ownership, since the trustee has in principle all the powers over the property which is held in *fiducie*."²⁹⁰ Therefore, fiduciary ownership is a possible device to introduce the trust into civilian jurisdictions because of its similarity with dual ownership and its potential presence of absolute ownership.

²⁸⁷ *Ibid* at 22.

²⁸⁸ Waters, "The Institution of the Trust", *supra* note 117 at 394.

²⁸⁹ Emerich, *supra* note 286 at 24.

²⁹⁰ *Ibid*.

From the practical perspective, French civil code defines the *fiducie* in article 2011 as ‘the arrangement by which one or more settlors transfer property, rights or guarantees for the performance of an obligation, or an assemblage of property, rights or guarantees, present or future, to one or more trustees who, holding them *separate from their own patrimony*, act for a *determinate purpose* in favour of one or more *beneficiaries*’ (Emerich’s translation and italics).²⁹¹ It is not hard to draw from this definition that the *fiducie* is an arrangement by which a settlor transfers property to a trustee. Furthermore, another point derived from the definition of *fiducie* is that the *fiducie* property is to be held by the fiduciary separately from the fiduciary’s own personal property. In order to guarantee the separation of the two patrimonies by the fiduciary, it is necessary to make sure that there is no mixture between the fiduciary’s personal assets and *fiducie* assets. In addition, the liabilities of the fiduciary with respect to his own property should not be confused with the liabilities in relation to the administration of the *fiducie* assets. Namely, two types of creditors, the fiduciary’s personal creditors and the creditors of the *fiducie* assets should be distinguished; also the *fiducie* assets do not fall into the estate of a deceased trustee. Nevertheless, “the French *fiducie* does not involve a genuinely autonomous patrimony, since the *fiducie* patrimony is not completely separated either from the personal patrimony of the trustee or the personal patrimony of the settlor. Accordingly, the second paragraph of article 2025 of the French Civil Code provides that where the *fiducie* patrimony is insufficient, the creditors of the *fiducie* can seek payment of their claim from the patrimony of

²⁹¹ *Ibid* at 27, n 25: Three principal elements can be drawn from this definition: (1) *fiducie* is an arrangement by which a settlor transfers property to a trustee; (2) the trustee holds this property apart from his own patrimony; (3) the trustee acts for a determinate purpose in favour of a beneficiary.

the settlor.”²⁹² Therefore, this kind of separated patrimony actually creates “a sub-patrimony within the trustee’s personal patrimony rather than an actual patrimony by appropriation”.²⁹³

Based on the above analysis of the fiduciary ownership, Professor Emerich characterized fiduciary ownership as a modality of ownership, in other words, a particular mode of existence of ownership.²⁹⁴ This is because the fiduciary ownership is a type of ownership that comes under an appropriation and is directed to a purpose, which perfectly fits in terms of the modality defined by Professor Jean Carbonnier: the modalities of ownership “are ways of being with which the right of ownership clothes itself; their result, in the final analysis, is always limits on the powers of the owner, yet without the right of ownership being dismembered, for all that”.²⁹⁵ Actually, it is “possible to find the traditional attributes of ownership within the fiduciary ownership of French law, since the trustee receives the right to make use of the property that comes within the *fiducie*, to collect the fruits of this property and to alienate them”.²⁹⁶

The concept of *fiducie* sheds light on the study of introducing the trust into civilian jurisdictions. It inspires comparativists to research on whether it is adequate enough to introduce the common law trust using the term *fiducie*, namely whether the *fiducie* plays the same role and

²⁹² *Ibid* at 27.

²⁹³ *Ibid*.

²⁹⁴ *Ibid* at 23.

²⁹⁵ *Ibid* at 29, n 35: J. Carbonnier, *Les biens : Droit civil*, 19th edn., 4 vols. (Paris: Presses Universitaires de France, 2000) v III : Les Biens (*monnaie, immeubles, meubles*), p. 144, n° 78. See also S. Normand, ‘La notion de modalité’, in S. Normand (ed.), *Mélanges offerts au professeur François Frenette: Études portant sur le droit patrimonial* (Québec: Presses de l’Université Laval, 2006), p. 255ff.

²⁹⁶ *Ibid* at 29.

achieves the same objectives as the trust. One of its successful examples can be seen in Scots law.

(2) Fiduciary ownership in Scots law

A description of the typical trust under Scots law was made by Lord Normand in the English House of Lords case, *Camille and Henry Dreyfus Foundation Incorporated v Commissioners of Inland Revenue*. He stated that

A fund is held as their property in trust by persons who are directed to hold it, subject to purpose which operate as a qualification of their rights and constitute a burden on the property preferable to all claims by or through them, and subject also to a reversionary right remaining with the truster, his heirs and assignees, so far as the estate is not exhausted by the purpose.²⁹⁷

It is evident from the definition that the essential element of the trust in Scots law is the concept of fiduciary ownership. Fiduciary ownership in Scots law arises when the owner of property is under a duty to use it for the benefit of another and not for himself. In the law of trusts, the fiduciary owner of the trust property is the trustee. The beneficiary is the person for whose benefit the trustee must administer the property under a fiduciary obligation. The trust itself is simply a legal device that creates rights and obligations among settlors, trustees and beneficiaries.²⁹⁸ In other words, the ownership of trust assets is transferred from a settlor to a trustee, while the right of a beneficiary is classified only as a personal claim, i.e. a simple personal right as opposed to a real right. That is, being the owner of trust assets, the trustee can transfer a good's title to a third party under the authority of the declaration of trusts or statute.

²⁹⁷ *Camille and Henry Dreyfus Foundation Incorporated v Commissioners of Inland Revenue*, [1956] AC 39, 48, [1955] SLT 335.

²⁹⁸ *Discussion Paper on the Nature and the Constitution of Trusts*, *supra* note 188 at para 2.1.

The beneficiary cannot vindicate the property from the third party since he has no proprietary interest in the trust property. His right to seek recovery of trust property is defeated by a *bona fide* transferee for value.²⁹⁹

The notion of fiduciary ownership addresses the idea that the trustee is the owner of trust property. This idea has been advised by Professor Reid on the grounds of convenience. He believes that attributing the ownership to the trustee will remove the burden of proof from the trustee in showing a third party that he has the power to manage the trust property even without ownership. Moreover, this method is relatively effective to avoid a limbo of ownership. For instance in the circumstance when there are no current beneficiaries or too many; when there is a dispute as to whether a person is a beneficiary or not; and when the settlor or beneficiary is dead or dissolved. Although with regards to the last example the trustee may also die, it is easier to appoint new trustees than new beneficiaries or settlors.³⁰⁰ Moreover, the idea of trustee's ownership is also recognized and implemented in the academic project of EU. *The Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference (DCFR)* defines a trustee as "the person in whom the trust fund becomes or remains vested".³⁰¹ It argues that "[a]n essential feature of a trust is that title to the trust fund is vested in the trustee. For the purposes of performing the trust the trustee is cloaked in the mantle of an outright owner".³⁰²

However, a difficulty is faced by civil law systems with respect to the trustee's

²⁹⁹ *Ibid* at para 2.8.

³⁰⁰ Reid, "Conceptualising the Chinese Trust", *supra* note 189 at 116.

³⁰¹ Christian von Bar & Eric Clive, eds, *Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference (DCFR)* (Munich: Sellier European Law Publishers, 2009), X.-1:203 (2).

³⁰² *Ibid*, full Edition, vol. 6, at 5691.

ownership. That is the claim that the trustee's ownership of trust property leads to a trustee's personal creditors having first claim against the trust property. Scots law has denied this claim. The courts "held that the trust estate is not the 'property of the trustee' as that term is used in the Bankruptcy Acts, and for that reason they decided that the trust property does not pass to the trustee of the trustee's personal sequestration."³⁰³ The statement of the personal creditor's first claim against trust property is inconceivable because the trustee was always seen as someone who wore two hats; one hat was his personal obligation and the other hat was that of a trustee.

Another idea that is reflected in the notion of fiduciary ownership is that the nature of the beneficiary's right is classified as a personal claim. At first, Scottish lawyers were of the opinion that the beneficiary has a mere personal right or the right otherwise of the unsecured creditor.³⁰⁴ As late as 1939 in *Commissioner of Inland Revenue v Clarke's Trustee*³⁰⁵, Lord President Normand described the beneficiary's right as nothing more than a personal right to sue the trustees and to compel them to administer the property in accordance with the directions which [the trust instrument] contains.

Nevertheless, this opinion is not agreed with by all Scottish authors since the beneficiary's right seems to lie somewhere in between. The reason why a beneficiary's personal claim is different from the unsecured rights of a trustee's personal creditors over which it appears to prevail, is not because the beneficiary's right is a real right, but because the trust property is not available to a trustee's ordinary personal creditors.³⁰⁶ In other words, even though the nature

³⁰³ Waters, "The Institution of the Trust", *supra* note 117 at 351.

³⁰⁴ *Ibid* at 352.

³⁰⁵ *Commissioner of Inland Revenue v Clarke's Trustee*, [1939] SC 11 at 22, [1939] SLT 2.

³⁰⁶ *Discussion Paper on the Nature and the Constitution of Trusts*, *supra* note 188 at para 2.13.

of the beneficiary's right is still not a real right, "[t]he rights of beneficiaries do not behave like ordinary personal rights."³⁰⁷

It is a curious phenomenon. The general principle of insolvency law is that the unsecured creditors ... are subject to third party real rights but prevail over third party personal rights ... Since the right of a beneficiary in a trust is a personal right one would expect that it would be subject to the claims of the [trustee's] unsecured creditors. But it is not. Though a personal right, it is an enhanced personal right. So enhanced, indeed, that some people have felt a temptation to call it a real right, but that view, quite properly, has not prevailed. The right of a trust beneficiary is, in our law, not a real right which in some ways is like a personal right, but a personal right which in some ways is like a real right ... It is this quality that takes the trust wholly out of the law of obligations.³⁰⁸

Returning to the notion of special patrimony³⁰⁹, we see that the reason for which the beneficiary's rights seem to prevail over those of unsecured rights of trustee's personal creditors is not because the beneficiary's rights are real rights. Instead, it is because the beneficiary is claiming against the trustee's special patrimony. This type of claim, as noted, is different from the trustee's personal patrimony claim against his personal creditors. Therefore, "*the insolvency effect operates in all trusts regardless of whether the rights of the beneficiaries are 'real' or not*".³¹⁰ Moreover, Scots law does not recognize the beneficiary's right as a real right because: first, beneficial rights are often indeterminate and second, the identity of beneficiaries may be unknown. Whilst personal rights can more or less be reconciled with indeterminacy, real rights cannot.³¹¹ Additionally, it believes that the object of the real right must be particular, whereas the beneficiary's right is constantly changing rather than pointing to a particular object. Furthermore, if the beneficiary's right was considered as a real right, it should be registered and in that case

³⁰⁷ George L. Gretton, "Trust and Patrimony" in MacQueen, ed, *Scots Law into the 21st Century: Essays in Honour of W A Wilson* (Edinburgh: University of Edinburgh, 1996) 182 at 184.

³⁰⁸ George L. Gretton, "Constructive Trusts" (1997) 1:3 *Edinburgh Law Review* 281 at 287.

³⁰⁹ See Chapter II 2 A (2) The notion of special patrimony.

³¹⁰ Gretton, "Trusts Without Equity", *supra* note 170 at 606-07.

³¹¹ *Ibid* at 606.

the beneficiary's identity would have to be revealed. Since secrecy is deemed as the greatest advantage of the trust system, the beneficiary's identity should not be revealed. Under Scots law, the relationship between the trustee and beneficiary is essentially a claim but not a real right.³¹²

Instead of asking in which category, *in personam* right or *in rem* right, the beneficiary's right falls into, the real question might be what kind of interest has been given to the beneficiary. It is generally believed that when trust property has been wrongfully transferred by the trustee to a third party who had knowledge of the breach of trust or who took it gratuitously, the beneficiary can sue for the recovery of that trust property. Under Scots law, there appears to be no difficulty in recognizing the beneficiary's rights, either to take in succession to a previous chargee or to make proprietary claims against third parties who have received trust property wrongfully transferred by the trustee. Thanks to the notion of fiduciary ownership, Scots law has successfully introduced the trust into its mixed legal system. It rationalizes the trustee's ownership in the notion of fiduciary ownership and justifies the interest of the beneficiary in terms of a burden or charge upon absolute ownership.³¹³

Recent scholarship has developed the Scots law. Consequently, the implementation of fiduciary ownership has been considered as a means of understanding multiple patrimonies. This means, for example, that when a person becomes a trustee of a trust, he in fact owns two separate patrimonies: his private patrimony as before and a new patrimony – a trust patrimony. The key to understanding trusts in Scots law then, is to grasp the challenge of dual patrimonies.

³¹² Kenneth G C Reid, "National Report for Scotland [G]" in D.J. Hayton, ed, *Principles of European Trust Law* (Hague: Kluwer Law International, 1999) 67 at 70.

³¹³ Waters, "The Institution of the Trust", *supra* note 117 at 351.

5. Ownership of Trust Property in Quebec Law

Another classic example of a civilian jurisdiction that adopts the trust is Quebec. Unlike its French counterpart and Scots law, “Quebec law imagines the *fiducie* as a patrimony by appropriation, which is widely conceded as an alternative to fiduciary ownership because fiduciary ownership is deemed to be a concept too heavily imprinted with the common law.”³¹⁴ Nevertheless, it is worth noting that the term of patrimony by appropriation in Quebec law “has been considered by legal doctrine to differ from the European concept of patrimony by appropriation, seen as a *de facto* universality (in other words a mass of property without an associated set of liabilities)”.³¹⁵

The nature of the trust in Quebec law is defined as a patrimony by appropriation by the *Civil Code of Quebec*³¹⁶ (hereinafter referred to as CCQ). The term of patrimony by appropriation recognizes the trust as an impersonal patrimony. Namely, the trust itself is not a legal personality in Quebec law. This regulation is the same as the trust under common law.³¹⁷ Moreover, same as the common law trust, the Quebec law trust is not of a contractual nature; it is not contract of agency.³¹⁸ Although the trust can be established by contract, it is not a contract. That is why Quebec law regulates the trust as a new judicial institution on the part of the law of property. Unlike a principal in an agent relationship, the settlor cannot withdraw rights that have

³¹⁴ Emerich, *supra* note 286 at 30. Also see n 41: See on this point J.E.C. Brierley, ‘Regards sur le droit des biens dans le nouveau Code civil du Québec’ (1995) 47 *Revue internationale de droit comparé* 33, 45, para. 17; M. Cantin Cumyn, ‘The Quebec Trust: A Civilian Institution with English Law Roots’, in J.M. Milo and J.M. Smits (eds.), *Trusts in Mixed Legal System* (Nijmegen: Ars Aequi Libri, 2001), p. 80.

³¹⁵ *Ibid* at 32.

³¹⁶ *Civil Code of Quebec*.

³¹⁷ Fortin, *supra* note 180 at 287.

³¹⁸ *Ibid* at 288.

been transferred to the beneficiaries, unless the power to do so has been expressly reserved. Once the trust is created, the settlor is deprived of ownership of the trust property. The trustee does not need to follow the directives of the settlor, but only acts in the interest of the beneficiary within the scope of the trust. In a contract of agency, the agent is not the owner of the property and can only manage the property in accordance with his principal. Although Quebec law trusts and common law trusts are similar in these aspects, they are different in nature.

Indeed, the concept of dual ownership has never been accepted in Quebec law, though it was originally thought that the ownership of trust property resided in the revenue beneficiary.³¹⁹ In 1994, the CCQ rejected the duality of ownership in article 1261 and opted for the notion of a patrimony by appropriation over which no person has any real right. From a historical perspective, the reason for rejecting the dual ownership is rooted in French civil law. The basic principle of indivisibility of ownership of Quebec property law, which originated in the Napoleonic Codes that spread throughout Europe in the 19th century, makes the juridical nature of the Quebec trust different from that of the common law trust that adopts dual ownership. As a result, Quebec did not adopt the trust at first. However, with the development of business, certain types of trusts were created in Quebec in 1879³²⁰ and were transferred to the Civil Code as article 981a to 981n in 1888. The trust is of interest to Quebec due to the fact that Canada is a member of numerous treaties that recognize trust residence in Canada in order to give relief against double taxation; and trusts were recognized in all other provinces except Quebec. Therefore, due to the pressure of developing cross-provincial transactions and international trade, there was a

³¹⁹ William E. Stavert, "The Quebec Law of Trust" (2002) 21 Estates, Trusts & Pensions Journal 130 at 130.

³²⁰ *Act relating to Trusts*, SQ 1879, c 29.

need for Quebec to introduce the trust.³²¹ Nevertheless, the concept of dual ownership was not recognized in Quebec. Evidence can be found in *Royal Trust v Brodie*³²² in 1989, where the court held that a testamentary general power of appointment in a will was void and that the rule in *Saunders v Vautier* was not part of Quebec law.

With respect to the issue of the ownership of trust property, Quebec law has come a long way in its development. A series of cases on trusts indicates the development of the concept of the ownership of trust property. Its transition underwent three stages: first, the revenue beneficiary of the trust was considered as the owner of the trust property, reflected in *Masson*³²³ and in article 932 of the *Civil Code of Lower Canada* (hereinafter referred to as CCLC). Second, the ownership of trust property was held to subsist in trustees. Proof was found in *Curran*³²⁴, *Tucker*³²⁵, and *Todd*³²⁶. And third, neither the trustees nor the beneficiaries have any real right in trust ownership pursuant to the notion of patrimony by appropriation, stipulated in article 1261 of the CCQ and referred to in *Webster*³²⁷.

A. Regulations of Ownership of Trust Property pre CCQ

(1) Beneficiaries' ownership of trust property

The theory of beneficiaries' ownership of trust property was the first step in the

³²¹ *Fortin*, *supra* note 180 at 287.

³²² *Royal Trust v Brodie*, [1989] 25 Q.A.C. 22, 16 A.C.W.S. (3d) 205 (C.A.).

³²³ *Masson v Masson* (1907) 33 Que. S.C. 108 (S.C.), revd 20 Que. K.B. 1 (C.A.), revd 47 S.C.R. 42.

³²⁴ *Curran v Davis* (1931) Que. S.C. 123 (S.C.), affd 53 Que. K.B. 231 (C.A.), affd [1933] S.C.R. 283, [1934] 1 D.L.R. 161.

³²⁵ *Royal Trust Co. v Tucker*, 1982, SCC.

³²⁶ *Todd v Todd*, [1985] Que. S.C. 931, affd [1989] R.J.Q. 1176 at 1184-85, 29 Q.A.C. 99, leave to appeal to S.C.C. refused 27 Q.A.C. 159n 103 N.R. 398n.

³²⁷ *Royal Trust Corp. of Canada v Webster*, [2000] R.J.Q. 2361 (S.C.).

development of the ownership of trust property adopted in Quebec law. This theory was established in *Masson v Masson* by the Supreme Court of Canada in 1912, which stated that whoever is in the third rank of beneficiaries is entitled to the capital of a trust.³²⁸ In the absence of any express provision in the old law prior to 1994 limiting the duration of a trust, Anglin J. applied article 932 of the CCLC³²⁹, which limits the duration of a substitution to three degrees. The CCLC was replaced by the CCQ in 1994, and the word ‘degree’ was replaced by the term ‘rank’ as a consequence. Moreover, in *Masson*, capital beneficiaries were not designated in the trust deed, either by name or generation, which is an important distinction from the trust in a recent case *Webster* where the capital beneficiaries were stated by settlors.

(2) Trustee’s ownership of trust property

The second step of the transition of trust property occurred in 1933 in *Curran v Davis*. This case recognized trustees as the owners of trust property. The Supreme Court of Canada in this case found that the trustees were given a kind of right of ownership, temporary and limited as to its effects.³³⁰ This opinion, i.e. trustees’ ownership of the trust property, got confirmed in more certain terms in *Royal Trust Co v Tucker* by the Supreme Court of Canada in 1982. A major difference between the cases of *Curran* and *Tucker* is whether capital beneficiaries needed to be born when the trust is created. The answer was positive in the former case, but negative in the latter one.³³¹ Therefore, the court in *Tucker* faced the question whether the same decision would be made when the capital beneficiaries were not alive upon the creation of the trust. In

³²⁸ See *Masson*, *supra* note 323 at 88-90.

³²⁹ *Civil Code of Lower Canada*, art. 932: Substitutions created by will or by gifts *inter vivos* cannot extend to more than two degrees exclusive of the institute.

³³⁰ *Curran*, *supra* note 324 at 293-94.

³³¹ *Stavert*, *supra* note 319 at 137.

order to answer this question, the court held that:

[I]n a great many cases he ranks second or third and has not even been born or conceived. When the property held in trust is finally conveyed to him, as art. 981(1) expressly provides, the trust has terminated. That leaves only the trustee in whom ownership of the trust property can be vested. Clearly the right of ownership is not the traditional one, since, for example, it is temporary and includes no *fructus*. It is a *sui generis* property right, which the legislator implicitly but necessarily intended to create when he introduced the trust into the civil law.³³²

In other words, the court believed that the trustee's title to the trust property (pursuant to a trust constituted under a will or a gift) was characterized as a *sui generis* property right, and his or her relationship *vis-à-vis* the beneficiary was therefore seen as that of debtor. Conversely, the trust beneficiary was seen as a creditor of the trustee rather than a creditor of the trust itself.³³³

Another judgment relating to the ownership of trust assets, the judgment in *Todd v Todd*, was issued after *Tucker*. In *Todd v Todd*, Rothman J. of the Quebec Court of Appeal denied the statement in article 4 of the testator's will that she was bequeathing the 'ownership' of the trust property to her three daughters, who were the beneficiaries. Rothman J. held that the Supreme Court of Canada in 1982 in *Tucker* decided that the trustees, but not the beneficiaries, were the owners of trust property while the trust lasted. Moreover, in this case the testator intended to nominate the trustees as the owners of the trust property, given the fact that she, in her will, expressed the clear intention to convey her property to executors and trustees and authorized the executors and trustees the fullest powers of administration and control over the trust property. Rothman J. addressed that "[t]his, in my view, is the key to the interpretation of the intention of the testator and the critical distinction between a trust and a substitution – the right of access to

³³² *Tucker*, *supra* note 325 at 272-73.

³³³ Michel Benoit, "The Development of the Concept of Pension Trust under Quebec Civil Law" (1998) 17 *Estates, Trusts & Pensions Journal* 203 at 210.

the property conveyed by the testator under the will and the power to administer and control that property.”³³⁴

B. Regulations of Ownership of Trust Property in the CCQ

The third step of the transition of the concept of ownership occurred in 1994 when the CCQ came into effect and replaced the CCLC. The CCQ denied the trustee’s ownership of trust property, with the reason that it was unable to endorse common law dual ownership in Quebec law. However, “the drafters acknowledged that the ownership of the trust property does not vest in the revenue beneficiaries and therefore they provided in art. 1261 of the CCQ that it constitutes a patrimony by appropriation, autonomous and distinct from that of the settlor, trustee or beneficiary and in which none of them has any real right.”³³⁵ The significance of article 1261 of the CCQ was confirmed for the first time in *Royal Trust Corp. of Canada v Webster*, which was decided by Judge Carol Cohen of the Quebec Superior Court in August 2000. Acting as the final step of the transition of trust ownership in Quebec law, the CCQ³³⁶ plays a significant role in several aspects, including fixing the concept of ownership, i.e. a separate patrimony by appropriation, and developing the trust in Quebec law.

(1) The CCQ’s significance in stipulating the notion of patrimony by appropriation

(a) Notion of patrimony by appropriation

³³⁴ Todd, *supra* note 326 at 1185.

³³⁵ Stavert, *supra* note 319 at 140.

³³⁶ The chapter on trusts in the Code, from arts. 1260 to 1298, is divided into the following five sections: I - Nature of the Trust (arts. 1260 to 1265); II - Various Kinds of Trusts and their Duration (arts. 1266 to 1273); III - Administration of the Trust (arts. 1274 to 1292); IV - Changes to the Trust and to the Patrimony (arts. 1293 to 1295); and V - Termination of the Trust (arts. 1296-1298).

The most significant contribution made by the CCQ is that it regulated the notion of patrimony by appropriation in order to introduce the trust into Quebec law without adopting dual ownership.

Before characterizing the trust as a patrimony by appropriation in article 1260, the CCQ first adopts the modern theory that patrimony can be divided or appropriated to a purpose in article 2. It states that “[e]very person has a patrimony. The patrimony may be divided or appropriated to a purpose, but only to the extent provided by law”.³³⁷ In relation to legal persons, article 302 regulates that legal person in Quebec law also “[have] a patrimony which may, to the extent provided by law, be divided or appropriated to a purpose. It also has the extra-patrimonial rights and obligations flowing from its nature”.³³⁸ Moreover, the CCQ adopts Lepaulle’s theory that “*a trust is an appropriation of assets*”³³⁹ but the assets are “*in nobody’s patrimonium*”³⁴⁰. It confirms the ownerless status of the trust property in article 915, which stipulates that “[p]roperty belongs to persons or to the State or, in certain cases, is appropriated to a purpose.”³⁴¹ In other words, when property is appropriated, no one owns it. These stipulations laid the foundation for the proposal of the concept of patrimony by appropriation.

In article 1260, the CCQ regulates the trust and its nature of patrimony by appropriation. It states that a trust is “[a]n act whereby a person, the settlor, transfers property from his patrimony to another patrimony constituted by him which he appropriates to a particular purpose

³³⁷ *Supra* note 316, art. 2 CCQ.

³³⁸ *Ibid*, art. 302.

³³⁹ Pierre Lepaulle, “An Outsider’s View Point of the Nature of Trusts” (1928) 14 Cornell Law Quarterly 52 at 55.

³⁴⁰ *Ibid* at 58.

³⁴¹ *Supra* note 316, art. 915 CCQ.

and which the trustee undertakes, by his acceptance, to hold and administer”.³⁴² The notion of patrimony by appropriation accommodates the hybrid proprietary nature of the trust and harmonizes it with the civilian property system in Quebec.

According to this notion, when the trust property “is transferred by the settlor to the trustee for a stated purpose and the trust is accepted by the trustee, it becomes a ‘patrimony’, i.e., property which is separate and distinct from that of the settlor, the trustee and the beneficiary, and which the trustee is bound to ensure is effected to the purpose for which it was appropriate.”³⁴³ The act of assigning a purpose is central to the constitution of the trust because the appropriation of the patrimony requires the property to be transferred in trust, which thus ensures the settlor be divested of his property. In this way, although the settlor may also be involved in the administration of the trust and maybe benefit from the trust, he abandons his ownership over the trust property through transferring the property to a patrimony in which he has no real right. This is confirmed by article 1261 of the CCQ. Therefore, the property of the trust is separated from the respective patrimony of the settlor and becomes ownerless since neither the trustee nor the beneficiary is vested with a real right for a personal benefit.

The trustee does not have the same right as a real owner under the concept of patrimony by appropriation since he only has the right to hold and administer the trust property. As Cantin Cumyn states: “[u]nlike the titulary of a right, the administrator invested with a power is legally bound to act in the interest of another or to carry out the purpose for which the power was

³⁴² *Ibid*, art. 1260.

³⁴³ Benoit, *supra* note 333 at 210-11.

attributed to him.”³⁴⁴ Additionally, the beneficiary does not hold the ownership of the trust property either. For the duration of the trust, the beneficiary has no real right in the property. He has only a personal right to demand the benefit or the payment that he has been granted in the constituting act.³⁴⁵ The beneficiary can claim the remaining property only at the termination of the trust. Therefore, the nature of the trustee’s right is the power to manage the trust property and that of the beneficiary’s right is to receive the benefits of the trust. Neither the trustee nor the beneficiary is the owner of the trust property that makes up the trust patrimony and the trust is not considered a person.³⁴⁶

As a result, the reception of patrimony by appropriation has been interpreted as a clear rejection of dual ownership. As Professor J.E.C. Brierley addressed, this reception was “couched as one appropriated to a purpose ... in order to avoid any suggestion of having imported the duality of title.”³⁴⁷ The concept of patrimony by appropriation exemplifies the idea that an owner of property has expressed an intention to assign a particular purpose to property rather than to acknowledge its apprehension (*appréhension*) or *occupatio*, by some other person. Namely, the trust property may be expressed to be effected to a particular purpose. This kind of regulation determines that the notion of patrimony is a different starting premise to the trust concept compared to dual ownership under common law trusts.

(b) Rights and obligations of the settlor, trustees and beneficiaries under the notion of

³⁴⁴ Madeleine Cantin Cumyn, “The Legal Power” (2009) 17:3 European Review of Private Law 345 at 352-53.

³⁴⁵ Fortin, *supra* note 180 at 293.

³⁴⁶ Cantin Cumyn, “The Legal Power”, *supra* note 344 at 357.

³⁴⁷ John E.C. Brierley, “The New Quebec Law of Trust: The Adaption of Common Law Thought to Civil Law Concepts” in Glenn H. Patrick, ed, *Droit québécois et droit français: communauté, autonomie, concordance* (Cowansville: Les Édition Yvon Blais, 1993) 383 at 383.

patrimony by appropriation

Although the notion of patrimony by appropriation rejects the transplant of dual ownership, it assigns the rights and obligations between the settlor, trustee and beneficiary in a way to ensure that the trust in Quebec law plays the same role as the trust under common law.

Firstly, with respect to the rights of the settlor, although he loses the ownership of the property transferred to a trust, he may have connections to the trust that extend beyond the role of creator.³⁴⁸ Pursuant to article 1275 of the CCQ, the settlor may be a trustee, “but he shall act jointly with a trustee who is neither the settlor nor a beneficiary.”³⁴⁹ Moreover, the settlor can be a beneficiary according to article 1281, in that he could “reserve the right to receive the fruits and revenues or even, where such is the case, the capital of the trust, even a trust constituted by gratuitous title, or share in the benefits it procures”.³⁵⁰

Even not being one of the trustees or beneficiaries, pursuant to article 1282, “the settlor may reserve for himself the power to appoint the beneficiaries or determine their shares, or confer it on the trustees or a third person” in discretionary trusts.³⁵¹ In other words, the power of appointment involves the power to choose the beneficiaries from a determined class, for instance, from heirs in a personal trust or from retired employees in a private trust. Moreover, in personal trusts, the power of appointment can be conferred and therefore be exercised by the trustees or a third person if it is stated clearly in the constituting act. No matter who, pursuant to article 1283, “[t]he person holding the power to appoint the beneficiaries or determine their

³⁴⁸ Fortin, *supra* note 180 at 294.

³⁴⁹ *Supra* note 316, art. 1275 CCQ.

³⁵⁰ *Ibid.*, art. 1281.

³⁵¹ *Ibid.*, art. 1282.

shares exercises it as he sees fit. He may change or revoke his decision for the requirements of the trust.”³⁵² The discretion gives the settlor a right to delay the determination of particular beneficiaries who shall receive the trust property. Nevertheless, the settlor “may not appoint beneficiaries for his own benefit”.³⁵³

With regards to the rights and obligations of the trustee, in Quebec law, the rights of a trustee are not real rights in the trust property, but fall into the scope of full administration of the property with corresponding obligations. Pursuant to article 1275, when a trust is created, the settlor is divested of the property and the trustee is thereby charged with the administration of the trust.³⁵⁴ Although according to the notion of patrimony by appropriation neither the trustees nor the beneficiaries have any real right in the property, the CCQ nevertheless entitles the trustees the powers necessary to manage and administer the trust property which is enumerated in article 1278. It reads as follow:

A trustee has the control and the exclusive administration of the trust patrimony, and the titles relating to the property of which it is composed are drawn up in his name; he has the exercise of all rights pertaining to the patrimony and may take any proper measure to secure its appropriation.

A trustee acts as the administrator of the property of others charged with full administration.³⁵⁵

In other words, the trustee has all the rights or powers pertaining to the patrimony except the real rights in the trust property. He has full control and exclusive administration of the trust property to the extent that the administration is necessary or useful in the interest of the trust or the beneficiary. The trustee may “alienate the property by onerous title, charge it with a real right or

³⁵² *Ibid.*, art. 1283.

³⁵³ *Ibid.*

³⁵⁴ *Ibid.*, art. 1275.

³⁵⁵ *Ibid.*, art. 1278.

change its destination and perform any other necessary or useful act, including any form of investment”.³⁵⁶ The powers to manage and administer the trust property tie the trustee to the property of the trust in Quebec law. It is important to note that the relationship between the trustee and the trust property is a power relationship, rather than an ownership relationship as adopted in common law.³⁵⁷

As the constraints on the full powers of administration, the trustee shall undertake corresponding obligations, i.e. fiduciary duties. Actually the trust is not created until the trustee accepts his fiduciary duties.³⁵⁸ According to article 1308, the trustee “shall act within the powers conferred on him [and] shall comply with the obligations imposed on him by law or by the constituting act”.³⁵⁹ He “shall preserve the property and make it productive, increase the patrimony or appropriate it to a purpose, where the interest of the beneficiary or the pursuit of the purpose of the trust requires it”.³⁶⁰ This means that no trustee may “mingle the administered property with his own property”³⁶¹ or “use for his benefit the property he administers or information he obtains by reason of his administration except with the consent of the beneficiary or unless it results from the law or the act constituting the administration”³⁶². Moreover, the trustee shall act with prudence, diligence, honesty, and in the best interests of the beneficiary. He may not “exercise his powers in his own interest or that of a third person or place himself in a position where his personal interest is in conflict with his obligations as administrator. If the

³⁵⁶ *Ibid*, art. 1307.

³⁵⁷ Madeleine Cantin Cumyn, “The Trust in a Civilian Context: The Quebec Case” (1994) 3 *Journal of International Trust and Corporate Planning* 69 at 69.

³⁵⁸ Fortin, *supra* note 180 at 294-95.

³⁵⁹ *Supra* note 316, art. 1308 CCQ.

³⁶⁰ *Ibid*, art. 1306.

³⁶¹ *Ibid*, art. 1313.

³⁶² *Ibid*, art. 1314.

administrator himself is a beneficiary, he shall exercise his powers in the common interest, giving the same consideration to his own interest as to that of the other beneficiaries”.³⁶³ The trustee shall “without delay, declare to the beneficiary any interest he has in an enterprise that could place him in a position of conflict of interest and of the rights he may invoke against the beneficiary”.³⁶⁴

Nevertheless, this does not mean the trustee is the debtor of the beneficiary, “given that his or her own property is not subject to the performance of the obligations as trustee.”³⁶⁵ Moreover, “within the limits of his powers, [the trustee] is not personally liable towards third persons with whom he contracts when he acts in the name of the beneficiary or the trust patrimony. [He is liable only] if he binds himself in his own name, subject to any rights they have against the beneficiary or the trust patrimony.”³⁶⁶ “Unless the third persons were sufficiently aware of that fact or unless the obligations contracted were expressly or tacitly ratified by the beneficiary.”³⁶⁷ In addition, the trustee “is not liable for loss of the property resulting from a superior force or from its age, its perishable nature or its normal and authorized use”.³⁶⁸

Lastly, with respect to the rights of the beneficiary, according to article 1284 of the CCQ, throughout the duration of the trust, a beneficiary “has the right to require, according to the constituting act, either the provision of a benefit granted to him or the payment of both the fruits

³⁶³ *Ibid*, art. 1310.

³⁶⁴ *Ibid*, art. 1311.

³⁶⁵ Fortin, *supra* note 180 at 294.

³⁶⁶ *Supra* note 316, art. 1319 CCQ.

³⁶⁷ *Ibid*, art. 1320.

³⁶⁸ *Ibid*, art. 1308.

and revenues and the capital or of only one of these”.³⁶⁹ “The beneficiary of the fruits and revenues is entitled to the net income of the administered property from the date determined in the act giving rise to the administration or, if no date is determined, from the date of the beginning of the administration or that of the death which gave rise to it.”³⁷⁰ In addition to achieving benefits from the trust property, the beneficiary has the right to supervise the administration of the trust. The beneficiary may “take action against the trustee to compel him to perform his obligations or to perform any act which is necessary in the interest of the trust, to enjoin him to abstain from any action harmful to the trust or to have him removed”.³⁷¹ The beneficiary may also “replace the administrator or terminate the administration, particularly by exercising his right to require that the property be returned to him on demand”.³⁷²

Moreover, it is worth noting that “[t]he right of the beneficiary is transferable and can be seized by a beneficiary’s creditor, unless the constituting act states to the contrary”.³⁷³ Therefore, although the beneficiary has the right to require the performance of the trustee’s fiduciary duties and to take an action in damages against the trustee for maladministration³⁷⁴, he is more than an ordinary creditor, “in whose case such remedies do not lie”.³⁷⁵ As explained by Professor John E.C. Brierley,

[t]he price to be paid, in embracing the trust, is to admit the proposition that a patrimony can be not only affected to a purpose but also be without a titulary and that, as a consequence, the juridical characterisation of *the actors, trustee and beneficiary, must be conceived as more than that of debtor and creditor*. This is not so much an

³⁶⁹ *Ibid*, art. 1284.

³⁷⁰ *Ibid*, art. 1348.

³⁷¹ *Ibid*, art. 1290.

³⁷² *Ibid*, art. 1360.

³⁷³ Fortin, *supra* note 180 at 297.

³⁷⁴ *Supra* note 316, art. 1343 CCQ.

³⁷⁵ Brierley, *supra* note 347 at 396.

incoherence in general theory as it is a bold step necessary to free the trust from the seemingly intractable grip of traditional understanding. It extends known concepts to do the new work that the trust implies.³⁷⁶

Therefore, vis-à-vis the trustee, the juridical situation of the beneficiary is certainly not an ordinary creditor and varies according to the type of trust. In a personal trust, the beneficiary's right is limited to a right to claim what the constituting act has granted him or her. In connection to this limited right, "the beneficiary does not, in principle, assume any liability with respect to the creditors of the settlor or of the trustee acting *ex officio*"³⁷⁷.³⁷⁸ In a discretionary trust, either private or personal, the juridical situation of the people who may be designated as beneficiaries is more precarious. They are only potential beneficiaries since their designation is uncertain and depends on the choice of the trustee. Therefore, they "can, at the utmost, demand that the trustee be compelled, in accordance with the constituting act, to exercise the obligation to choose the beneficiaries ... In a social trust, the public has no right to the benefits arising out of the trust. The individuals who can benefit are not, strictly speaking, beneficiaries; they are only persons through whom the goals of the trust are realized".³⁷⁹ In addition, pursuant to article 1287, the people who have the right to supervise the trustee's administration are the persons or bodies designated by law.³⁸⁰

(2) The CCQ's significance in developing the trust in Quebec law

In addition to stipulating the notion of patrimony by appropriation, the CCQ has also

³⁷⁶ *Ibid.*

³⁷⁷ Fortin, *supra* note 180 at 297.

³⁷⁸ Article 1292 of the CCQ gives a different rule, but only in the case of fraud. See *supra* note 316, art. 1292: The trustee, the settlor and the beneficiary are solidarily liable for acts in which they participate that are performed in fraud of the rights of the creditors of the settlor or of the trust patrimony.

³⁷⁹ Fortin, *supra* note 180 at 298.

³⁸⁰ *Supra* note 316, art. 1287 CCQ.

developed the previous code of CCLC in numerous aspects. The main progress it made is:

(a) Introducing a wider and more defined concept of the trust

In comparison to the CCLC, the CCQ introduces a much wider and defined concept of trust into civil law.³⁸¹ It moved the provisions of trusts into Book Four of property. As a consequence, the trust is no longer limited to gifts and estate planning as it was under the CCLC. The trust has been increasingly used for commercial purposes, in particular in the area of investment and finance, on the grounds of the regulation of perpetual duration of such a trust.

In addition, the CCQ classifies the trust into three categories according to its different purpose: personal trusts, private trusts and social trusts.³⁸² The gratuitous personal trust that secures a benefit for a determinate or determinable person is equivalent to the conventional common law trust. The private trust on the other hand is equivalent to the non-charitable purpose trust under common law in some circumstances. This kind of trust can be used in numerous cases and is more flexible than its common law counterpart that is restricted by case law to a certain number of purposes. Non-charitable purpose trusts in common law have a limited application since the courts state that no one can compel the trustee to fulfill his duties, while in Quebec, it is possible for a settlor and his heirs to supervise the management of the trustee to ensure the achievement of the purpose of the trust.³⁸³ More importantly, the Quebec private trust can be used for commercial purposes which keeps with the trend of the modern use of the trust. For instance, mutual fund trusts, pension fund trusts and trusts that potentially embrace a wide range

³⁸¹ Benoit, *supra* note 333 at 207.

³⁸² *Supra* note 316, art. 1266 CCQ.

³⁸³ Aline Grenon, "Of Codifications, the Uniform Trust Code and Quebec Trusts: Lessons for Common Law Canada?" (2004) 23 *Estates, Trusts & Pensions Journal* 237 at 252-53.

of profit-sharing arrangements and other benefit schemes within the context of commercial organizations. Their advantages in a commercial context are apparent because these kinds of trusts can be perpetual in Quebec law. With respect to the social trust, it is the Quebec equivalent of common law charitable purpose but with a wider ambit. This is because it is “constituted for a purpose of general interest, such as a cultural, educational, philanthropic, religious or scientific purpose”.³⁸⁴

Furthermore, specific to the issue of the ownership of a trust, the CCQ changed the characteristic of the fourth rank of beneficiary and thus made it possible for him to enjoy the revenues of the trust. Pursuant to article 1271, which substitutes the old article 932 of the CCLC, revenue beneficiaries of a trust in the third degree or rank are not necessarily capital beneficiaries if the capital beneficiaries have been clearly designated in trust instruments.³⁸⁵

(b) Simplifying the modification of the trust

Another progress made by the CCQ is that it simplifies the modification of the trust. Before the CCQ came into force, a private bill had to be adopted by the National Assembly of Quebec in order to modify a trust under Quebec law. Since January 1, 1994, the date of the coming into force of the CCQ, the modification of a trust has become relatively easy in practice. Article 1294 states that “where a trust has ceased to meet the first intent of the settlor, particularly as a result of circumstances unknown to him or unforeseeable and which make the pursuit of the purpose of the trust impossible or too onerous, the court may, on the application of

³⁸⁴ *Supra* note 316, art. 1270 CCQ.

³⁸⁵ *Ibid.*, art. 1271.

an interested person, terminate the trust”. In the case of a social trust, “the court may substitute another closely related purpose for the original purpose of the trust”. Even when “the trust continues to meet the intent of the settlor”, the court may also amend the provisions of the constituting act if “new measures would allow a more faithful compliance with his intent or favour the fulfilment of the trust”.³⁸⁶

The commentary of the Minister of Justice, written at the time of the adoption of the new *Civil Code of Quebec*, states (translation): This article should, in the future, help in avoiding the sometimes long and onerous procedure for the adoption of a private bill, which represented the only means to resolve problems resulting from outdated trusts, which became problematic, impossible, or too onerous to realize, or whose conditions of administration were deficient.³⁸⁷

Now under the CCQ, the steps needed to modify the trust is as simple as: “a motion must be presented in the Superior Court of Quebec and a notice must be served on the settlor and trustee and, if necessary, the beneficiary, the liquidator of the settlor’s estate, the heirs and any other interested party”.³⁸⁸

In addition to simplifying the steps for modification of a trust, the CCQ also paves the way for Quebec law to make reference to the *Hague Trust Convention*.³⁸⁹ The articles on private international law in the CCQ are based on the *Hague Trust Convention* and the rule with respect to the conflict of laws relevant to the trust are straightforward.³⁹⁰ According to article 3107,

[w]here no law is expressly designated by, or may be inferred with certainty from, the terms of the act creating a trust, or where the law designated does not recognize the institution, the applicable law is that with which the trust is most closely connected. To determine the applicable law, account is taken in particular of the place of administration of the trust, the place where the trust property is situated, the residence or

³⁸⁶ *Ibid.*, art. 1294.

³⁸⁷ Fortin, *supra* note 180 at 315.

³⁸⁸ *Ibid.*

³⁸⁹ Canada is one of the signatories of the *Hague Trust Convention*.

³⁹⁰ Fortin, *supra* note 180 at 315-16.

the establishment of the trustee, the objects of the trust and the places where they are to be fulfilled.³⁹¹

Moreover, pursuant to article 3108, “[t]he law governing the trust determines whether the question to be resolved concerns the validity or the administration of the trust. It also determines whether that law or the law governing a severable aspect of the trust may be replaced by the law of another country and, if so, the conditions of replacement.”³⁹²

Therefore, it is not hard to find that the CCQ modernizes and expands the ambit of the Quebec law of trust. It also fleshes out the concept of trusts and provides it with a theoretical construct compatible with civilian property law concepts. The Quebec experience of trust law is clearly of great value in casting light on the introduction of the trust, in particular in the harmonization of the dual ownership of trust into the civilian property system. The value of the Quebec experience in trust law is best concluded by Professor D.W.M. Waters:

The Civil Code of Quebec has a *fiducie* provision which is meticulously thought through, is broadly comprehensive of the trust elements in its provision, and while offering efficient operation to those among the public who employ it, has satisfied civilians that it has a ready reconciliation with the concepts of the civil law. ... Indeed, civilians in Quebec are proud of the fact, and justifiably so, that the kinds of *fiducie* made possible by the new Code include not only the “personal” *fiducie* for the benefit of persons and the “social” *fiducie* that is created for charitable or similar purposes, but also a trust known in French as the “*fiducie d’utilité privée*”.³⁹³

From the above analyses of the legislations and practices of different jurisdictions, it is not hard to find that “[i]t is not, in reality, essential to a system of trust law that ... the assets should be subject to a dual ownership”.³⁹⁴ The conceptual differences between absolute ownership in the civilian property system and dual ownership under the common law should not

³⁹¹ *Supra* note 316, art. 3107 CCQ.

³⁹² *Ibid.*, art. 3108.

³⁹³ Waters, “The Institution of the Trust”, *supra* 117 at 407.

³⁹⁴ Honoré, “Trusts: The Inessentials”, *supra* note 181 at 9.

constitute an obstacle to the introduction of trusts into the civil law system. Indeed, “there is a much greater acceptance of the idea in modern civil law that the owner of an asset may hold it for the benefit of others rather than for his own.”³⁹⁵ It is unsurprising that civilian jurisdictions, both pure and mixed, have developed a number of legal devices to fulfill at least some of the roles performed by the trust. For instance, the creation of a new legal device with its own patrimony, such as the modern *fiducie* of Quebec law, being a patrimony devoted to particular purposes; and the legal device creating a binary system of a trustee’s fiduciary ownership and beneficiary’s personal claim, such as the case in Scots law. All these devices are possible to introduce and develop the trust law in civilian systems without causing damages to the civilian notion of absolute ownership and legal traditions. In particular, these devices are of a great interest to China, given that they successfully integrate the trust concept into civilian jurisdictions that function the same as the common law trust and yet whose characteristics conform to the fundamental principles of the law of property and the unitary ownership in civil law systems.

³⁹⁵ Matthews, “The Compatibility of the Trust”, *supra* note 158 at 338.

III TRUSTS AND OWNERSHIP OF TRUST PROPERTY IN CHINA

Chapter I and Chapter II examined trust laws, with a focus on ownership, in both common and civil law systems. This comparative study of the trust and its ownership provides lessons and experience for the design of China's own institutions, which seek to mimic the functions of dual ownership found in the civil and common law systems. This study also permits the author to make several recommendations for how Chinese law should be amended. Before proposing amendments to Chinese trust law, Chapter III first contextualizes China's trust. It outlines the basic features of the Chinese trust with a view to showing how these features put in place the essential elements of a trust as seen in international practice, and highlights the theoretical and practical challenges of the Chinese approach. Although this thesis concerns ownership of trust property, this chapter provides other issues to give a clear picture of the Chinese trust law.

Because of the trust's advantages in investment, banking, financing and property management, China took the bold step of introducing the trust in 2001.³⁹⁶ However, as a product of equitable jurisdiction, the trust seemed to be alien to Chinese law, and seemed particularly inconsistent with the Chinese property system. Therefore, China went down a tortuous road upon its introduction of trusts before eventually promulgating the *Trust Law of China* in 2001. However, the *Trust Law of China* deliberately leaves open the fundamental question of the introduction of dual ownership of trust property, which results in a number of limitations in the Chinese legislation. For instance, the ambiguous ownership of trust property, the outstanding

³⁹⁶ Dan Qi & Lin Yan, "The Study of Modern Trust Function" (2005) 4 Journal of Shaoyang University Social Science) 44 at 44 [translated by author].

nature of the beneficiary's rights, and a confusing registration system of trust property all bedevil efforts to analyse Chinese trust law. In this chapter, the author first investigates the history and the notion of trust in China and considers the difficulties in the introduction of the trust. Based on this analysis, the following section presents a detailed examination of the *Trust Law of China* and the limitations of the Chinese trust system. This conceptual baseline will provide a better understanding of dual ownership of trust property in China.

1. History of Trusts in China, Legal Reforms of Chinese Trust Business, and the Drafting of *Trust Law of China*

The notion of trusts never found root in dynastic China. Inheritance was predominantly regulated by customary law, and there was little room for testamentary disposition by individuals. Therefore, a trust-like device was not needed for property owners to entrust the management of their property to others.³⁹⁷ Starting from 1911 however, when dynastic rule ended and the Chinese Nationalist Party took over control of the country, the so-called trust business was operated by trust institutions. At the beginning and lasting until the communist victory in the Civil War, trust institutions were set up inside banks in the form of a department of trust. For example, in 1919, the Shanghai branch of *Ju Xing Cheng* Bank established the department of trust to manage trust business. In addition to the trust institutions within banks, several governmental trust institutions were also enacted, such as the Central Trust Bureau and Shanghai *Xingye* Trust. With them came regulation, an example being the two significant trust rules promulgated by the Central Trust Bureau in 1945: the *Issuing Measures of Securities and Trust*

³⁹⁷ Lusina Ho, "Trust laws in China: History, ambiguity and beneficiary's rights" in Lionel Smith, ed, *Re-imagining the Trust: Trusts in Civil Law* (Cambridge: Cambridge University Press, 2012) 183 at 186-87.

and *Regulations of Issuing Investment Trust and Securities*.³⁹⁸ Finally, a third type of trust institution was broadly adopted at that time, and still exists as a major use of trust in China: ‘the trust company’. In August 1921, the first trust company, *Tongshang* Trust Company of China was established in Shanghai; and quickly within the next month, twelve similar trust companies³⁹⁹ sprang up in China.⁴⁰⁰

These trust companies came to a halt after the Communist takeover in 1949. They obtained a new lease of life in 1979, when China adopted an open-door policy for foreign trade and investment. The trust companies provided the government with flexible avenues for financing outside the rigid state-planned budget.⁴⁰¹ The first trust and investment company of the People’s Republic of China, China International Trust and Investment Corporation, was established with the approval of State Council in Beijing on October 4th, 1979.⁴⁰² From 1979 to 1988, a number of provinces, cities and financial institutions set up their own trust and investment companies and the number of trust and investment companies rose up to more than one thousand.⁴⁰³ This period also saw the introduction of a new form of commercial trust, the collective capital trust, only operable by trust companies.⁴⁰⁴ Moreover, charitable trusts were also established in this period. The first charitable trust, the *Soong Ching Ling* Foundation, was

³⁹⁸ Hong Wu, Xiling Jia & Sheng Cheng, *Trust Law: Legal Regulations of the Development of China Trust Market* (Shanghai: Lixin Accounting Press, 2003) at 25-26 [translated by author].

³⁹⁹ The 12 trust companies are Zhongyi, Zhongguo, Shangye, Tongyi, Dazhonghua, Zhongyang, Shanghai, Tongshang, Shenzhou, Zhongwai, Huasheng, and Shanghai Yunshi.

⁴⁰⁰ Yufen Huo, *Discussions of Trust Law* (Beijing: China University of Political Science and Law Press, 2003) at 27-28 [translated by author].

⁴⁰¹ *Ibid* at 28-29.

⁴⁰² Jingxin Guan, *Trust Law & Practice in China* (Beijing: Law Press China, 2008) at 25 [translated by author].

⁴⁰³ Jinshu Tang & Ran Chao, *Financial Trust and Financial Market* (Tianjin: Tianjin science and Technic Press, 1990) at 29 [translated by author].

⁴⁰⁴ Lusina Ho, Rebecca Lee & Jin Jinping, “Trust Law in China: a critical evaluation of its conceptual foundation” in Lusina Ho & Rebecca Lee, eds, *Trust Law in Asian Civil Law Jurisdictions: A Comparative Analysis* (Cambridge: Cambridge University Press, 2013) 80 at 80.

formed in 1982. Over the following decade, a number of these kinds of trusts were rapidly established. In order to regulate these charitable trusts, State Council promulgated *the Measures for the Management of Foundations*⁴⁰⁵ in September 1988.⁴⁰⁶

As the flexibility of trusts in managing the assets of others has been recognized in common law jurisdictions, China sought to develop its legal infrastructure to include trusts. As the 1980s wore on, this project acquired new urgency: with the development of international trade and the growth of private wealth in China after its economic reforms, China was keen to adopt the trust as a means of establishing a modern system for the fiduciary management of assets. Nevertheless, due to the lack of adequate legal norms and theoretical supports, the trust developed in an unusual way. Due to the government's active promotion of this form of fiduciary management, Chinese trusts rapidly over-expanded, as the trust and investment companies operated an excessively broad scope of business, including traditional banking activities such as the management of retail and corporate loans and deposits.⁴⁰⁷ More specifically, the trust companies engaged in trust loans, trust investments and trust deposits, activities which were effectively deposit-taking activities authorized by the lack of legal requirements for the segregation of investor and trustee funds. Whatever profits or losses accrued went to the trust and investment companies rather than to the customers.⁴⁰⁸

Facing this highly irregular expansion of trusts, the Chinese government tried to correct

⁴⁰⁵ *The Measures for the Management of Foundations*, (promulgated by Order No. 18 of the President of the People's Republic of China on September 27, 1988, and was abolished and replaced by *The Regulations for the Management of Foundations* on June 1, 2004).

⁴⁰⁶ Huo, *supra* note 400 at 29-30.

⁴⁰⁷ Guan, *supra* note 402 at 11.

⁴⁰⁸ Ho, "History, ambiguity and beneficiary's rights", *supra* note 397 at 188-89.

its inappropriate promotion and to regulate trust business via legal reforms, i.e. a series of ‘rectifications’ dating from 1988 to 1998 in which trust institutions were separated from banks.⁴⁰⁹ The number of trust and investment companies was reduced to two hundred and thirty-nine by the end of 1998. The fifth, and most significant rectification, took place 1998, when the *Guangdong International Trust and Investment Corporation* was acquired by the *People’s Bank of China* (hereinafter referred to as *PBC*)⁴¹⁰ and forced into liquidation. A further culling of companies with payment difficulties, insufficient assets, or poor management, reduced the number of trust and investment companies to fifty-eight.⁴¹¹

The experience of the four rectifications had become one of the primary reasons for initiating the drafting of the *Trust Law of China* in 1993.⁴¹² In other words, the *Trust Law of*

⁴⁰⁹ Dongsheng Su, “Trusts and Taxes” (2006) 11 *Times Finance* 7 at 7 [translated by author].

⁴¹⁰ The People’s Bank of China was established on December 1, 1948 based on the consolidation of the Huabei Bank, the Beihai Bank and the Xibei Farmer Bank. In September 1983, the State Council decided to have the PBC function as a central bank. *The Law of the People’s Republic of China on the People’s Bank of China* adopted on March 18, 1995 by the 3rd Plenum of the 8th National People’s Congress has since legally confirmed the PBC’s central bank status. With the improvement of the socialist market economic system, the PBC, as a central bank, will play an even more important role in China’s macroeconomic management. The amended *Law of the People’s Republic of China on the People’s Bank of China*, adopted by the 6th meeting of the Standing Committee of the 10th National People’s Congress on December 27, 2003, provides that the PBC performs the following major functions: (1) Drafting and enforcing relevant laws, rules and regulations that are related to fulfilling its functions; (2) Formulating and implementing monetary policy in accordance with law; (3) Issuing the Renminbi and administering its circulation; (4) Regulating financial markets, including the inter-bank lending market, the inter-bank bond market, foreign exchange market and gold market; (5) Preventing and mitigating systemic financial risks to safeguard financial stability; (6) Maintaining the Renminbi exchange rate at adaptive and equilibrium level; Holding and managing the state foreign exchange and gold reserves; (7) Managing the State treasury as fiscal agent; (8) Making payment and settlement rules in collaboration with relevant departments and ensuring normal operation of the payment and settlement systems; (9) Providing guidance to anti-money laundering work in the financial sector and monitoring money-laundering related suspicious fund movement; (10) Developing statistics system for the financial industry and responsible for the consolidation of financial statistics as well as the conduct of economic analysis and forecast (11) Administering credit reporting industry in China and promoting the building up of credit information system; (12) Participating in international financial activities at the capacity of the central bank; (13) Engaging in financial business operations in line with relevant rules; (14) Performing other functions prescribed by the State Council.

⁴¹¹ Guan, *supra* note 402 at 11-12.

⁴¹² Before the *Trust Law of China*, the Chinese trust was regulated by the *Provisional Regulations on the Management of Financial Trust Investment Institutions* promulgated in April 1986 and the *Provisional*

China aimed at regulating trust business.⁴¹³ After three years of efforts, the working group proposed a draft on November 29, 1996, which included six chapters: general provisions, the relationship between trust parties, special provisions of charitable trust, trust companies, legal liabilities of trust, and supplementary provisions.⁴¹⁴ Nevertheless, how exactly China regulates trust companies is a subject that still needs further research. For the purposes of this thesis however, suffice it to note that, since the supervision of the trust business should be governed by public law, the specific way in which the trust industry is governed is ontologically separate from the laws surrounding the institution of trust. This fact is recognized in other civilian jurisdictions such as Japan, South Korea and Taiwan.⁴¹⁵ The Law Committee of National People's Congress revised the legislative purpose of the *Trust Law of China* to regulate the relationship between trust parties and deleted the provisions regarding trust companies in the draft.⁴¹⁶

After almost eight years of drafting, China promulgated the *Trust Law of China* (the third draft) on 28 April 2001. The act came into effect on 1 October 2001,⁴¹⁷ making China one of the first socialist and civil law jurisdictions to have introduced a domestic law of trusts. This trust law has attracted much attention, both in China and overseas. "First, [because] there is much hope in China that the Law will put in place an important legal instrument for the professional management of assets and, ultimately, for modernising China's financial

Regulations on the Capital Management of Financial Trust Investment Institutions promulgated in December 1986.

⁴¹³ Xiaoming Zhou, *Trust Legislation: Theories and Practice* (Beijing: China Legal Publishing House, 2012) at 24 [translated by author].

⁴¹⁴ *Ibid* at 24-25.

⁴¹⁵ Wu, Jia & Cheng, *supra* note 398 at 41.

⁴¹⁶ Zhou, *supra* note 413 at 25, 27.

⁴¹⁷ China is not a party to the Hague Convention. Therefore the *Trust Law of China* contains no provision on choice of law rules and it is applicable to trust activities carried out in China.

infrastructure. Second, [because] the Chinese experiment might be useful to civil law jurisdictions generally as an illustration of how thorny issues regarding the reception of the common law trust can be tackled,”⁴¹⁸ analysts have been examining the law upon a number of grounds. It is worth noting that when the *Trust Law of China* was drafted, the initial and most typical kind of trust existing in China was the commercial trust used as a mechanism to facilitate investment, financing and property management, not the trust that used for management of intergenerational wealth. Therefore, as shown in the history of the development of trusts in China, trusts created by wills can barely be found in Chinese law.

In addition to the *Trust Law of China*, further legislation and regulations have been passed to provide for the use of the trust in financial arrangements focusing on the regulation of trust and investment companies.⁴¹⁹ For example, *Law of the People’s Republic of China on Securities Investment Funds*⁴²⁰, *The Measures for the Administration of Trust Companies*⁴²¹, and *The Rules for Administration of Collective Capital Trust Plans*⁴²². Thanks to its these laws and regulations, China’s trust business has rapidly developed: its total revenue has increased from RMB 21.9 billion in 2007 to 63.8 billion in 2012 (an increase of 191.32%), and total industry profits have increased from 15.8 billion in 2007 to 44.1 billion in 2012 (an increase of

⁴¹⁸ Lusina Ho, *Trust Law in China* (Hong Kong: Sweet & Maxwell Asia, 2003) at 2.

⁴¹⁹ Lingyun Gao, *The Misunderstood Trust: Principles on Trust Law* (Shanghai: Fudan University Press, 2010) at 277 [translated by author].

⁴²⁰ *Law of the People’s Republic of China on Securities Investment Funds*, (Adopted at the fifth Session of the Tenth National People’s Congress, promulgated by Order No. 9 of the President of the People’s Republic of China on October 28, 2003, and effective as of June 1, 2004).

⁴²¹ *The Measures for the Administration of Trust Companies*, Decree of the China Banking Regulatory Commission No. 2, adopted at the 55th chairmen’s meeting on December 28, 2006, and hereby promulgated and shall go into effect as of March 1, 2007.

⁴²² *The Rules for Administration of Collective Capital Trust Plans*, Decree of the China Banking Regulatory Commission No. 3, adopted at the 55th chairmen’s meeting on December 28, 2006, and hereby promulgated and shall go into effect as of March 1, 2007. They are amended at the 78th chairmen’s meeting on December 17, 2008.

179.11%).⁴²³

2. Notion of Trusts in China and Difficulties in the Introduction of Trusts

From these notions of the history of trusts in China, it is not hard to see that China has gone through a number of difficulties in introducing trusts, and that its notion of trust has evolved differently from common law's conception of trust. As shown, trust companies are the main type of trust in China, and have played a significant role in the development of the market for trusts in China. This section first analyzes the concept of trust in China, in particular focusing on the trust companies, and then examines the main hurdles in the introduction of trusts.

A. Notion of Trusts in China – Trust and Investment Companies

In contrast to the concept of trust under common law, the Chinese trust is more similar to a contractual relationship between a trust company⁴²⁴ and its clients. Most of trust disputes are therefore contractual in nature.⁴²⁵ Where the *Trust Law of China* is silent on salient factors, Chinese courts have not hesitated to invoke the *Contract Law of the People's Republic of China*⁴²⁶ (hereinafter referred to as *Contract Law of China*) to fill whatever normative gaps there might be.⁴²⁷ Indeed, it is only as a result of inaccurate transliteration that trust and investment

⁴²³ Zhi Xin Asset Management Institute, *Annual Report on the Development of China's Trust Industry (2013)* (Beijing: Social Sciences Academic Press, 2013) at 89-90 [translated by author].

⁴²⁴ Since 2007, CBRC has changed the name of trust and investment companies to trust companies. Nowadays, the two types of China's financial institutions that are engaged in profit-trust activities are trust companies and fund management companies. See Xiaoming Zhou, *Trust System: Theories and Practice* (Beijing: China Legal Publishing House, 2012) at 34.

⁴²⁵ Gao, *supra* note 419 at 258.

⁴²⁶ *Contract Law of the People's Republic of China*, (Adopted at the Second Session of the Ninth National People's Congress, promulgated by Order No. 15 of the President of the People's Republic of China on March 15, 1999, and effective as of October 1, 1999).

⁴²⁷ See *Yanxin Co. Ltd v Huabao Trust and Investment Co. Ltd*, Shanghai Intermediate People's Court Case No. 226

companies in China could be seen as operating ‘trust’ businesses. Even though there is a possibility for the existence of non-commercial private trusts such as inheritance trusts, no such trusts have ever really existed in China.⁴²⁸ The Chinese trust is mainly used at the public level for charitable donations and foundations. At the commercial level, Chinese trusts are used for securitization and collective investment schemes such as investment and pension funds, via dual-use trust and investment companies. This section discusses the development, regulations and duties of those trust and investment companies.

Trust and investment companies are non-bank financial institutions that were revived after China’s adoption of the Open Door Policy in 1978. As noted, the rapid “growth of private wealth in China, ... [spurred] demand for a greater variety of investment vehicles beyond bank deposit, or private investment in the stock market or in real estate.”⁴²⁹ In response to this demand, trust and investment companies sprang into existence, encouraged by guidelines issued by the State Council and the PBC in 1980.⁴³⁰ In the early days of the Open Door Policy, the primary business of the trust and investment companies was to act as agents⁴³¹ for the government in raising funds or extending credit in order to circumvent the rigid central budget. In other words, trust and investment companies served macroeconomic ends. A good example of

of 2004 (16 March 2005); on appeal from *Yanxin Co. Ltd v Huabao Trust and Investment Co. Ltd*, Case No. 201 of 2004 (25 November 2004).

⁴²⁸ Gao, *supra* note 419 at 241.

⁴²⁹ Ho, *Trust Law in China*, *supra* note 418 at 10.

⁴³⁰ *Ibid* at 3-4.

⁴³¹ The existing Chinese legislation on agency can be found mainly in some civil laws, for instance, *General Principles of the Civil Law of the People’s Republic of China*, *Contract Law of the People’s Republic of China*, as well as some administrative regulations such as *Temporary Regulations on the Foreign Trade Agent System*, and the judicial interpretation of the Supreme People’s Court.

General Principles of the Civil Law regulates the civil agent system in a single section in Chapter IV. According to Article 63 of *General Principles of the Civil Law*, “Citizens and legal persons may perform civil juristic acts through agents. An agent shall perform civil juristic acts in the principal’s name within the scope of the power of agency. The principal shall bear civil liability for the agent’s acts of agency”.

this is found the establishment of *Yi Fu* China Investment Cooperation in 1987.⁴³²

Since 1982, the Chinese government has sought to regulate the trust and investment companies through numerous regulations of the China Banking Regulatory Commission⁴³³ (hereinafter referred to as CBRC). In 1997, the first national regulation on investment funds was promulgated in the form of the *Administration of Securities Investment Funds Tentative Procedures*⁴³⁴. This regulation only allows closed-end investment funds. It was subsequently supplemented and extended by the Pilot Projects for Opened Securities Investment Funds Procedures⁴³⁵, which was enacted by the Chinese Securities Regulatory Commission in 2000. The Chinese Securities Regulatory Commission, the regulatory body for investment funds, also issued *Implementing Rules and Circulars* from time to time to provide detailed rules on how the implementation of trust-related regulations was to take place. Moreover, in order to fulfill China's accession commitments to the World Trade Organization, the Chinese Securities Regulatory Commission promulgated the *Establishment of Fund Managed Companies with Foreign Equity Participation Rule*⁴³⁶ on 1 June 2002, coming into effect 1 July 2002. Those regulations contain provisions that broadly accord with the principles of common law trusts, such

⁴³² Wu, Jia & Cheng, *supra* note 398 at 159.

⁴³³ See the official website of the CBRC: <http://www.cbrc.gov.cn/english/index.html>. The main functions of the CBRC are: (1) Formulate supervisory rules and regulations governing the banking institutions; (2) Authorize the establishment, changes, termination and business scope of the banking institutions; (3) Conduct on-site examination and off-site surveillance of the banking institutions, and take enforcement actions against rule-breaking behaviors; (4) Conduct fit-and-proper tests on the senior managerial personnel of the banking institutions; (5) Compile and publish statistics and reports of the overall banking industry in accordance with relevant regulations; (6) Provide proposals on the resolution of problem deposit-taking institutions in consultation with relevant regulatory authorities; (7) Responsible for the administration of the supervisory boards of the major State-owned banking institutions; and Other functions delegated by the State Council.

⁴³⁴ *Administration of Securities Investment Funds Tentative Procedures*, the State Council Securities Commission, 14 November 1997.

⁴³⁵ *Pilot Projects for Opened Securities Investment Funds Procedures*, Chinese Securities Regulatory Commission, 8 October 2000.

⁴³⁶ *Establishment of Fund Managed Companies with Foreign Equity Participation Rule*, Chinese Securities Regulatory Commission, 1 June 2002, effected on 1 July 2002.

as the segregation of the trust assets from the general assets of the custodian. Nevertheless, they failed to set out the private law rights and duties of the trust parties. There was for example, no provision on fiduciary duties of reasonable prudence, which is typically required to address agency problems in collective investment funds.⁴³⁷ Consequently, and despite regulation of the micro-economic aspects of trust and investment companies, a normative gap persisted until 2007.

In order to fill this gap, a 2007 administrative regulation called *Measures for the Administration of Trust Companies*⁴³⁸ was published. It has since acted as the main legal resource regulating trust and investment companies. The *Measures for the Administration of Trust Companies* establishes the trust and investment company as either a limited liability or a share-holding company.⁴³⁹ Moreover, the *Measures for the Administration of Trust Companies* regulates the establishment of a trust company. It sets out seven basic components that must be constituted in order to establish a trust company: an article of association, eligible shareholders, registered capital, a minimum of RMB 300 Million Yuan or the equivalent,⁴⁴⁰ an eligible board of directors, an organizational structure and a risk control system, and finally, business premises approved and stipulated by the CBRC.⁴⁴¹ Buffered by the promulgation of the *Rules Governing Trust Companies*, the quantity of assets managed by the trust companies expanded from RMB 940 billion in 1997 to 7.47 trillion in 2012.⁴⁴² At the end of 2011, there were sixty-five trust companies and more than ten thousand practitioners in China.⁴⁴³

⁴³⁷ Ho, *Trust Law in China*, *supra* note 418 at 12.

⁴³⁸ *Administration of Trust Companies*, *supra* note 421.

⁴³⁹ *Ibid.*, art. 6.

⁴⁴⁰ *Ibid.*, art. 10.

⁴⁴¹ *Ibid.*, art. 8.

⁴⁴² *Supra* note 423 at 106.

⁴⁴³ Tongqing Zhang, *The practice of Law in Trust Business* (Beijing: China Legal Publishing House, 2012) at 6

Because the trust companies have been largely used in financial and banking sectors in China, the CBRC has the power to regulate and supervise trust companies and investment companies and related activities.⁴⁴⁴ The CBRC, for example, can decide whether to approve the establishment of a trust company that is a financial institution and grant the business a license.⁴⁴⁵ Likewise, the subsequent establishment of company branches requires further approval from the CBRC,⁴⁴⁶ and in the event of bankruptcy, the trust and investment company must choose to apply for approval to the CBRC in order to obtain recourse from the People's Court for Bankruptcy. Alternatively, the CBRC can apply directly to the court for either the restructuring or the liquidation of the trust company.⁴⁴⁷

The essence however, of the trust and investment company's regulatory structure has been the separation of the trust company's own assets from assets entrusted to it. As stated in article 29 of the *Measures for the Administration of Trust Companies*, "[a] trust company shall clearly separate its own assets from entrusted property and manage them in different accounts, and manage entrusted property of different clients in different accounts."⁴⁴⁸ The aim of this statute was to prevent entrusted assets from falling into the hands of the personal creditors of the trust company. Therefore, the entrusted property must be separated from the liquidated assets and will be transferred to a new trustee upon the current trustee's bankruptcy.⁴⁴⁹ The relationship between the trust company and the beneficiaries is organized by laws, regulations, and the

[translated by author].

⁴⁴⁴ *Administration of Trust Companies*, *supra* note 421, art. 5.

⁴⁴⁵ *Ibid.*, art. 7.

⁴⁴⁶ *Ibid.*, art. 11.

⁴⁴⁷ *Ibid.*, art. 14.

⁴⁴⁸ *Ibid.*, art. 29.

⁴⁴⁹ *Ibid.*, art. 15.

stipulations in trust documents.⁴⁵⁰ Moreover, because the trust company acts in the interest of the beneficiaries, it owes these persons fiduciary duties. Namely, the trust and investment company must manage and administer the trust assets as an ordinary businessperson would manage his or her own affairs. It must, in other words, act honestly and in a way that is credible, prudent, efficient, and which will maximize the benefits of the beneficiaries.⁴⁵¹ The trust company cannot seek illegitimate gain by taking advantage of its trustee status or use the trust property other than for trust purposes.⁴⁵² It must not benefit from its position or provide financial assistance to the connected persons, such as guarantees or transferring assets.⁴⁵³ The trust company must bear in mind conflicts of interests⁴⁵⁴ and the principle of confidentiality⁴⁵⁵.

In conclusion, trusts have been fitted into other laws in China, particularly contract law. This is because Chinese trusts have mainly been in the form of trust and investment companies, and the nature of their relationship between the trust companies and their clients has been contractual. Due to the absence of legal theory and practice of the trust in early years following the Open Door, trust companies over-expanded and took on the role of other, non-trust financial institutions such as banks. Despite crackdowns on specific firms and the implementation of regulations especially during the period from 1988 to 1998, trusts have grown as commercial institutions. There has been very little, if any, demand in China to adopt the trust for use in family succession.

⁴⁵⁰ *Ibid*, art. 4.

⁴⁵¹ *Ibid*, art. 24.

⁴⁵² *Ibid*, art. 34.

⁴⁵³ *Ibid*, art. 33.

⁴⁵⁴ *Ibid*, art. 25.

⁴⁵⁵ *Ibid*, art. 27.

B. Difficulties in the Introduction of Trusts

The differences in the notion of trust between the common law and Chinese law caused difficulties in the introduction of trusts in China. Unlike the common law's real conception of trust, China's contract-based model cannot explain why trust property is immune from a trustee's private creditors. Given that a contract binds only the two parties who signed it, this conception also makes it hard to include the three parties of settlors, trustees and beneficiaries, required to form a trust.⁴⁵⁶

In addition to this fundamental difference in notion, a number of other difficulties also exist. Central to them is the main difficulty that lies in the different conceptions in the ownership of trust property. There is a widespread belief within common law jurisdictions that the trust is a special product of the common law tradition, in particular, of dual ownership.⁴⁵⁷ According to this reasoning, in common law, the ownership of trust property is divided into legal ownership and equitable ownership, with neither of them wholly absolute. On the other hand, in China, ownership is absolute and indivisible; and no separate equitable jurisdiction has ever existed. Furthermore, the common law trust is comprised of both obligation and property, whereas ownership in China is grounded solely upon the nature of property. Thus, it is hard to introduce the trust concept to China where ownership contains no nature of obligation.⁴⁵⁸ Those difficulties are reflected in the drafting of the *Trust Law of China* and result in a number of limitations. Before examining the main legal limitations however, the author will first analyze the statutory

⁴⁵⁶ Yihu Tang, *Studies of Trust Property Right* (Beijing: China University of Political Science and Law Press, 2005) at 266 [translaed by author].

⁴⁵⁷ Gretton, "Trusts Without Equity", *supra* note 170 at 600.

⁴⁵⁸ Tony Honoré, "On Fitting Trusts into Civil Law Jurisdictions" (2008) 27 University of Oxford Legal Research Paper Series at 10 <<http://ssrn.com/abstract=1270179>>.

provisions of the *Trust Law of China*.

3. Regulations of the Trust Law of China

The *Trust Law of China* is comprised of seventy-four articles in seven chapters.⁴⁵⁹ General provisions are found in Chapter I (articles 1 to 5), the creation of the trust in Chapter II (articles 6 to 13), trust property in Chapter III (articles 14 to 18); regulations concerning the trust parties – settlor, trustee and beneficiary – in Chapter IV (articles 19 to 49), modification to and termination of a trust in Chapter V (articles 50 to 58), and the charitable trust in Chapter VI (articles 59 to 73). Supplementary provisions are found in the last chapter (article 74). This section provides a detailed examination of the provisions of the *Trust Law of China*, focusing on the regulations of Chapter IV, i.e. the rights and obligations of the settlor, trustee and beneficiary.

A. Definition, the Creation, and the types of Trusts in China

Chapter I, article 2 defines the trust as a situation where “the settlor, based on his faith in trustee, entrusts his property rights to the trustee and allows the trustee to, according to the will of the settlor and in the name of the trustee, administer or dispose of such property in the interest of a beneficiary or for any intended purposes.”⁴⁶⁰ It stipulates the property right of the trustee as a wider legal definition of the notion of property where it relates to the ownership of property to competing rights. It embraces real property, the interest arising from a real property and personal property.⁴⁶¹

⁴⁵⁹ The governmental English translation of the *Trust Law of China* is set out in an annex.

⁴⁶⁰ *Trust Law of China*, *supra* note 1, art. 2.

⁴⁶¹ Mark Hsiao, *Financial Regulation of Banking Derivatives, Securitizations and Trusts in China* (Toronto: Carswell, 2009) at 224.

The *Trust Law of China* anticipates only an express trust, which requires certain formalities to be completed.⁴⁶² According to the provisions of Chapter II, in order to establish the trust, both the trust's lawful purposes⁴⁶³ and definite property⁴⁶⁴ must be specified. Furthermore, the creation of the trust must be done in writing,⁴⁶⁵ in the form of stipulated trust contracts, testament or other instruments according to the relevant administrative regulations.⁴⁶⁶ Unlike the requirement of the declaration of trust under common law, Chinese law only recognizes the trust created in writing and excludes the creation of trust by oral declaration or by conduct. So, a refusal invalidates any application of the doctrines regarding resulting or constructive trusts.⁴⁶⁷ While the Supreme People's Court recognized *de facto* trust relationships without a trust contract in *Appeal Case of Trademark Ownership Dispute between Guangdong Light Industrial Products Import & Export Corporation and Hong Kong TMT Trading Co. Ltd*⁴⁶⁸, subsequent statutory changes to the *Trust Law of China* have removed this option for trust formation and affirmed a writing requirement.⁴⁶⁹ Professor Lusina Ho stated that the requirement of written documents

⁴⁶² *Ibid* at 225.

⁴⁶³ *Trust Law of China*, *supra* note 1, art. 6.

⁴⁶⁴ *Ibid*, art. 7.

⁴⁶⁵ *Ibid*, art. 8.

⁴⁶⁶ There is no specific explanation of what are "other documents specified by laws and administrative regulations" in either legal or judicial interpretations. Currently, the contract of funds regulated in the *Law of the People's Republic of China on Funds for Investment in Securities* is the only kind of written document found in relevant laws and regulations.

⁴⁶⁷ See George Gleason Bogert et al, *Cases and Text on the Law of Trusts*, 9th ed (New York: Foundation Press, 2012) at 2. In Common Law, "trusts are classified according to the manner of their origin. When created by some manifestation of intent by the settlor they are called express trusts; when based upon an inferred or presumed intent of the settlor they are named resulting trusts; and when established by court action to work justice, without regard to the intent of the parties, they are denominated constructive trusts. Trusts created by a provision in a will are called testamentary trusts, and trusts created by lifetime transfers of property are called inter vivos or living trusts. The settlor may retain for himself, or give another, the power to revoke a trust, in which case the trust is called a revocable trust. If the settlor declares that the trust may not be revoked, the trust is referred to an irrevocable trust".

⁴⁶⁸ *Appeal Case of Trademark Ownership Dispute between Guangdong Light Industrial Products Import & Export Corporation and Hong Kong TMT Trading Co. Ltd*, Supreme People's Court (1998) Zhi Zhong Zi No. 8 "Civil Judgment".

prevent an *inter vivos* trust from being established by a unilateral declaration. “As a consequence, Chinese settlors may not declare themselves to be trustees as might their counterparts in common law jurisdictions, for they cannot enter into a trust contract or indeed any contract with themselves.”⁴⁷⁰ However, there are no express provisions prohibiting settlors from being trustees. Given this reality, and similar practice across various common law jurisdictions, it would seem evident that Chinese law ought to allow settlors to be trustees. Therefore, in this case, the requirement for written documents is problematic insofar as it prevents settlors from being trustees. That said, this issue might be still solved with reference to the miscellaneous category of ‘other written instruments required by laws or regulations’. As of yet no such documents have yet been authorized and this option is not open without the promulgation of necessary laws and regulations.⁴⁷¹

Another difference of the Chinese trust law from its common law counterpart is that transfer requirement during the establishment of trusts under common law, i.e. the transfer of relevant property to the trustee, is ignored in Chinese law. There is no express provision for such a transfer in the *Trust Law of China*, and it is implicit in numerous articles that the transfer is not necessary.⁴⁷² With the absence of express provision and the presence of provisions that are consistent with the contrary position, it is clear that a Chinese trust can be established without the transfer of the trust property. It is possible that some may simply involve a trust contract, whereby the settlor continues to retain the ownership of the trust property.

⁴⁶⁹ Shaohua Liu, *Trust Principle in the Practice of Civil and Commercial Law* (Beijing: Law Press China, 2012) at 213 [translated by author].

⁴⁷⁰ Ho, *Trust Law in China*, *supra* note 418 at 78.

⁴⁷¹ Ho, Lee & Jin, *supra* note 404 at 82.

⁴⁷² The issue of the transfer of trust property will be discussed in details in sub-section, 4 (Uncertainties of the Chinese Trust System) A. “*Ambiguous Ownership of Trust Property*”.

Moreover, unlike the common law rules surrounding trusts, Chinese law makes no express reference to perpetuity rules or an express provision to render void a trust obtained by fraud or duress. Should fraud occur, the victim is obliged to refer to the broad provision of the principle of voluntariness, fairness, and good faith in article 5 of the *Trust Law of China*. He may also rely on article 52(1) of the *Contract Law of China* when the trust is established by a trust contract or pursuant to article 22 of the Succession Law when the trust is established by will.⁴⁷³ He may not however, rely on the *Trust Law of China*.

In addition to the requirements found in articles 6, 7 and 8, the *Trust Law of China* codifies the three certainties of an express trust in article 9. These are: certainty of intention, certainty of subject matter and certainty of object. Uncertainty of any of these requirements will cause the trust to be invalid. A more specific, though non-exhaustive enumeration of failure conditions is found in article 11:

(1) The purposes of the trust constitute a violation of laws or administrative regulations, or impair public interest; (2) The property under trust cannot be fixed; (3) The settlor creates the trust with unlawful property or with property which, according to this law, may not be used for creating a trust; (4) The trust is created specially for the purpose of taking legal actions or for recovering debts; (5) The beneficiary or beneficiaries cannot be determined; and (6) Other circumstances stipulated in laws or administrative regulations.⁴⁷⁴

From those regulations, we can see that in order to create a trust in China, the intention of establishing the trust should be ascertained in writing, and that the trust property should be legal and ascertained. Moreover, there must be certainty of object. However, unlike the common

⁴⁷³ *Contract Law of China*, *supra* note 426, art. 52: A contract is invalid under any of the following circumstances: (1) either party enters into the contract by means of fraud or coercion and impairs the State's interests. Article 22 of the Law of Succession of China: Wills shall manifest the genuine intention of the testators; those made under duress or as a result of fraud shall be void.

⁴⁷⁴ *Trust Law of China*, *supra* note 1, art. 11.

law rules of trusts, the transfer of trust property is not provided in the *Trust Law of China*. In respect to different types of trust, the Chinese law only recognizes the type of trust established for the benefit of a beneficiary or a specified purpose in article 2, and deals with charitable trusts in Chapter VI. Doctrines of resulting and constructive trusts have rightly not been introduced into China because the Chinese trust is established by a written contract, a will or other documents.⁴⁷⁵

Once the trust is created successfully, it comes into being as a legal device to manage trust property. In order to facilitate the management and administration of the trust, the main purpose of the *Trust Law of China* is to “regulate trust relationship, to standardize trust acts, [and] to protect the lawful rights and interests of the parties involved in a trust.”⁴⁷⁶ Therefore, Chapter IV, adopting many articles, stipulates the legal rights and obligations of the settlors, trustees, and beneficiaries.

B. Rights and Obligations of the Settlor

This section examines the Chinese regulations of the rights and obligations of the settlor, points out its unique provisions, and analyzes the reasons for these provisions as well as problems arising from these provisions.

In the *Trust Law of China*, a settlor is defined as “a natural person, a legal person, or an organization established in accordance with law, that has full capability for civil conduct.”⁴⁷⁷⁴⁷⁸

⁴⁷⁵ Ho, “History, ambiguity and beneficiary’s rights”, *supra* note 397 at 192-93.

⁴⁷⁶ *Trust Law of China*, *supra* note 1, art. 1.

⁴⁷⁷ *Ibid*, art. 19.

⁴⁷⁸ The definition of natural person with full capability for civil conduct can be found in article 11 of the *General*

The settlor is conferred a broad information power which allows him to access “the administration, use and disposition of, and the income and expenses relating to, his trust property [and] to request the trustee to give explanations in this regard. [He also has] the right to check, transcribe or duplicate the trust accounts related to his trust property and other documents drawn up in the course of dealing with trust business”.⁴⁷⁹

Moreover, the settlor is given the power to ask the trustee to modify his administration when the methods for the administration “are not favorable to the realization of trust purposes or do not conform to the interests of the beneficiary [or] due to special reasons unexpected at the time the trust is created”.⁴⁸⁰ Article 22 provides a similar remedy of restitution to the settlor, allowing him to annul the trustee’s disposition and restore trust property when the trustee disposes of the trust property in breach of the purposes of the trust, or causes losses to the trust property due to his departure from his administrative duties or improper handling of trust business. In these cases, it is the settlor who can “apply to the People’s Court for annulling such disposition [and] to ask the trustee to restore the property to its former state or make compensation.”⁴⁸¹ While this right is subject to statutory limitations, it has to be exercised “within one year beginning from the date [the settlor] comes to know or should have known the

Principles of Civil Law, which states that “a citizen aged 18 or over shall be an adult. He shall have full capacity for civil conduct, may independently engage in civil activities and shall be called a person with full capacity for civil conduct. A citizen who has reached the age of 16 but not the age of 18 and whose main source of income is his own labour shall be regarded as a person with full capacity for civil conduct.” The definition of legal person is found in article 37 of the General Principles of Civil Law, stating that: “A legal person shall have the following qualifications: (1) establishment in accordance with the law; (2) possession of the necessary property or funds; (3) possession of its own name, organization and premises; and (4) ability to independently bear civil liability”.

⁴⁷⁹ *Trust Law of China*, *supra* note 1, art. 20.

⁴⁸⁰ *Ibid*, art. 21.

⁴⁸¹ *Ibid*, art. 22.

reason for annulling the disposition, [otherwise] such right shall cease to exist”.⁴⁸² Alternatively, the settlor also has the right to “dismiss the trustee according to the provisions in the trust documents or apply to the People’s Court for dismissing him”.⁴⁸³ In relation to charitable trusts, the settlor can file a lawsuit at the People’s Court when “the public welfare administration authority violates” the provisions of the *Trust Law of China*.⁴⁸⁴

The settlor is also granted the powers to resolve uncertainties or disputes relating to the administration of the trust. In the absence of a provision in the trust instrument, the settlor has the right to give consent to transactions conducted by the trustee between his own property and trust assets at fair market price,⁴⁸⁵ to resolve disagreements between joint trustees in the administration of trust,⁴⁸⁶ or to enter into a supplementary agreement with the trustee and the beneficiary to authorize remuneration to the trustee.⁴⁸⁷ He can also consent to the trustee’s resignation⁴⁸⁸ or to appoint a new trustee after termination of the trustee’s appointment.⁴⁸⁹ Moreover, upon the termination of the trust, as a consequence of the trustee’s removal, bankruptcy, loss of legal qualifications, resignation, dismissal or other circumstances stipulated in laws or administrative regulations, the settlor has the right to approve the report submitted by the trustee on his administration of the trust.⁴⁹⁰

Additionally, it is even possible for the settlor to terminate the trust through consultation

⁴⁸² *Ibid.*

⁴⁸³ *Ibid.*, art. 23.

⁴⁸⁴ *Ibid.*, art. 73.

⁴⁸⁵ *Ibid.*, art. 28.

⁴⁸⁶ *Ibid.*, art. 31.

⁴⁸⁷ *Ibid.*, art. 35.

⁴⁸⁸ *Ibid.*, art. 38.

⁴⁸⁹ *Ibid.*, art. 40.

⁴⁹⁰ *Ibid.*, art. 41.

with the trustee and beneficiary.⁴⁹¹ Alternatively, when the settlor is the trust's sole beneficiary, and in the absence of provision in the trust instrument, he can revoke the trust himself.⁴⁹² Moreover, according to article 51, "the settlor may replace the beneficiary or dispose of his right to benefit from the trust under one of the following circumstances: (1) the beneficiary commits a major tort against the settlor; (2) the beneficiary commits a major tort against the other co-beneficiaries; (3) the change or disposition wins the consent of the beneficiary; and (4) other circumstances stipulated in the trust documents."⁴⁹³ Upon termination of the settlor is also entitled to receive the trust property in secondary priority after the beneficiary and his successors.⁴⁹⁴

It is worth noting that some of the settlor's rights are uniquely regulated in Chinese law and have been questioned by jurists. In particular, article 2 of the *Trust Law of China* allows for the possibility of title to trust property being held by the settlor, rather than by the trustee. This possibility is totally unknown in common law and is highly unusual internationally. Likewise, the settlor's right to replace the beneficiary, given by article 51, usually does not exist in common law unless the settlor expressly reserved such right in trust documents. Moreover, the settlor's right to supervise the trust's management and administration, or to modify or even annul the trustees' disposition of trust property, enunciated in articles 20, 21 and 22, is usually not to be found in common law jurisdictions either, because the settlor automatically loses those rights when he transfers the trust property to others. As Ho explains,

in relation to self-dealing transactions, given that any harm or loss will be suffered by

⁴⁹¹ *Ibid*, art. 53.

⁴⁹² *Ibid*, art. 50.

⁴⁹³ *Ibid*, art. 51.

⁴⁹⁴ *Ibid*, art. 54.

the beneficiaries rather than the settlors, it is difficult to see why the latter should be given the right to authorize such transactions. [Moreover,] it is not inconceivable that a settlor who has settled property upon trust may wish to revoke his or her gift. The risk of giving powers to the settlor as above is that he or she may exercise these powers arbitrarily, or in preference for his or her own rather than the beneficiaries' interests.⁴⁹⁵

The unique regulations of the settlor's rights imply that most Chinese trusts are alter ego trusts.⁴⁹⁶ However, when the settlor is not the sole beneficiary, granting the same rights to both settlors and beneficiaries, or more specifically, retaining the beneficiary's rights as to settlors, as regulated in article 49, will cause conflicts between those two parties. Although these conflicts can be solved by the court, the efficiency of the trust's management will be decreased. Even though the trust contract may restrict the settlor's act, whether expressly or by necessary implication, such restrictions operate only at the level of obligation and do not invalidate juridical acts.⁴⁹⁷ Therefore, the Chinese legislation grants too much power to the settlors and fails to provide sufficient restraints on the powers: It decreases the efficiency of trust management, increases the cost of trust administration, and confuses the trust with other legal institutions such as agency. While in other legal systems the trust, at least in comparison to other institutions has the advantage of being able to allow the trustee to manage the trust property in his own name and be immune from the interference of others, the current Chinese system reduces this advantage, and, consequently, weakens the attractions of the trust.⁴⁹⁸

C. Rights and Duties of the Trustee

In this section, the author first indicates the trustee's capacity, as well as the situations

⁴⁹⁵ Ho, *Trust Law in China*, *supra* note 418 at 115-16.

⁴⁹⁶ Gao, *supra* note 419 at 267.

⁴⁹⁷ Reid, "Conceptualising the Chinese Trust", *supra* note 189 at 11.

⁴⁹⁸ Tang, *supra* note 456 at 59.

for the trustee needed to assign duties and resign. After that, the author will present a detailed analysis of the obligations and rights of the trustee.

In Chinese law, “[a] trustee shall be a natural person or legal person who has full capability for civil conduct.”⁴⁹⁹ Unlike settlors, unincorporated organizations cannot be trustees. The original trustee of the trust is appointed by the settlor upon the entry into the trust contract or the trustee’s acceptance of the trust.⁵⁰⁰ Under the *Trust Law of China*, a trustee may be removed only under limited circumstances, specifically “[w]here the trustee disposes of the trust property against the purposes of the trust or commits gross negligence in administering, using or disposing of the trust property”.⁵⁰¹ In addition, Chinese trust law only leaves an extremely limited scope for a trustee to resign, which is considered to restrict the trustee’s power.⁵⁰² The trustee cannot resign in the absence of the consent of the settlor and beneficiary, even when there are enough trustees to manage the trust.⁵⁰³ It is unclear whether this stipulation is mandatory or can be overridden by express provision in the trust instrument. This is different from the common law regulation where the trustee has the discretion to resign. Moreover, while most of the jurisdictions give the court power to permit a trustee to resign, no such provision can be found under the *Trust Law of China*. When the trustees’ appointment can be terminated according to article 39, the trust property will be kept on hold *ad hoc* until a new trustee is appointed.⁵⁰⁴ In the case of joint trustees, if some of the trustees’ appointments are terminated,

⁴⁹⁹ *Trust Law of China*, *supra* note 1, art. 24.

⁵⁰⁰ *Ibid*, art. 8.

⁵⁰¹ *Ibid*, art. 23.

⁵⁰² Gao, *supra* note 419 at 270.

⁵⁰³ *Trust Law of China*, *supra* note 1, arts. 38, 66.

⁵⁰⁴ *Ibid*, art. 40.

the other trustees will continue the administration.⁵⁰⁵

(1) Trustee's duties

In managing the trust property for the beneficiary's interests, the trustees "have the obligation to pay the beneficiary benefits from the trust with the limits of the trust property".⁵⁰⁶

(a) The regulations of fiduciary duties and their limitations

The *Trust Law of China* enumerates the fiduciary duties of trustees. Article 25 states that "[t]he trustee shall abide by the provisions in the trust documents and handle trust business for the best interests of the beneficiary; [and] in administering the trust property, the trustee shall be careful in performing his duties and fulfill his obligations with honesty, good faith, prudence and efficiency."⁵⁰⁷ However, at least one Chinese commentator argues that this provision reduces the standard of trustee's duty from that required from the good administrator to that of a normal administrator taking care of his own property.⁵⁰⁸ This compares unfavorably with the Chinese trust's common law counterparts, which generally subjects all trustees to general duty of care and prudence while also taking into account the knowledge and experience of individual trustees. These jurisdictions thus place demand a more rigorous duty of care from professional trustees.⁵⁰⁹ Furthermore, there is no elaboration in article 25 or other provisions that explain what standard of prudence is expected from the trustee, and whether the standard varies depending on the type

⁵⁰⁵ *Ibid.*, art. 42.

⁵⁰⁶ *Ibid.*, art. 34.

⁵⁰⁷ *Ibid.*, art. 25.

⁵⁰⁸ Haiyong Yu, *How to Localize the British and American Law on Trust Property in China* (Beijing: China University of Political Science and Law Press, 2011) at 162 [translated by author].

⁵⁰⁹ Ho, *Trust Law in China*, *supra* note 418 at 106-07.

of trust involved. In this light, it is suggested that the Chinese law should be amended with reference to other jurisdictions and include a specific explanation of the standard of trustees' duty of care.

In addition to the general rule of the fiduciary duties in article 25, the *Trust Law of China* also lists other specific obligations of the trustee. It provides that “except obtaining remuneration according to the provisions of this Law, the trustee may not seek interests for himself by using the trust property”⁵¹⁰ or “convert the trust property into his own property”⁵¹¹. Additionally, the trustee is prohibited from self-dealing or merging the trust property with his personal property. As it states, the trustee may not make transactions “between his own property and trust assets or between the trust assets of different settlors, unless it is otherwise stipulated in the trust documents.”⁵¹² The trustee “shall administer the trust property separately from his own property and keep separate accounting books, and he shall do the same with regard to the trust property of different settlors”.⁵¹³ These regulations comply with the rule of the independence of the trust property and prevent the trust property from falling into the hands of trustees' personal creditors.⁵¹⁴ It provides that the trust property comprises the initial settled property, and property lawfully and unlawfully obtained from the use, management or disposal of the initial property.⁵¹⁵ Furthermore, despite the absence of express stipulation in the *Trust Law of China*, it is implied in article 25 that the trustee should also be prohibited from engaging in any business in competition

⁵¹⁰ *Trust Law of China*, *supra* note 1, art. 26.

⁵¹¹ *Ibid*, art. 27.

⁵¹² *Ibid*, art. 28.

⁵¹³ *Ibid*, art. 29.

⁵¹⁴ However, there is no provision of the segregation of trust fund capital and interest in Chinese trust law. The importance of such segregation is not recognized because non-commercial private trusts have not been adopted in China.

⁵¹⁵ *Trust Law of China*, *supra* note 1, art. 14.

with the trust.

However, the Chinese provisions of the trustee's fiduciary duties seem to be vague, and there are both gaps and overlaps in the provisions as compared to systematic and comprehensive regulations in common law. The *Trust Law of China* only stipulates the general rules of fiduciary duties in article 25 in very broad terms and provides a sporadic list of specific fiduciary duties. It is unclear whether a trustee has any fiduciary duties in situations that are not specially regulated. Moreover, Chinese law does not recognize the duty of impartiality, given that most of the trusts in China are short-term, alter ego trusts with no complicated conflicts of interests existing between the beneficiaries.⁵¹⁶ Another outstanding issue, or gap in the regulation of fiduciary duties, is the burden of proof. The *Trust Law of China* has no provision stating how the burden of proof should be allocated. According to article 64 of the *Civil Procedure Law of the People's Republic of China* (hereinafter referred to as *Civil Procedure Law of China*)⁵¹⁷, it would be the duty of settlors or beneficiaries as the claimant to provide evidence in support of his allegations against the fiduciary. This would be extremely difficult in practice for the settlors or beneficiaries to prove that the trustee has not acted in the best interest of the beneficiaries.⁵¹⁸ Therefore, an express provision should be regulated in Chinese trust law to shift the burden of proof to trustees in order to show that they indeed have acted in the best interest of the beneficiaries.

⁵¹⁶ Gao, *supra* note 419 at 283.

⁵¹⁷ *Civil Procedure Law of the People's Republic of China*, (Adopted at the Fourth Session of the Seventh National People's Congress, promulgated by Order No. 44 of the President of the People's Republic of China on April 9, 1991, and amended by the Decision of October 28, 2007, on Amending the Civil Procedure Law of the People's Republic of China). Article 108 states that "The following conditions must be met when a lawsuit is brought: (1) the plaintiff must be a citizen, legal person or any other organization that has a direct interest in the case".

⁵¹⁸ Xueping Chen & Jingjun Dou, *Trustees' Rights and their Balance Mechanism under the Trusts* (Beijing: Law Press China, 2008) at 222 [translated by author].

As to the problem of overlaps in the provisions, an example can be found in article 22. It states that “[w]here the trustee disposes of the trust property in breach of the purposes of the trust, or causes losses to the trust property due to his departure from his administrative duties or improper handling of trust business, [he shall] restore the property to its former state or make compensation.”⁵¹⁹ However, the duty of “departure from his administrative duties” involves an “improper handling of trust business”, thus creating an overlap and potential conflict. As if to add to the confusion, these two phrases are not defined, creating difficulties in the implementation of the law. For instance, it is unclear whether an improper handling arises when the trustee has not breached any specific duty but has nonetheless caused loss to the trust property, such as when he has made an unprofitable investment.

(b) The regulations of duty to act personally and their limitations

In addition to the fiduciaries duties, the trustee is also required to act personally when carrying out the trust’s business. According to article 30, “[t]he trustee shall handle trust business himself.”⁵²⁰ With regard to this duty, questions arise as to when the delegation should be allowed, what duties a trustee owes in the delegation, and when the trustee should be liable for the acts of a third party. As to the first question, delegation under the *Trust Law of China* is essentially allowed on the ground of necessity, i.e. for when the trustee “has to do so for reasons beyond his control [or] where the trust documents provide otherwise”.⁵²¹ This regulation is much more restrictive than the common law approach that permits delegation on the ground of

⁵¹⁹ *Trust Law of China*, *supra* note 1, art. 22.

⁵²⁰ *Ibid.*, art. 30.

⁵²¹ *Ibid.*

prudence or simply grants a general power of delegation to the trustees. For example, the Trustee Act 2000 of England and Wales provides that “[a] trustee is not liable for any act or default of the agent, nominee or custodian unless he has failed to comply with the duty of care applicable to him.”⁵²² “Given the increasing sophistication and specialization of modern commercial transactions, it is submitted that a broad power of delegation ought to be granted to trustees.”⁵²³ The Chinese approach runs a serious risk of hindering the trustee’s administration of the trust.

With respect to the second question, Chinese law is silent. Nevertheless, in order to prevent trustees from abandoning their duties through provided delegation, it ought to be a given that the trustees should exercise due care and skill in appointing and supervising the agent. This is a position adopted by most jurisdictions. As to the third question, namely when should a trustee be liable for the acts of a third party, the Chinese law provides in article 30 that the trustee “shall bear the responsibility for the acts committed by that person in handling such affairs.”⁵²⁴ This is different from international practice, which holds a trustee liable for the agents’ defaults if he fails to exercise care or prudence. In light of these discrepancies, the *Trust Law of China* should be amended to make it better fit with international practice.⁵²⁵

(c) The regulations of duty to account and their uncertainty

Another duty of the trustee is the duty to keep accurate accounts. Legislatively, this done by stipulating that the trustee shall “at regular intervals every year, report to the settlor and beneficiary on the administration and disposition of the trust property and the income and

⁵²² *Trustee Act 2000*, *supra* note 92, s 23(1).

⁵²³ Ho, *Trust Law in China*, *supra* note 418 at 109.

⁵²⁴ *Trust Law of China*, *supra* note 1, art. 30.

⁵²⁵ Ho, *Trust Law in China*, *supra* note 418 at 109.

expenses relating to the property.”⁵²⁶ In charitable trusts, the requirement is slightly different: “[t]he trustee shall, at least once a year, make a report on the trust business handled and the status of assets disposed of, and upon acceptance by the trust supervisor, the report shall be submitted to the public welfare administration authority for examination and approval, and the trustee shall announce the report.”⁵²⁷ In applying these provisions, uncertainty arises as to the consequences of the trustee’s failure to discharge such duties. Currently, the only route to obtain remedies for breaches of these duties is to see whether the breaches are falling into the duty regulated by article 22 – improper handling of trust affairs or breach of his management responsibilities. If yes, the trustee is obliged to restore the trust property to its original state or to pay compensation if loss is caused by the breach.⁵²⁸ If no, the result is unclear. Therefore, in order to offer greater clarity to potential beneficiaries, Chinese law ought to be amended based on comparative studies of other jurisdictions and entitle a beneficiary or a settlor the right to compel a trustee to render accounts when the trustee refuses to do so, or to appoint an independent professional or the court to prepare the trust accounts while all relevant costs are borne by the defaulting trustee.⁵²⁹

(2) Trustee’s rights

This section indicates the rights of the trustee under the *Trust Law of China*. It analyses the right to remuneration and the right of indemnity, and examines current limitations of existing regulations. Finally, it proposes amendments to these regulations.

The only benefit that a trustee can anticipate from the management of trust property is

⁵²⁶ *Trust Law of China*, *supra* note 1, art. 33.

⁵²⁷ *Ibid*, art. 67.

⁵²⁸ *Ibid*, art. 22.

⁵²⁹ Ho, *Trust Law in China*, *supra* note 418 at 97-98.

remuneration.⁵³⁰ After the termination of trusts, the trustee is entitled to two means of redress to exercise the right to request remuneration from the trust property: “he may have a lien on the property or raise the request to the owner of the property”.⁵³¹ However, this regulation causes a number of problems: first, a Chinese lien can only be established over movable property.⁵³² The trustee however, could lose this statutory protection if the trust property happens to be real property. In addition, the Chinese concept of lien requires the creditor to be in physical possession of the property.⁵³³ This could cause practical difficulties for a Chinese trustee who may not often be given possession of the property in question. Therefore, it is doubtful whether the imposition of the lien offers the Chinese trustee the same protection as that enjoyed by a common law trustee. In this light, amendments to the Chinese law have been proposed in order to remove restrictions on the type of trust property. Further suggestions advance the notion that the lien of the trustee should be expanded to real estate. Finally, commentators argue that the trustee ought to be entitled to obtain priority repayment from the value of the property as determined by valuation or from the proceeds of sale by auction of the property upon the termination of trust.⁵³⁴

In addition to the right of remuneration, the trustee also has a right of indemnity. Where the trustee effects a payment owed to a third party during the course of discharging his duties as administrator of the trust’s business in advance with his personal property, he has the right to be

⁵³⁰ *Trust Law of China*, *supra* note 1, art. 35.

⁵³¹ *Ibid.*, art. 57.

⁵³² *Property Law of the People’s Republic of China*, (Adopted at the Fifth Session of the Tenth National People’s Congress, promulgated by Order No. 62 of the President of the People’s Republic of China on March 16, 2007, and effective as of October 1, 2007), art. 230.

⁵³³ *Ibid.*

⁵³⁴ Ho, *Trust Law in China*, *supra* note 418 at 102-03.

paid in priority with the trust's properties. Any remaining debts in this circumstance would be borne by the trust property.⁵³⁵ However, a preliminary question to ask is whether the expenses or liabilities are properly incurred or not. According to article 37, the trustee will not be indemnified if the debts owed to a third party or the losses suffered by the trustee are "as a result of his departure from his administrative duties or his improper handling of trust business".⁵³⁶ With respect to this regulation, Professor Ho argues that it is too vague to be of much use. Moreover, she states that the wording of article 37 should be interpreted broadly to refer to "any breach of the trustee's duties as set out in the Trust Law and in the trust instrument".⁵³⁷ Even with this said, article 37 is still more stringent than the approach adopted in international practice. For example, English case law allows a trustee who acts in good faith to be indemnified to the extent that the unauthorized act benefits the trust estate,⁵³⁸ or where such an act was expressly or impliedly consented to by the beneficiaries.

Moreover, another problem is that in order to secure the trustee's right of indemnity, article 37 grants the trustee the right to obtain priority repayment from the trust fund; however, article 37 lacks an explanation of the nature of such a right and how it compares with security interest. In Chinese law, the rights of priority repayment, as opposed to security rights, are rights over debts that are specially protected by laws and regulations. There is an overwhelming opinion within Chinese doctrine that the nature of the right of priority repayment articulated in article 37 is the right to obtain payment from the trust fund, and ranks ahead of the rights of all

⁵³⁵ *Trust Law of China*, *supra* note 1, art. 37.

⁵³⁶ *Ibid.*

⁵³⁷ Ho, *Trust Law in China*, *supra* note 418 at 123.

⁵³⁸ *Vyse v Foster* (1872) 8 Ch. App. 309 at 336-37.

secured and unsecured creditors.⁵³⁹ Support for this argument can be found in an opinion of the Supreme People's Court on article 286 of the *Contract Law of China*, which grants similar right of priority repayment for the price of construction projects and clarifies that such a right ranks ahead of mortgage rights and other rights over debts.⁵⁴⁰

(3) Trustee's powers

In addition to the above-listed rights, the trustee holds powers over the trust property. He holds these powers in order to enable the management and administration of the trust to the same extent as an absolute owner. However, there is no such granting of power to be found in the *Trust Law of China*. The only article that mentions the trustee's powers of administration is article 2. When defining the notion of trust, this article stipulates, in very broad terms, that the trustee is entrusted the settlor's property rights and is allowed to administer or dispose of the trust property in his own name. However, there is no provision that clearly regulates what specific powers the trustee should have, or whether it simply embraces the power to maintain the trust property or also involves the power to invest, lease or insure relevant properties. This is an enormous gap, and requires an amendment to the regulation of trustee's powers.

Another amendment that needs to be made is to the Chinese regulation of the variation of trust administration in article 21 and article 69. It is submitted that these provisions should be revised in order to provide maximum flexibility for the administration of trusts. As Professor Ho suggests, "the requirement of the occurrence of unforeseeable circumstances can be abandoned;

⁵³⁹ Ho, *Trust Law in China*, *supra* note 418 at 124.

⁵⁴⁰ *Reply to the Question Concerning the Right of Repayment of the Price of Construction Projects*, Supreme People's Court, issued on 11 June 2002; came into effect on 27 June 2002.

it could simply be stated that the method for administering the trust could be varied if it is in the interest of the beneficiaries as a whole.”⁵⁴¹ Since there is no express provision that regulates whether articles 21 and 69 are permissive or mandatory, a clarification should be added that the statutory powers under those two articles can be overridden by express provisions in the trust instrument. The *Trust Law of China* is unique in giving the settlor the power to vary the administration of the trust without any judicial scrutiny in article 21 and to adversely change the entitlement of the beneficiaries in article 51. Amendments are also needed to these regulations so as to properly protect the beneficiaries’ interests and to prevent the settlor from abusing the trust.⁵⁴²

In short, a comparison of the regulations of rights and obligations of the settlor as well as the duties imposed on the trustee by the *Trust Law of China* reveal that the Chinese provisions are broadly similar to those found in common law. However, and in contrast to the common law, Chinese law does not seek to preserve the independent discretion of the trustee in acting in a manner that he considers to be in the best interests of the beneficiaries.⁵⁴³

D. The Capacity and Rights of the Beneficiary

In the *Trust Law of China*, the beneficiary is defined as “the person that enjoys the right to benefit from a trust. He may be a natural person, legal person or an organization established according to law”.⁵⁴⁴ Unlike in the case of settlors and trustees, beneficiaries need not have civil capacity, which means infants and unincorporated organizations that do not have legal

⁵⁴¹ Ho, *Trust Law in China*, *supra* note 418 at 130.

⁵⁴² *Ibid* at 131.

⁵⁴³ Ho, Lee & Jin, *supra* note 404 at 89, 91.

⁵⁴⁴ *Trust Law of China*, *supra* note 1, art. 43.

personalities can be beneficiaries. Furthermore, and consistent with international practice, both settlors and trustees can be beneficiaries. In this case however, the trustee/beneficiary may not be the only trustee. There is no provision outlining whether the beneficiary should exist at the time of the trust's formation. However considering that there is no problem should a beneficiary be absent prior to the distribution of trust benefit, the existence of a beneficiary upon the creation of trust does not seem to be required as long as the beneficiary can be identified during the trust's duration. This complies with the both trust's purpose and with Anglo-American law.⁵⁴⁵

Knowing the capacity of the beneficiaries, we can now discuss the rights of the beneficiaries. According to the statute, beneficiaries are entitled to "benefit from a trust beginning from the date the trust becomes effective, unless otherwise stipulated in the trust documents."⁵⁴⁶ In the event that the beneficiary "cannot repay the matured debts, his right to benefit from a trust may be used to repay the debts, except this is restricted by provisions in laws, administrative regulations and trust documents."⁵⁴⁷ As Professor Ho notes, "in this way, the [Chinese] Trust Law permits the creation of American-style spendthrift trusts or English-style protective trusts, which aim at making appropriate provisions to the beneficiaries, but which also restrict them from disposing of the property as they wish."⁵⁴⁸ It is worth noting that the beneficiaries can dispose of this right to benefit: according to article 46, they may either give up this right or instead transfer the right. In the case of co-beneficiaries, according to article 45, "the co-beneficiaries shall enjoy the benefits from a trust according to the provisions in the trust

⁵⁴⁵ Zhou, *supra* note 413 at 125.

⁵⁴⁶ *Trust Law of China*, *supra* note 1, art. 44.

⁵⁴⁷ *Ibid*, art. 47.

⁵⁴⁸ Ho, *Trust Law in China*, *supra* note 418 at 117-18. Also see n 122, according to art. 15, it appears that the Trust Law of China does not permit self-settled spendthrift trust, which involve the settlor as the sole beneficiary or a co-beneficiary of a spendthrift trust.

documents. Where no percentage or methods for distribution of the benefits from the trust are specified in the documents, all the beneficiaries shall enjoy the benefits equally.”⁵⁴⁹ Compared to the common law approach, this Chinese provision is less stringent because it does not require the certainty of beneficiary’s share and allows this to be cured by equal division.⁵⁵⁰

In addition to the right to benefit, beneficiaries can also claim against the trustees pursuant to article 49. This article states that beneficiaries “may exercise the rights that the settlor enjoys as stipulated in article 20 through 23.”⁵⁵¹ This means that the beneficiary retains not only the right to use and dispose of assets in the trust, as well as the income and expenses relating to his trust property, but also that he has the right to check the trust account, ask the trustees to modify their administration, apply to the People’s Court for annulling trustee’s improper disposition, ask the trustee to restore the property, or even dismiss the trustee according to the provisions in the trust documents or by application to the People’s Court. Moreover, the beneficiaries are given powers, again along with the settlor, to help fill gaps in the trust instrument and to facilitate the smooth administration of the trust. In other words, in the absence of provision in the trust instrument, the beneficiaries can give consent to transactions conducted by the trustee between his own property and trust assets at fair market price,⁵⁵² resolve disagreement between joint trustees in the administration of trust,⁵⁵³ give consent to the trustee’s resignation,⁵⁵⁴ and approve the report submitted by the trustee on his administration of the trust

⁵⁴⁹ *Trust Law of China*, *supra* note 1, art. 45.

⁵⁵⁰ Hsiao, *supra* note 461 at 234.

⁵⁵¹ *Trust Law of China*, *supra* note 1, art. 49.

⁵⁵² *Ibid*, art. 28.

⁵⁵³ *Ibid*, art. 31.

⁵⁵⁴ *Ibid*, art. 38.

upon the termination of the trust in certain circumstance.⁵⁵⁵ Additionally, the beneficiary is entitled to appoint another person as the trustee where the person designated in a testament refuses or is unable to act as a trustee pursuant to article 13,⁵⁵⁶ and to appoint a new trustee when the trustee's appointment is terminated according to article 40.⁵⁵⁷ However, Professor Ho denies the wisdom of those two provisions. As she argues "[allowing] a beneficiary to appoint a trustee is to ignore the need for maintaining the crucial check and balance between the trustee and the beneficiaries."⁵⁵⁸

However, the beneficiary's role in the trust relationship in China is significantly different when compared to its common law counterpart. Apart from the right to receive distribution, the beneficiary's entitlements to monitor the trustee and bring actions for breach are granted by way of duplication of the settlor's rights, as discussed earlier. Such duplication suggests that the administration of the Chinese trust will be shadowed by the conflicting interests between the settlor and the beneficiaries: given the lack of statutory guidance in the law as to whose interests should take priority, there is a great risk that under the current legal regime beneficiary's rights could be encroached upon by settlors. Admittedly, this might not be the case in the investment trusts so are prevalent in China in which investors are both settlors and beneficiaries. However, the issue could become prominent if other trusts that are not alter ego trusts, such as family trusts, were to take off in China.⁵⁵⁹

⁵⁵⁵ *Ibid.*, art. 41.

⁵⁵⁶ *Ibid.*, art. 13.

⁵⁵⁷ *Ibid.*, art. 40.

⁵⁵⁸ Ho, *Trust Law in China*, *supra* note 418 at 121.

⁵⁵⁹ Ho, Lee & Jin, *supra* note 404 at 93.

E. Termination of Trusts and the Charitable Trusts

After outlining the regulations of settlor rights and obligations, as well as those of trustees and beneficiaries, the *Trust Law of China* prescribes the termination of trusts and the charitable trusts in the following chapters. In Chapter V, the *Trust Law of China* describes the termination of a trust. In this chapter, the *Trust Law of China* follows the fundamental rule in common law, which holds that a trust cannot fail solely for want of a trustee. The statute provides in article 52 that “[a] trust will not be terminated due to the facts that the settlor or trustee dies, loses his capacity for civil conduct, the trusteeship is dissolved or canceled according to law or he is declared bankrupt, neither will it be terminated due to the fact that the trustee resigns, except it is otherwise stipulated in this Law or the trust documents.”⁵⁶⁰ On the contrary, article 53 lists the consequences under which a trust shall be terminated: “(1) the cause for its termination specified in the trust documents arises; (2) the continuance of the trust goes against the purposes of the trust; (3) the purposes of the trust have been realized or cannot be realized; (4) the parties concerned, through consultation to terminate it; (5) the trust is cancelled; (6) the trust is revoked”,⁵⁶¹ or “[w]here the settlor is the only beneficiary, he or his successor may revoke the trust.”⁵⁶² Upon the termination of the trust, and in absence of any provision of the distribution of trust property in trust documents, “the following order of precedence shall be applied for determining the ownership: (1) the beneficiary or his successor; and (2) the settlor or his successor.”⁵⁶³ If upon termination the trustee is still owed remuneration from the duty of managing the trust property, the trustee “may have a lien on the property or raise the request to

⁵⁶⁰ *Trust Law of China*, *supra* note 1, art. 52.

⁵⁶¹ *Ibid.*, art. 53.

⁵⁶² *Ibid.*, art. 50.

⁵⁶³ *Ibid.*, art. 54.

the owner of the property.”⁵⁶⁴ At that moment, the trustee’s obligation is to “make a liquidation report on the trust business handled. Where the beneficiary or the owner of the property has objections to the report, the trustee shall be exempted from the liability for issues listed in the report, except for the illegitimate acts committed by him.”⁵⁶⁵

There are many issues that can arise from trust termination under Chinese trust law. One major issue arising from regulations dealing with trust termination in relation to the ability of the trust parties to terminate the trust at will is that the current statutes give a strong impression that the drafters of the *Trust Law of China* saw trusts as a form continuing contractual relationship involving three parties. As noted, the trust parties can consent to terminate the trust just as contractual parties terminate their relationship upon agreement. In particular, the settlor is given the most extensive right with respect to termination. Likewise, in breach of trust instrument, similar to the remedies set forth in the *Contract law of China*, the trustee owes duties to both the settlor, who entered into a trust contract with him, and the beneficiaries, who receive benefits under the trust.⁵⁶⁶ That said, the fiduciary duties are different in nature from contract duties insofar as fiduciary duties require the trustee to act in the best interests of the beneficiaries while the contractual duties demand the parties to act reasonably to protect their own interests. The unique nature of the fiduciary duty therefore requires the trust-based remedies to lean more in favor of the beneficiaries than those for breaches of contract.

The following chapter of the *Trust Law of China* is on charitable trust. Passed to clamp

⁵⁶⁴ *Ibid*, art. 57.

⁵⁶⁵ *Ibid*, art. 58.

⁵⁶⁶ Lusina Ho, “China: trust law and practice since 2001” (2010) 16 *Trusts and Trustees* 124 at 125.

down on banks taking advantage of the tax allowances for charitable trusts, the enactment was driven part by international trust law, particularly, after the Northern Rock scandal in Great Britain.⁵⁶⁷ To that end, the *Trust Law of China* stipulates that a charitable trust must be dedicated to public welfare, and enumerates lists the seven regulatory purposes in article 60 categories which meet this purpose.⁵⁶⁸ Public welfare trust is largely promoted and encouraged by the Chinese government⁵⁶⁹ with the approval of the Public welfare Administration Authority.⁵⁷⁰

Sections A to E have examined some of the important regulations of the *Trust Law of China* and offered brief amendments proposed to solve its limitations and uncertainties. In addition to the main regulations, another interesting issue arises with regards to the Chinese trust law arise as to the remedies for a breach of trust.

F. Remedies for a Breach of Trust

This section deals with remedies for a breach of trust. Part of the reasons trusts are so popular in the common law is due in great part to the extensive equitable remedies that trusts provide to beneficiaries. Nevertheless, the *Trust Law of China* is silent on numerous important issues in relation to these remedies⁵⁷¹. Only six articles – article 22, 27, 28, 30, 32 and 37 – that stipulate civil liabilities for a breach of trust in general terms. Nor does the *Trust Law of China*

⁵⁶⁷ Hsiao, *supra* note 461 at 236.

⁵⁶⁸ *Trust Law of China*, *supra* note 1, art. 60: A trust created for one of the following purposes in the interest of public welfare is a public welfare trust: (1) relief for the poor; (2) relief assistance to people suffering from disasters; (3) helping the disabled; (4) developing education, science, technology, culture, art and sports; (5) developing medical and public health undertakings; (6) developing undertakings for the protection of the environment and maintaining ecological environment; and (7) developing other public welfare undertakings.

⁵⁶⁹ *Ibid*, art. 61.

⁵⁷⁰ *Ibid*, art. 62.

⁵⁷¹ The Roman legal maxim *ubi ius ibi remedium* means where there is a right, there is a remedy.

contain any further guidelines on the detailed remedial principles, such as rules relating to the measure of recovery. It does however offer some guidelines for those seeking remedies.

Specifically, in order to “ascertain the availability of a remedy under the current Trust Law, a claimant needs to identify: first, which duty is breached; second, whether breach of the duty in question attracts any remedies (some duties do not seem to do so); and third, which remedies are available.”⁵⁷² The first question is answered by the *Trust Law of China* in the form of parties’ duties and obligations, discussed in sections B, C, and D. As to the second and the third issues treating the awarding of remedies the statutes are unclear and sometimes nonexistent. Consequently and given the potential for abuse that exists in Chinese trust law the remedies for breach of trust are currently a hot issue in China.⁵⁷³ Partially in response to this gap, and in response to the furor in China, this section first seeks to identify a systematic framework for the remedies for a breach of trust and second, point out the gaps that ought to be filled. In general, remedies for breaches of trusts are classified into personal remedies against trustees, proprietary remedies, claims against third parties, and criminal liabilities for a breach of trust.

(1) Personal remedies against trustees

Remedies against trustees may be divided into monetary remedies and non-monetary remedies in China. According to various functions they serve, the monetary remedies can be subdivided into awards that aim to restore the trust property, in monetary terms, to its original state, or alternatively compensate loss, restitute trustee enrichment arising from abuse of trust

⁵⁷² Ho, *Trust Law in China*, *supra* note 418 at 150.

⁵⁷³ *Ibid* at 139.

and rectify a trustee's unjust enrichment. Non-monetary remedies include nullification, return of property, restoration of property to its original state, cessation of infringement, removal of obstacle, and elimination of dangers.⁵⁷⁴ It should be noted at the outset that not all of remedies are currently available under the *Trust Law of China*. Instead, some of them are referred to in the regulations in the *General Principles of Civil Law of People's Republic of China*⁵⁷⁵ (hereinafter referred to as *General Principles of Civil Law*).

(a) Monetary remedies against trustees

The focus of the restoration of the trust fund is the trust property itself. Thus the remedy is available when the trustee has committed an omission to apply the trust fund as required, or when the trust property has been wrongfully disposed. In the *Trust Law of China*, the remedy of restoration is regulated in both article 22 and 27, in situations where the trustee “disposes of the trust property in breach of the purposes of the trust, or causes losses to the trust property”⁵⁷⁶ and that where the trustee converts the trust property into his own property⁵⁷⁷ respectively. Although the wording of these two articles appears similar, these two provisions are nonetheless quite different. In relation to misappropriation, the remedy of restoration is considered as an addition to compensation for loss in article 27, while article 22 defines restoration only as an alternative to compensation. Moreover, article 22 requires proof of loss as a result of the breaches of trust. No such condition is prescribed in article 27, possibly since that article's drafters might have

⁵⁷⁴ *Ibid* at 150-51.

⁵⁷⁵ *General Principle of the Civil Law of the People's Republic of China*, (Adopted at the Fourth Session of the Sixth National People's Congress, promulgated by Order No. 37 of the President of the People's Republic of China on April 12, 1986, and effective as of January 1, 1987).

⁵⁷⁶ *Trust Law of China*, *supra* note 1, art. 22.

⁵⁷⁷ *Ibid*, art. 27.

assumed any loss to have been self-evident in cases of wrongful disposal or misappropriation. These provisions set out the availability of the remedy of restoration. Nevertheless, neither articles 22 or 27 provide an explanation of how the remedy actually operates.

In addition to articles 22 and article 27, the *Trust Law of China* recognizes the availability of compensation, which plays a crucial role of enabling recovery of consequential losses, for breaches of the self-dealing and fair-dealing rules.⁵⁷⁸ However, it does not regulate the measures of the compensation. Instead, as Professor Ho notes, Chinese law can allow for the compensation in torts against property rights to be adopted for the breach of trust. “As the trust undertaking is a more onerous duty than the tortious duty to respect other’s property, the remedy for a breach of trust should not be any lighter than that for a tort. [She also suggests] the compensation remedy should not be limited by foreseeability or remoteness, though causation between the breach and the loss ought still be proven.”⁵⁷⁹

Likewise it is unclear whether compensation should return the trust fund back to its state immediately before the breach, or alternatively, the state in which the fund would have been if the breach had not occurred. The latter option, which is consistent with international practice, should be adopted in Chinese trust law. Adopting a remedy in which compensation would seek to restore the fund’s position works because of the relation between trust and contract law: if the remedy of compensation under trust law were less favorable, the beneficiary of an *inter vivos* trust, for example, established by a trust contract and in which the parties are bound by

⁵⁷⁸ *Ibid*, art. 28.

⁵⁷⁹ Lusina Ho, “The People’s Republic of China” in John Glasson & Geraint Thomas, eds, *The International Trust* (Bristol: Jordan Publishing Limited, 2006) 826 at 837.

contractual relations, could merely invoke the remedies of the *Contract Law of China* that allow recovery of “benefits that could have been obtained”.⁵⁸⁰ Not doing so, or not allowing the recourse, would lead to an unjustifiable discrepancy of remedies between trusts that are established by trust contract and those that created by other instruments such as wills. In addition, there is no reason why the more onerous trust duty should be protected by a less rigorous degree of compensation than the contractual duty.

Apart from causing loss to the trust property, a trustee’s breach may also result in benefits for him. With regard to this kind of breach, article 26 provides that “the interests gained therefrom shall be integrated into the trust property”.⁵⁸¹ However, in comparison to the common law approach, which imposes both a constructive trust on profits made from breach of trust and a personal liability on the trustee to account for such profits, the Chinese law is flawed in that no mention of such liability has been made. It is submitted that the Chinese Trust Law should impose the personal liability of account of profits on the trustee.⁵⁸²

(b) Non-monetary remedies

One of the most important non-monetary remedies available under Chinese law is nullification. In the common law, nullification is known as rescission. This remedy seeks to cancel a transaction by releasing the parties from future obligations, and unwinds obligations that are already performed. Its fundamental purpose is to put the parties back to their exact position before the breach. Accordingly, following nullification, all benefits already obtained from the

⁵⁸⁰ *Contract Law of China*, *supra* note 426, art. 113(1).

⁵⁸¹ *Trust Law of China*, *supra* note 1, art. 26.

⁵⁸² Ho, *Trust Law in China*, *supra* note 418 at 159.

relevant transaction must be returned *in specie*. As to the grounds for nullification, article 22 of the *Trust Law of China* prescribes that nullification applies when the trustee's disposal of the trust property is against the purposes of the trust. Nevertheless, this provision is open-ended and vague, and, importantly, it does not explain what situations constitute a breach of trust purposes. It has been argued that this regulation should be explained as a breach of trustees' duties since the common objective of all trusts should be understood as the protection of the beneficiaries' interests and trustees are given a series of duties to protect such interests.⁵⁸³

In addition to the grounds for nullification, another issue regarding nullification is what prevents it. In common law, a full set of impediments includes lapse of time, the intervention of third-party rights, affirmation by the claimant, and impossibility of counter-restitution.⁵⁸⁴ In China, only the lapse of time and the intervention of third-party rights can be found in its trust law, particularly in article 12 and article 22. Article 12, for example, states that the claimant must petition for this remedy within one year from the date he became aware or ought to have become aware of the ground for nullification. This one-year period of time is consistent with limitation periods in the Chinese law generally.⁵⁸⁵ As to the bar of the protection of third-party rights, article 12 states that nullification shall not affect the trust benefits already obtained by a *bona fide* beneficiary.

That said, the *Trust Law of China*, fails to make any provision of the affirmation by the claimant and impossibility of *restitutio in integrum*. It is submitted that the relevant provisions of

⁵⁸³ *Ibid* at 162-63.

⁵⁸⁴ Guenter H. Treitel, *The Law of Contract*, 11th ed (London: Sweet & Maxwell, 2003) at 378-85.

⁵⁸⁵ See *Contract Law of China*, *supra* note 426, art. 55(1).

the Contract Law on those remedies ought to be applied to resolve these gaps. There is no policy reason for distinguishing between nullification for contacts as opposed to unlawful disposal in breach of trust. Accordingly, as in the *Contract Law of China*, nullification ought to be denied under the trust if the party entitled waives the right “by an explicit declaration or through his own conduct after he knows the cause for rescission”.⁵⁸⁶ Likewise, the bar of impossibility of *restitutio in integrum* should also be stipulated with reference to the *Contract Law of China*. Article 58 of the *Contract Law of China* provides that “where it is impossible or unnecessary to return [the property], its value should be made good”.⁵⁸⁷ Therefore, nullification is denied when it is impossible in practice to return the relevant property and the trustee is required to make good the loss in money in this case. Perhaps more importantly however, Chinese trust law allows both settlor and beneficiaries to claim nullification. However, as one of the basic principles of trust law is to provide benefit to the beneficiaries, it seems odd that the statute would provide protection for settlor interest. Therefore, the *Trust Law of China* should be amended to solve those problems and fill in the gaps.

There remain huge gaps in the legislation as regarding ongoing breaches: while nullification can be used to unwind wrongful dispositions that have already been made other forms of non-monetary remedies dealing with ongoing breaches are necessary and nonexistent. Indeed, it is unfortunate that the *Trust Law of China* is silent on these reliefs. With reference to the regulation of article 134 of the *General Principle of Civil Law*, the remedies of cessation of infringement, removal of obstacles, and elimination of danger, all of which are taken from the

⁵⁸⁶ *Ibid*, art. 55(2).

⁵⁸⁷ *Ibid*, art. 58.

common law, should be added into Chinese trust law.

(2) Proprietary remedies and claims against third parties

Proprietary remedies, namely the remedies that ensure the segregation of the trust from those of the settlor's assets, are what originally made the trust widely popular in common law. These remedies also pose one of the most taxing issues in introducing the trust to civilian jurisdictions.⁵⁸⁸ As with other provisions of remedies however, article 16, which stipulates that trust property is segregated from the general assets of the trustee and the trust property shall not fall into the trustee's estate or liquidation property, remains only a general rule, and misses specific regulations of the liabilities for breach of this rule. As to the third type of remedy, claims against third parties, the only provision stipulating it is article 22. It requires that in order to claim against a third party, the third party needs to have received the property and he needs to be well aware that it came from a breach of trust. However, the remedies regulated in this provision have a narrow scope compared to the right to trace in common law. The remedies are restricted to the right to claim nullification of trustee's disposition, to restore trust property and to make compensation.⁵⁸⁹

(3) Criminal liabilities for a breach of trust

Although breach of trust is not a criminal offense, a breach of trust might in certain circumstances be a crime. Firstly, a trustee who breaches his duty of confidentiality under article 33 of the *Trust Law of China* might also be in breach of article 219 of the *Criminal Law of the*

⁵⁸⁸ Ho, *Trust Law in China*, *supra* note 418 at 168.

⁵⁸⁹ Chen & Dou, *supra* note 518 at 228.

*People's Republic of China*⁵⁹⁰ (hereinafter referred to as *Criminal Law of China*) which treats violations of commercial secrets.⁵⁹¹ Additionally, a trustee's misappropriation of the trust fund in private trusts may also constitute a crime under article 270 of the *Criminal Law of China*, which regulates unlawful taking over of another's property placed in his possession.⁵⁹² Moreover, if the trustee is an employee of the settlor, his misappropriation may alternatively fall into the crime under article 272 of the *Criminal Law of China* relating to the exploitation of his office to misappropriate his employer's funds for his own use.⁵⁹³ It may also constitute a crime under article 271 for illegally taking possession of property of his employer by taking advantage of his office.⁵⁹⁴ Regarding charitable trusts, a trustee who misappropriates state funds authorized to be used to establish a charitable trust could conceivably be found guilty of the crime of misappropriating State funds allocated for disaster relief under article 273 of the *Criminal Law of*

⁵⁹⁰ *Criminal Law of the People's Republic of China*, (Adopted at the Second Session of the Fifth National People's Congress on July 1, 1979; revised at the Fifth Session of the Eighth National People's Congress on March 14, 1997 and promulgated by Order No.83 of the President of the People's Republic of China on March 14, 1997).

⁵⁹¹ *Ibid*, art. 219: Whoever commits any of the following acts of infringing on business secrets and thus causes heavy losses to the obligee shall be sentenced to fixed-term imprisonment of not more than three years or criminal detention and shall also, or shall only, be fined; ... (1) obtaining an obligee's business secrets by stealing, luring, coercion or any other illegitimate means; (2) disclosing, using or allowing another to use the business secrets obtained from the obligee by the means mentioned in the preceding paragraph; or (3) in violation of the agreement on or against the obligee's demand for keeping business secrets, disclosing, using or allowing another person to use the business secrets he has.

⁵⁹² *Ibid*, art. 270: Whoever unlawfully takes possession of another person's money or property under his custody and refuses to return it, if the amount is relatively large, shall be sentenced to fixed-term imprisonment of not more than two years, or criminal detention or be fined; ... Whoever unlawfully takes possession of an object, which another person has forgotten about or buried, and refuses to hand it over, if the amount is relatively large, shall be punished in accordance with the provisions of the preceding paragraph.

⁵⁹³ *Ibid*, art. 272: Any employee of a company, enterprise or any other unit who, taking advantage of his position, misappropriates the funds of his own unit for personal use or for loaning them to another person, if the amount is relatively large and the funds are not repaid at the expiration of three months, or if the funds are repaid before the expiration of three months but the amount involved is relatively large and the funds are used for profit-making activities or for illegal activities, shall be sentenced to fixed-term imprisonment of not more than three years or criminal detention.

⁵⁹⁴ *Ibid*, art. 271: Any employee of a company, enterprise or any other unit who, taking advantage of his position, unlawfully takes possession of the money or property of his own unit, if the amount is relatively large, shall be sentenced to fixed-term imprisonment of not more than five years or criminal detention.

China.⁵⁹⁵ When it is unclear whether the trust is private or charitable, a trustee who misappropriates trust funds commits a crime of theft under article 264.⁵⁹⁶ Where a fraudulent breach of trust does not comply with any articles of specific crimes, the breach might fall into the crime of fraud under article 266.⁵⁹⁷ Moreover, a trustee who intentionally destroys trust property might also be liable for criminal damage according to article 275 of the *Criminal Law of China*.⁵⁹⁸

These criminal liabilities provide advantages to the Chinese trust system: they offer a far greater deterrence to a breach of trust than civil liabilities; the scope of some of these crimes might be wider than the scope of the civil liabilities for breach of trust, such as the case of use of commercial secrets.⁵⁹⁹ Furthermore, pursuant to article 36 of the *Criminal Law of China*, the court may order a criminal to compensate the victim for the economic loss. Such compensation will take priority when the trustee's property is insufficient to satisfy all the fines.⁶⁰⁰

In short, contingent upon a breach of trusts, Chinese trust law provides proprietary

⁵⁹⁵ *Ibid*, art. 273: In cases of misappropriation of funds or materials that are allocated for disaster relief, emergency rescue, flood prevention and control, support to disabled servicemen and families of revolutionary martyrs and servicemen, aid to the poor, migration and social relief, if the circumstances are serious and major harm is caused to the interests of the State and the people, the person who is directly responsible for the offence shall be sentenced to fixed-term imprisonment of not more than three years or criminal detention.

⁵⁹⁶ *Ibid*, art. 264: Whoever steals a relatively large amount of public or private property or commits theft repeatedly shall be sentenced to fixed-term imprisonment of not more than three years.

⁵⁹⁷ *Ibid*, art. 266: Whoever swindles public or private money or property, if the amount is relatively large, shall be sentenced to fixed-term imprisonment of not more than three years.

⁵⁹⁸ *Ibid*, art. 275: Whoever intentionally destroys or damages public or private money or property, if the amount involved is relatively large or if there are other serious circumstances, shall be sentenced to fixed-term imprisonment of not more than three years.

⁵⁹⁹ Ho, *Trust Law in China*, *supra* note 418 at 185.

⁶⁰⁰ *Criminal Law of China*, *supra* note 590, art. 36: If a victim has suffered economic losses as a result of a crime, the criminal shall, in addition to receiving a criminal punishment according to law, be sentenced to making compensation for the economic losses in the light of the circumstances.

If criminal who is liable for civil compensation is sentenced to a fine at the same time but his property is not sufficient to pay both the compensation and the fine, or if he is sentenced to confiscation of property at the same time, he shall, first of all, bear his liability for civil compensation to the victim.

remedies, claims against third parties, and personal remedies as means of obtaining satisfaction against trustees. However, under personal remedies against trustees, the *Trust Law of China* only recognizes the remedy of restoration and the remedy of compensation under monetary remedies and the remedy of rescission as a non-monetary remedy. The *Trust Law of China* is silent regarding the other reliefs, and all its provisions merely offer general rules to follow rather than detailed regulations. That said, in addition to the remedies provided by the *Trust Law of China*, a breach of trust can also cause criminal liabilities under the *Criminal Law of China*.

4. Uncertainties of the Chinese Trust System

After offering a detailed examination of the provisions of the *Trust Law of China*, this section concludes by examining the significant uncertainties of the Chinese trust system. In addition to the gaps and overlaps of the regulations of the rights and obligations of trust parties, the biggest problem of the *Trust Law of China* is that it avoids dealing with the key issue of the ownership of trust property. As a consequence, the *Trust Law of China* causes renders ambiguous the ownership of trust property, unclear nature of beneficiary's rights, and results in a registration system of trust which exists in name only.⁶⁰¹

A. Ambiguous Ownership of Trust Property

In contrast to dual ownership under common law, ownership in China is absolute and indivisible, as it is in most civilian jurisdictions. Therefore, the ownership of trust property is a serious problem in the introduction of trusts in China. Regrettably, Chinese legislation has

⁶⁰¹ Yu, *How to Localize*, *supra* note 508 at 11, 13.

remained silent on this issue. There is neither direct reception of dual ownership nor clear stipulation of unitary ownership in the *Trust Law of China*; and the Supreme People's Court of China issued no judicial interpretation in relation to this issue. Instead, academics hold different opinions on the ownership of trust property. As a result, the lack of clarity and contending theorists creates ambiguity. This is reflected by both statutory ambiguity and interpretation ambiguity.

(1) Statutory ambiguity

Article 2 of the *Trust Law of China* regulates that:

For purposes of this Law, a trust refers to that the settlor, based on his faith in trustee, entrusts his property rights to the trustee and allows the trustee to, according to the will of the settlor and in the name of the trustee, administer or dispose of such property in the interest of a beneficiary or for any intended purposes.⁶⁰²

Instead of adopting the term of 'transfer' that is used in common law, this article chooses the expression of 'entrust' (委托) the property to describe the relationship between a settlor and a trustee. However, in Chinese law, 'entrust' is not a unique legal term used to describe a trust relationship. On the contrary, it is typically adopted in agency relationships or in mandates, where the transfer of property is not required.⁶⁰³ Therefore, use of the term of 'entrust' blurs the line between the trust and agency, causing the misunderstanding which incorrectly holds that that trusts do not require transfer of trust property.

Fittingly the vague term 'entrust' leaves open the question of the ownership of trust property, which, as it so happens, remains unanswered by the *Trust Law of China*. This seems

⁶⁰² *Trust Law of China*, *supra* note 1, art. 2.

⁶⁰³ See *General Principle*, *supra* note 575, art. 64; *Contract Law of China*, *supra* note 426, art. 396.

almost deliberate: the *Trust Law of China* consistently adopts ambiguous expressions in its constituent parts which indicate either laxness in drafting, or more likely, confusion as the nature of ownership. For example, article 14 states that “[t]he property obtained by the trustee due to a trust accepted is trust property”.⁶⁰⁴ The expression of ‘obtains’ (取得) seems to recognize the transfer of ownership; however, the same term ‘obtain’ is also used in agency law to refer to the agent’s acquisition of possession, as opposed to ownership of relevant property.⁶⁰⁵ Similarly, article 16 provides that “[t]he trust property shall be segregated from the property owned by the trustee”.⁶⁰⁶ Such a drafting seems to imply that a trustee is the owner of trust property, whereas article 15, by contrast, adopts the same stipulation for settlors.

Moreover, the *Trust Law of China* avoids saying that settlors and trustees are co-owner of the trust property, and refrains from distinguishing when these two provisions would apply.⁶⁰⁷ Specifically, articles 15 and 16 seem to only aim at imposing the duty of segregating trust property from personal property on the settlor and the trustee instead of authorizing them the ownership of trust property. Support for this opinion can be found in the *Law of the People’s Republic of China on Securities Investment Funds*, which stipulates that “fund property shall be independent from the property owned by the fund manager and fund trustee”⁶⁰⁸ while only the fund trustee but not the fund manager owns the fund assets.

⁶⁰⁴ *Trust Law of China*, *supra* note 1, art. 14.

⁶⁰⁵ Rebecca Lee, “Conceptualizing the Chinese Trust” (2009) 58:3 *International and Comparative Law Quarterly* 655 at 660.

⁶⁰⁶ *Trust Law of China*, *supra* note 1, art. 16.

⁶⁰⁷ Ho, “History, ambiguity and beneficiary’s rights”, *supra* note 397 at 195.

⁶⁰⁸ *Securities Investment Funds*, *supra* note 420, art. 6.

In addition, pursuant to article 9 of the *Trust Law of China*, whether the transfer of ownership takes place seems to depend on the terms of the trust contract or decisions made by the settlors when there are no such terms regulated in the trust contract. The article stipulates that:

The following items shall be stated clearly in the written documents required for the creation of a trust:

...

(4) the scope, types and status of the assets under trust; and

...

In addition to the items mentioned above, the period of the trust, the methods for the administration of the property under trust, remuneration payable to the trustee, manner for appointing another trustee, the cause for termination of the trust, etc. may be stated clearly.⁶⁰⁹

(2) Interpretation ambiguity

Not only is legislation silent on the issue of the transfer of ownership, neither legislative interpretation nor judicial interpretation clarifies whether the term ‘entrust’ could be interpreted as ‘transfer’. The Supreme People’s Court has issued no judicial interpretation on the *Trust Law of China*. Although other People’s Courts have interpreted ‘entrust’ in relation to the ownership of trust property, these decisions unfortunately lack the effect of legal interpretation because precedents are not a source of law and do not bind subsequent case decisions in China. Further difficulties arise given that certain case decisions either bypass the *Trust Law of China* or stand in conflict with it. For instance, in *Beijing Haidian Science & Technology Development Co. Ltd v Shenzhen Xinhua Jinyuan Touzi Fazhan Youxian Gongsi and Others*⁶¹⁰, the Higher People’s Court of Chongqing rejected the argument that the trustee is the owner of trust property and held that either the settlor or the beneficiary was, or even both of them were, the owner of the trust

⁶⁰⁹ *Trust Law of China*, *supra* note 1, art. 9.

⁶¹⁰ *Beijing Haidian Science & Technology Development Co. Ltd v Shenzhen Xinhua Jinyuan Touzi Fazhan Youxian Gongsi and others* (2006) Yugaofa Minchu zhi [First Instance, Civil Cases, Chongqing High People’s Court] No. 14, Chongqing High People’s Court, 19 March 2007 [translated by author].

property. It stated that either the settlor or the beneficiary had the right to bring action in a title dispute against a third party over the trust property. The trustee, as a titular owner, does not have a direct interest in a title dispute. So pursuant to article 108(1) of the *Civil Procedure Law of China*, he or she can only participate in the litigation as a third party but is not able to make any title claim against a third party. Similar views can be found in *Yanxin Co Ltd v Huabao Trust and Investment Co Ltd*. However, the *Trust Law of China*, even article 2, never denies a trustee to be the owner of trust property. Significantly, these cases are not an aberration of the People's Courts' perception of the trust, but are evidence that the trust is conceptualized as a subspecies of contract in China. The Courts had no difficulty invoking the *Contract Law of China* to characterize the assignment of rights and obligations, both internal and external, of trust parties.⁶¹¹

(3) Reasons for the vague regulation of the Chinese law and its problems

The Chinese regulation of trust ownership, neither preventing a trustee from obtaining the ownership nor mandating that the settlor shall be the owner, is a deviation from international practice. It is not only different from the common law rules, but also alien to its neighboring civil law jurisdictions (i.e. Japan).⁶¹² Although the *Hague Trust Convention* does not require the transfer of a trust asset in its article 2, it still provides that the asset be held under the control of the trustee. China's unique approach is the result of a last-minute change, since all the earlier drafts of the law contemplate the transfer of the settlor's property to the trustees.⁶¹³

⁶¹¹ Ho, "History, ambiguity and beneficiary's rights", *supra* note 397 at 205-06.

⁶¹² Ho, *Trust Law in China*, *supra* note 418 at 66.

⁶¹³ *Ibid* at 66-67. Also see n 82: Clause 3 in the 1996 and 2000 drafts requires the transfer of assets to the trustee; it follows the relevant part of article 1 of the Taiwan Trust Law, 1996 word by word. Cf. similar views of the author

Questions may arise as to why the Chinese legislature chose to adopt vague expressions rather than use the term ‘transfer’. One reason lies in the concern that once the ownership was clearly vested in the hand of the trustee, the trustee’s rights might become over expanded and consequently the settlors’ right to supervise the management of the trust would be affected. Unlike common law ownership, ownership in China is absolute and indivisible. Therefore, in the drafters’ perspective, the choice of the term ‘entrust’, as opposed to ‘transfer’, was not an oversight. Professor Jiang Ping, the *Trust Law of China*’s main drafter, considered it an innovation of the Chinese law to leave open the issue of the location of ownership. In his opinion, the *Trust Law of China* only needed to provide that a trustee is authorized to manage and administer trust properties, so as to draw an adequate balance between the need to grant trustees the right to dispose of trust property and to protect beneficiaries’ rights. Moreover, because most of the trusts established in China aim to be collective investment schemes, the investors would transfer their investment to the trustees anyway, therefore the drafters do not think it urgent to entitle the ownership of trust property to the trustees.⁶¹⁴ For the purposes of collective investments then, studied vagueness was at least appropriate, or, in the circumstances not as inappropriate as it would later become.

Yet because the trust is no longer restricted to collective investment, studied ambiguity can no longer suffice. Therefore, in order to adapt to the rapid development of the trust and its broad application in China, amendments to the regulation of ownership in the *Trust Law of China* are required. Rather than resolving the concerns of the drafters, these vague expressions

in “PRC Trust Law: Opportunity or Danger?” in *Law Lectures for Practitioners* (Hong Kong: Sweet & Maxwell Asia, 2002), pp. 87-108.

⁶¹⁴ Ho, “History, ambiguity and beneficiary’s rights”, *supra* note 397 at 201-02.

work against drafter's intention to entitle the trust management to the trustee and to equally protect the beneficiaries' interests. Instead, vagueness leaves room for settlors to choose whether to transfer the ownership to their trustees. However, because settlors are usually reluctant to relinquish their ownership of property to a stranger-trustee if no enforceable obligation is imposed, settlors are likely to abuse such ambiguity in order to retain the ownership of trust property in contravention of the original design of the trust.

In the absence of a clear entitlement of trust property therefore, the balance of interests between trust parties is destroyed and the efficiency of trust management is decreased. As Professor Ho said: "the absence of ownership will significantly limit the trustee's powers to act in his own name as envisaged by the Trust Law, and this will limit in turn the convenience that a trust relationship is supposed to bring."⁶¹⁵ Indeed, it is difficult to see how a trustee can obtain any independent control of the trust property and manage efficient trust administration without having the ownership of property. The settlor's retention of the ownership requires the trustee to seek the settlor's consent and cooperation in every disposition of the trust property. Additionally, the *Trust Law of China* grants considerable powers to the settlor to monitor the trustee.⁶¹⁶ Should the trustee sets up hurdles in order to safeguard the trustees' management of trust assets, there is a great risk that the settlor might misappropriate the trust contrary to the terms of the trust, unbeknownst to the trustee. In such cases, the redresses available to the beneficiaries may at best be theoretical and at worst nonexistent. Given that none of the provisions of the *Trust Law of China* imposes any specific duties on a settlor to segregate trust property, observe the terms of

⁶¹⁵ *Ibid* at 200.

⁶¹⁶ See *Trust Law of China*, *supra* note 1, arts. 21-23.

the trust or to refrain from misappropriating trust property the beneficiary may find himself bereft of legal benefit. Even such provisions were to exist for beneficiaries, the *Trust Law of China* does not provide any remedies for breach by the settlor. Moreover, no provision is made in the Chinese law for the replacement of settlors. Consequently, if a settlor, the apparent owner of trust property, dies, the trust assets will be left in a sort of legal limbo given that the trust assets do not fall to the settlor's heirs according to article 15. Likewise, questions will arise as to "under whose name the trust assets should be registered, to whom tax liabilities should be charged, and who has the title to sue upon torts infringing the ownership rights over the assets".⁶¹⁷

B. Outstanding Characteristic of the Beneficiary's Right

A beneficiary holds 'equitable ownership' under the dual ownership of common law. How to interpret this ownership and what is the nature of a beneficiary's right has been a key issue of the introduction of trusts in China. Unfortunately, like the issue of trust ownership, the Chinese legislation again adopts an evasive nomenclature, which makes the nature of the beneficiary's rights another unresolved difficult to pin down.

As discussed, the *Trust Law of China* provides that a beneficiary is entitled to benefit from a trust. It also establishes that this right is assignable and inheritable, and extends to exchange products lawfully or unlawfully obtained by the trustee and still held in his hands. Moreover, the beneficiary has the right to ask the trustee to adjust the methods of management of trust property, and to apply to the People's Court to annul the trustee's disposition of trust

⁶¹⁷ Ho, *Trust Law in China*, *supra* note 418 at 68.

property, as well as to ask the trustee to restore the property to its former state or make compensation. In other words, the beneficiary has the right to enjoy the trust benefits and can claim against trustees or exclude third parties' interference by annulling trustees' wrongful disposition.

However, there is no explicit provision in the *Trust Law of China* that regulates the nature of the beneficiary's rights. It does not indicate whether the right to claim against trustees and the right to exclude interference from third parties are in the essence of real rights or personal claims. What makes this 'vacuum' of legislation more complex is that various theories arise to interpret the nature of the beneficiary's rights in academia. For instance, the theory of real rights states that trustees' legal ownership is only a right of management, while the beneficiary's equitable ownership is the real title.⁶¹⁸ In contrast, the theory of personal claim posits that the beneficiary's right is in the nature of a debt. Equitable ownership would thus entitle the beneficiary to personal claims against trustees. As a compromise of the foregoing two theories, the theory of co-existing real rights and personal claim takes the position that the beneficiary's right has the dual nature of a personal claim against trustees and a real right over trust property.⁶¹⁹ In addition, a novel theory, termed as special right theory, simply defines the beneficiary's rights as a special right due to the difficulties in fully integrating it into either real rights or a personal claim.⁶²⁰ Likewise, some commentators describe the beneficiary's right as a trust property right (信托财产权), which is an independent civil right similar to intellectual

⁶¹⁸ Shiyang Wen & Xingjun Feng, "Ownership of Trust Property: On the Improvement of China's Legislation" (2005) 2 Wuhan University Journal (Philosophy and Social Science) 203 at 203 [translated by author].

⁶¹⁹ Zhesheng Xie, *General Trust Law* (Taipei: Yuan Zhao Press, 2003) at 14. [translated by author].

⁶²⁰ Linqing Jia, "The Legal Nature of the Trust Property and the Structure" (2005) 5 Jurists Review 81 at 83 [translated by author].

property rights and rights over shares.⁶²¹ However, as with the special right theory, there is little room under the present Chinese law to accommodate a new type of right.

C. The Registration System of Trust Property Exists in Name Only

Despite the silence of the *Trust Law of China* regarding the transfer of trust property ownership, the statute nevertheless accepts the rule of independence of trust property with no difficulty. As in the common law, Chinese law formally requires trust property to be segregated from the personal assets of settlors and trustees. As such, trust properties cannot be used to offset their personal debts and is immune from their creditors, successors, or spouses in the event of bankruptcy, death, or divorce.⁶²²

In order to implement the independence rule of trust property and to ensure a third party's right to know (especially when the third parties are the creditors of settlors or trustees), a sound registration system of trust property is very much necessary. In article 10, the *Trust Law of China* regulates that “[w]here laws or administrative regulations stipulate that registration formalities shall be gone through for the creation of a trust, such formalities shall be gone through accordingly. Anyone who fails to go through the registration formalities prescribed in the preceding paragraph shall go through the formalities as required; otherwise, the trust shall have no effect.”⁶²³ However, this regulation remains too general and vague.⁶²⁴ In the absence of

⁶²¹ Tiantao Shi & Wenran Yu, *Law of Trusts* (Beijing: Publishing House of People's Court, 1999) at 60.

⁶²² Specific regulations of the independence of trust property in the *Trust Law of China* can be found in articles 15, 16, 17(2) and 29.

⁶²³ *Trust Law of China*, *supra* note 1, art. 10.

⁶²⁴ Professor Jiang stated that this vague provision is a compromise provision due to the arguments that registration for trust would be complicated and unnecessary. See the preface that Ping Jiang writes for the books of Haiyong Yu, *How to Localize the British and American Law on Trust Property in China* (Beijing: China University of

relevant regulations of when registration formalities shall be gone through for the creation of a trust, the regulation of article 10 is confusing. One reading of this article does not mandate registration for trusts involving property that need not be registered, such as moveable assets or money.⁶²⁵ In contrast, another reading of this article requires some kind of registration in relation to all types of trust property, regardless of whether it is real estate or movable property. If this is the case, a question arises as to where the trust property should be registered, due to the fact that the existing registration system for real estate in China does not include real estate trusts in its scope, nor does it mention the registration of movable property trusts, commercial trusts or intellectual property trusts.

Furthermore, Chinese trust law does not clarify to what extent the details of a trust need to be disclosed in the registration. That is, whether only the trust property should be disclosed or whether more details of the trust instrument, such as the identity of trust parties, must also be disclosed. In addition, the effect of non-registration is vague. Article 10 allows retroactive registration of trust property however it does not specify a time limit for the retroactive registration. Therefore, the trust would in practice never be voidable due to non-registration, unless the parties refuse to register. Furthermore, article 10 does not provide whether a trust for non-registrable property is enforceable against third parties.

Article 10's vague wording also causes a number of practical problems in relation to registration procedures and registration authorities. As it stands, article 10 is unclear as to which

Political Science and Law Press, 2011) at XIII-XIV.
⁶²⁵ Ho, *Trust Law in China*, *supra* note 418 at 79-80.

government authority should take responsibility for the registration of trust property.⁶²⁶ Currently, responsibilities could conceivably be split among a specialized authority established for trusts or normal government authorities that are in charge of real rights registration. In 2006, the Shanghai *Pudong* New Area Bureau established the Shanghai Trust Registration Centre, which aims to establish a publicly accessible registry of trusts and to promote the registration of trust property. However, compliance has not been satisfactory due to the lack of detailed regulations at both regional and national level. Individual institutions, as it were, exist in a kind of regulatory vacuum, cut off from each other. As Wang Hao and Zhou Yi note, “there are neither mandatory registration requirements nor unified registration institutions in China.”⁶²⁷ Due to the absence of clear entitlement of trust ownership, the definition of the nature of beneficiary’s rights, and workable registration norms, the registration system of trust exists in name only.

In short, while the *Trust Law of China* took the bold step of incorporating the trust into China and shed lights on the introduction of trusts in civilian jurisdictions, much more work needs to be done for it to work properly. The law avoids the key issue of ownership of trust property and has instead succeeded in introducing the trust as a species of contract subject to pre-existing contractual statutes. Ambiguities in the statute’s wording have created considerable hurdles for lawyers trying to understand the nature of the beneficiary’s rights, businessmen trying to efficiently manage the trust, and those tasked with safeguarding the independent exercise of discretion of the trustee. As it stands, the *Trust Law of China* is a piece of broad and

⁶²⁶ Yu, *How to Localize*, *supra* note 508 at 193.

⁶²⁷ Hao Wang & Yi Zhou, “China” in Charles Gothard & Sanjeev Shan, eds, *The World Trust Survey* (Oxford: Oxford University Press, 2010) 158 at 160.

general legislation with gaps and ambiguities to be fleshed out in the course of the development of a more comprehensive legal and regulatory regime for the trust.⁶²⁸ Clearly, work remains to be done: since its promulgation in 2001, the *Trust Law of China* has never been amended and all the regulations of trust companies stay at the level of CBRC regulations rather than administrative regulations of the State Council.⁶²⁹ As a result, the Chinese rules of trust fall behind the development of trust business.⁶³⁰ In consideration of all the uncertainties of the Chinese trust law discussed in this chapter, it is necessary and important to propose amendments to the Chinese trust law, in particular to propose a better understanding of trust ownership in China.

⁶²⁸ Ho, Lee & Jin, *supra* note 404 at 97.

⁶²⁹ *Supra* note 423 at 205.

⁶³⁰ *Ibid* at 202.

IV A BETTER UNDERSTANDING OF DUAL OWNERSHIP IN CHINA

From the lessons learned in Chapters I and II, we can see that even though dual ownership, deriving from the common law, is recognized as a main feature of the trust, it does not prevent the trust from fitting into a civilian jurisdiction where ownership is typically regarded as indivisible. The experience of Scots and Quebec law indicates that instead of completely copying the idea of dual ownership, civilian jurisdictions can adopt the binary system of personal claims and real rights⁶³¹, or the notion of patrimony, to introduce trusts in the absence of equity. This chapter seeks to integrate all the lessons learned from the above chapters in proposing suggestions of the amendments to Chinese trust law. In particular, it seeks to offer solutions to the problems identified in Chapter III, namely the troubles arising from the introduction of trusts into a legal system that does not acknowledge the concept of dual ownership. The resultant ambiguity within the regulation of Chinese trust has baffled both practitioners and scholars alike. This section therefore focuses on providing, a better understanding of dual ownership in China.

In keeping with the mantra of modern comparative studies to ‘compare function rather than form’, this chapter believes that the key to understanding dual ownership in China is to apply ‘the binary system of real rights and personal claims’ to achieve the functions of financial management and beneficiary security of trusts. The binary system requires China to maintain indivisible ownership while accommodating common law ownership as a trustee’s unitary ownership in real rights, all the while introducing a functional equivalent of equitable ownership

⁶³¹ The binary system of claims and real rights grants the unitary ownership to the trustees so as to enable them to maximize the property management function. Meanwhile, under the binary system, beneficiaries’ interests are protected through their beneficiary rights and personal claims against the trustees, like a creditor. It will be specifically explained below.

as a special kind of personal claim. This design fits the trust into the Chinese legal system without causing damage to either the function of the trust or the Chinese legal tradition, and has the benefit of being conducive to solving the problem of double taxation.

1. Possibilities to Distill the Trust and Its Dual Ownership into China

A. Dual Ownership is a Misunderstanding of the Common Law Trust

As mentioned, this thesis adopts the conventional concept of the essence of common law trusts as dual ownership in Chapter I.⁶³² However, as dual ownership is a misunderstanding of the common law trust, it is not an obstacle to the introduction of trusts in China. This misunderstanding, as we will see, derives from the fact that the *essence* of common law trusts does not lie in splitting ownership into legal title and equitable title, but rather in the split between the enjoyment and administration of trusts. Dual ownership then, merely is the external appearance of the trust, but is not its essence.⁶³³ Furthermore, the definition of ownership in common law and civil law is not exactly the same, consequently leading to the difference in owners' rights and obligations. Therefore the terminology for comparative studies is potentially misleading. As a result, completely adopting the dual ownership into the Chinese legal system is unnecessary and inappropriate⁶³⁴.

(1) Dual ownership is the external appearance but not the essence of the trust

China's copy of the dual ownership is unnecessary since the essence of the common law

⁶³² This was stated in Chapter I 2.

⁶³³ This was stated in Chapter II 2 A (1).

⁶³⁴ Yuanliang Zhang, "Localization of the Trust property system in China" (2007) 1 Journal of Henan Institute of Financial Management 100 at 101 [translated by author].

trust is found in the trustee's obligation with respect to trust property, while the division of ownership is only its external appearance. The concept of dual ownership creates the impression of an idiosyncratic set of rules that are English, peculiar, and peculiarly English. It suggests that such rules cannot possibly be exported to those prosaic civil jurisdictions that do not share English law's colourful history. However, trusts depend not on the localised tradition of equity. As far as equitable property rights are concerned, that perception can be resisted.⁶³⁵ The essence of the common law trust is the imposition of an equitable obligation on a trustee requiring the trustee to act in good faith when dealing with trust property in favour of the beneficiary.⁶³⁶ The nature of the obligation imposed on the trustee is evident in the definition of the trust provided by Keeton and Sheridan⁶³⁷, and by Hanbury and Martin⁶³⁸. It can be best regarded as a *sui generis* 'proprietary obligation'.⁶³⁹

More specifically, the focus of the trust is on property.⁶⁴⁰ "While the trust is a property holding device, the means by which trusts law effects the holding of property and the protection of the rights of the beneficiaries is by means of imposing obligations on the trustees."⁶⁴¹ In other words, the essence of the trust is reflected in the fact that beneficiaries have no direct control over the trust property. Thus the realization of their rights depends upon trustee performance. This means that the beneficiaries' rights are the converse of the obligations of the trustee owed to them in respect of the trust property. As Professor Smith notes, "[t]he rights of beneficiaries in

⁶³⁵ Ben McFarlane & Robert Stevens, "The Nature of Equitable Property" (2010) 4 Journal of Equity 1 at 28.

⁶³⁶ Thomas & Hudson, *supra* note 88 at 11.

⁶³⁷ Sheridan, *supra* note 5.

⁶³⁸ Jill Martin, *Hanbury and Martin: Modern Equity*, 19th ed (London: Sweet & Maxwell, 2012) at 48.

⁶³⁹ Robert Pearce, John Stevens & Warren Barr, *The Law of Trusts and Equitable Obligations*, 5th ed (Oxford: Oxford University Press, 2010) at 71.

⁶⁴⁰ Thomas & Hudson, *supra* note 88 at 14.

⁶⁴¹ *Ibid* at 16.

the common law trust are neither purely personal rights against the trustee, nor are they real rights in the trust property, but rather they are rights over the rights which the trustee holds as trust property; they have a proprietary character since they persist against many third party transferees of the trust property.”⁶⁴² Consequently, instead of separating ownership of trust property, the common law trust “was created by a distortion of the law of obligations, in particular an enormous expansion of the universally accepted possibility of third party liability for interference with obligations”.⁶⁴³ Since the common law was not created in dual ownership, so needless to say it is even more so in civilian jurisdictions.

(2) The difference in terminology used to study the trust is misleading

Another reason that dual ownership is a misunderstanding of the common law trust is that the definition of ownership in common law and civil law is different. Therefore, it is inappropriate to understand the notion of equitable ownership from the perspective of civilian jurisdictions, since its true meaning should instead be interpreted based on a review of its context and function. As Wesley Newcomb Hohfeld put it, the difference in terminology used to study the trust is misleading, as the language used to discuss the law of trusts in both the civil and common law system is so disparate as to be misleading.⁶⁴⁴ Additionally, Frederic William Maitland holds that some of the basic terminology of trust law, such as ownership, almost carries unexpected meaning, which tends to deviate from its strict definition.⁶⁴⁵

⁶⁴² Smith, “Trust and Patrimony”, *supra* note 2 at 332.

⁶⁴³ *Ibid* at 343-44.

⁶⁴⁴ Wesley N. Hohfeld, “Fundamental Legal Conceptions as Applied in Judicial Reasoning” (1917) 26 Yale Law Journal 710 at 718.

⁶⁴⁵ Frederic William Maitland, *Equity: A Course of Lectures*, 2nd ed (Cambridge: Cambridge University Press, 1936) at 23.

As discussed in Chapter II 1 A, the civilian understanding of ownership characterizes ownership as being the most absolute form of three types of right over a thing: *usus*, *fructus*, and *abusus*. All these rights, in the classical model of ownership, belong to a single person in relation to any particular thing. In contrast to the civilian model of absolute and indivisible ownership however, “[t]he old common law never thought in terms of absolute ownership, because all land was owned by the Crown ... As a result of feudalism, absolute ownership of land never appeared. What did appear was tenure, the reflection largely of a man’s status in the community, and then estate or interest, the economic measure of the rights of ownership to which he could lay claim”.⁶⁴⁶ In other words, the common law was never concerned with the direct ownership of land, but was concerned instead with the rights involved in ownership, including the rights to dispose, to manage, and to enjoy. Consequently, the common law conceived of a man as ‘owning’ an interest or estate in the land. Different from the theory of ownership of property in civilian jurisdictions, people do not own *things* (a physical approach), they own *rights in things* (a metaphysical approach) under common law. This is considered as a bundle of rights, estates or interests. This approach “makes it easy for ownership of the thing to be dismembered, and bits parcelled out to different people”.⁶⁴⁷

Specifically, the difference in the definition of ownership in civil law and common law can be summarized by two salient features: (a) the scope of equitable ownership in common law is narrower than absolute ownership in civil law; and (b) a trustee’s common law ownership is also narrower in scope than an equivalent ownership in civil law. Indeed, the reason why

⁶⁴⁶ Waters, Gillen & Smith, *supra* note 4 at 10.

⁶⁴⁷ Matthews, “The Compatibility of the Trust”, *supra* note 158 at 316.

ownership in civil law has a broader definition is that this ownership has the most comprehensive control over a property as a general rule. Namely, an owner in civil law is granted the right to *usus*, the right to use the thing, *fructus*, the right to take its fruits, and *abusus*, the right to alienate or even to destroy the thing. Different legal systems define these rights differently. For instance, in Chinese law, ownership comprises four kinds of rights: rights of possession, use, beneficial enjoyment, and disposal of property. Article 39 of the *Property Law of the People's Republic of China* (hereinafter referred to as *Property Law of China*) stipulates that “[t]he owner of a realty or chattel is entitled to possess, utilize, seek profits from and dispose of the realty or chattel in accordance with law.”⁶⁴⁸ On the contrary, equitable ownership in any case has no such full power of ownership because almost no equitable ownership involves the power of disposal over trust property, but only negative defense against the trustees’ misconduct. Therefore, the meaning of civilian ownership and equitable ownership under common law is different.

The difference between the trustee’s ownership in the common law and an equivalent civilian ownership is reflected in the perspectives of the rights of possession, use, enjoyment, and disposal of trust property.⁶⁴⁹ Firstly, the right of possession in Chinese law cannot be interfered with by other people, whereas the trustee’s possessory right of common law ownership can be eliminated by the beneficiaries’ will. As discussed before, according to the rule established in *Saunders v Vautier*, a beneficiary has the right to terminate the trust and obtain trust properties when he or she becomes an adult, has full capacity, and is entitled to enjoy the trust benefits. In the case of multiple beneficiaries, the termination of trust can be achieved by the beneficiaries’

⁶⁴⁸ *Property Law of China*, *supra* note 532, art. 39.

⁶⁴⁹ Because this part discusses the reception of the trust into the Chinese legal system, the author will take the Chinese law as an example of the civilian jurisdictions and will focus on its rules and legal theories.

agreement.

Unlike, however, an owner in civilian jurisdictions, a common law trustee cannot exercise the right to use trust property. This right is forbidden by the common law trust even when the trustee is willing to pay a reasonable consideration for the use of the trust property. The rationale for this is that a trustee ought not, as a normative principle, make a profit out of his trust or act for his own benefit rather than that of the beneficiary. Indeed trustees should not place themselves in the position where their personal interests would conflict with their fiduciary duties.⁶⁵⁰ The most important feature of the trust is that the trustee is not entitled to assert personal, beneficial ownership in the trust property.⁶⁵¹ Conversely, in civil law, the right of possession can be realized by the use of property. Even if the holder is not the owner of the property, his or her possession is still for the purpose of self-use.⁶⁵² Therefore, the rights of possession in common law and civil law are not of the same nature.

Similarly, unless otherwise provided in the trust terms, common law trustees do not have the right to enjoy the trust property. In civilian terms, this means that common law trustees usually cannot have fruits of the trust property. The trustees are under a duty to distribute income and capital to beneficiaries without demand,⁶⁵³ but must take care to distribute the trust property only to the beneficiaries who are properly entitled to it.⁶⁵⁴

Furthermore, a common law trustee's right to dispose of trust property is not as

⁶⁵⁰ Graham Moffat, *Trusts Law*, 5th ed (Cambridge: Cambridge University Press, 2009) at 421.

⁶⁵¹ Thomas & Hudson, *supra* note 88 at 30.

⁶⁵² Huixing Liang & Huashan Chen, *Property Law*, 5th ed (Beijing: Law Press China, 2010) at 198 [translated by author].

⁶⁵³ *Hawkesley v May*, [1956] 1 QB 304, [1995] 3 All ER 353.

⁶⁵⁴ Pettit, *supra* note 8 at 406.

complete as similar rights held by civilian owners. It is subject to many restrictions. For instance, a trustee is liable for a beneficiary's damage if he or she, whether deliberately or inadvertently, by a positive act or by a failure to act disposes of the trust property in breach of the trust instrument or legal regulations.⁶⁵⁵ Otherwise put, the trustees are personally liable to the beneficiaries. Therefore, different from the absolute and indivisible ownership in civil law, a trustee's common law ownership is a restricted real right that is limited to the existing period of the trust, and constrained by the trust instrument⁶⁵⁶ as well as the beneficiaries' benefits.

B. Renovations or New Judicial Interpretations of Trusts are Required to Fit into Modern Development

Besides the misunderstanding inherent in terms of dual ownership, China should maintain its indivisible ownership rather than copy the dual ownership idea, because the design of indivisible ownership, namely unitary ownership by the trustee, actually corresponds to the modern trends of trust law.⁶⁵⁷

Trusts have existed for centuries, and societies and economies have constantly advanced in the intervening years. This requires renovations or new judicial interpretations of the trust in order to adapt it into modern circumstances. In the modern legal and financial world, the trust fulfills many different functions, especially in investment and commerce. As a result, it is important that the trustee should have more powers and discretion and the law of trusts should be

⁶⁵⁵ *Ibid* at 512.

⁶⁵⁶ See Thomas & Hudson, *supra* note 88 at 30. "It will always be important to consider the precise terms of the trust ... the courts will tend to look very closely at the precise written terms of a trust or at the verbal expression of the settlor's intentions".

⁶⁵⁷ Chunhong Lin, Wei Zhang & Weidong Zhong, "New Opinions on Trust Property Right" (2003) 4 Commercial Research 84 at 85.

accessible to a wide range of usage.⁶⁵⁸ Moreover, with the development of international trade, trusts no longer exist only in common law systems.⁶⁵⁹ Because increasing international trade has proved an important trend over the last 30 years, amendments to trust law are urgently needed to comply with civilian property law. Doing so would be beneficial to promote international and inter-state trade between common law countries and civil law countries. It is for this reason that different jurisdictions have reformed their trust law in line with modern requirements. In keeping with the development of international commerce and society, and in order to facilitate the conversion from common law dual ownership to unitary ownership possible in China and other emerging civilian legal systems, dual ownership in common law trusts requires a better understanding or reform.

2. Trusts Without a Theory of Dual Ownership – Possible Designs in General

After recognizing the possibility of introducing the trust into China without dual ownership, questions arise as to how this change should be implemented in the design of China's ownership of trust property. For instance, a major question is whether Chinese trusts ought to use the notion of patrimony, like Quebec law, or focus on accommodating a binary system of personal claims and real rights. This leads to further questions: to whom the unitary ownership should be granted, trustees, beneficiaries or the trust itself? And, how to explain the nature of a beneficiary's right in a trust?

To answer these questions, Chinese scholars hold a variety of opinions. In 1987, He

⁶⁵⁸ *Discussion Paper on Supplementary and Miscellaneous Issues*, *supra* note 177 at para 1.3.

⁶⁵⁹ Paolo Panico, *International Trust Laws* (Oxford: Oxford University Press, 2010) at 2.

Xiaoyuan suggested that the ownership of trust property be transferred to a trustee, while a beneficiary has the right to revoke the trustee's disposition of trust property in breach of trust purpose and a right to follow the trust property.⁶⁶⁰ On the other hand, Wen Shiyang proposed a different explanation in 2005. He stated that beneficiary's equitable right is a real ownership; trustees' ownership is only a right of administration.⁶⁶¹ Xie Zaiquan, by contrast, considered the trustee's right as a limited real right, i.e. a real right on the property of other people and for their interests.⁶⁶² Moreover, Chen Sihan advanced that the trust should be granted legal personality and considered as a legal entity.⁶⁶³ As early as in 1994, Jiang Ping raised the dual attributes of real rights and personal claims. He indicated that the trustee's right to administer the trust property in his own name is in the nature of real right, but his obligation to distribute the trust income is a personal claim.⁶⁶⁴ In addition, Zhou Xiaoming in 1996⁶⁶⁵ and Li Qunxing in 2000⁶⁶⁶ raised the argument of a new type of right or right combination. As shown, Chinese scholars hold many different views as to how China should interpret the concept of dual ownership.

In turn, this thesis argues that China should remain its unitary ownership and should not, so as to avoid creating fundamental changes to the Chinese legal system, adopt the notion of patrimony as Quebec law or consider the trust as a legal person. In trying to answer, to whom the

⁶⁶⁰ Xiaoyuan He, "Studies of Trust Law" (1987) 1 *Chung Hsing Law Review* 1 at 6 [translated by author]. The right to revoke trustees' disposal of trust property and the right to follow the trust property are the two sides of the same kind of right.

⁶⁶¹ Wen & Feng, *supra* note 618 at 206.

⁶⁶² Zaiquan Xie, *Real Rights in Civil Law* (Beijing: China University of Political Science and Law Press, 1999) at 165 [translated by author].

⁶⁶³ Sihan Chen, "Study on the Ownership of Trust Property" (2010) 4 *Journal of Jiangxi Finance College* 48 at 51 [translated by author].

⁶⁶⁴ Ping Jiang, *Several Ideas of China's Trust Law* (Beijing: China Legal Publishing House, 2000) at 59 [translated by author].

⁶⁶⁵ Xiaoming Zhou, *Comparative Studies of Trust Law* (Beijing: Law Press, 1996) at 210 [translated by author].

⁶⁶⁶ Qunxing Li, "The Legal Nature and Basic Principles of Trust" (2000) 3 *Chinese Journal of Law* 118 at 121 [translated by author].

unitary ownership should be granted in the void created by the lack of dual ownership, four legal solutions have been suggested in theory in China: transferal of the ownership of trust property to beneficiaries; settlor retention of the ownership; ownerless trust property; and transfer ownership to trustees. This thesis takes up the last solution for the reason that this solution best fits with the existing Chinese legal system and causes no negative effect on trust functions. In order to support this argument, this section analyzes in detail the advantages and disadvantages of various solutions.

A. Transfer Ownership to Beneficiaries

An uncommon legal solution to the problem of who should be the unitary owner of a trust property is to allow a settlor to transfer his ownership of a trust property to a beneficiary instead of a trustee. This is despite the fact that the trustee is authorized to manage and administer trust property. Two of few examples of this theory can be found in the conception of the *Bewind* in the Netherlands and in South Africa.⁶⁶⁷ In the *Bewind* found in Dutch Law, it is the beneficiary who enjoys the ownership of property while an administrator, like a trustee in common law, holds the right to administer and dispose of the property. Similarly, in the *bewind* form trust in South Africa (as discussed in Chapter II), a beneficiary (heir) owns trust property (heritage) while a trustee (executor) has the right to manage the trust property. The rationale behind this theory is that the key purpose of trusts is to transfer the trust property for the interests of the beneficiaries.⁶⁶⁸

⁶⁶⁷ Reid, “Conceptualising the Chinese Trust”, *supra* note 189 at 8.

⁶⁶⁸ See Cameron, *supra* note 250 at 7-8.

Nevertheless, this rationale is not often the cause of the trust nowadays precisely because the trust is more frequent used as a legal device of property management, not a mechanism to avoid taxes when aiming at transferring the property to the beneficiary.⁶⁶⁹ Furthermore, this solution has a number of weaknesses. In the absence of ownership, the trustee's administration of trust property is less convenient and less efficient. That is because the trustees need to request and wait for the property owner's permission and cooperation in the trust management, such as a permission to enter into a transaction. In this case, the trustee acts the same as an agent. Additionally, if this solution were to prevail, the ownership of trust property would be in legal limbo for a certain period in some cases, such as the charitable trust, private purpose trust, and discretionary trust, that has no certain beneficiaries. For example, in *Royal Trust Co. v Tucker*, primary beneficiaries did not exist when the deed of donation and the trust were made; consequently, for a certain period of time ownership of the property in the trust would have been vested in no one.⁶⁷⁰

B. Settlor's Retention of Ownership

Another legal solution is for settlors to retain their ownership of the property, while trustees are entitled to manage the property based on a trust agreement.⁶⁷¹ Unfortunately, this solution is an aberration from the international practice⁶⁷² and thus has been rarely adopted by civilian jurisdictions; however, it is exactly the *de facto* rule adopted in China due to the vague regulation of the ownership of trust property in the *Trust Law of China*. Such vague regulation

⁶⁶⁹ Yu, *How to Localize*, *supra* note 508 at 89.

⁶⁷⁰ *Tucker*, *supra* note 325 at 264-65.

⁶⁷¹ Ho, *Trust Law in China*, *supra* note 418 at 41.

⁶⁷² Maurizio Lupoi, "Trusts in the Civil Law – An introduction" (1996) 2 *Trusts and Trustees* 21 at 21.

results in the Chinese trust law failing to distinguish the trust from similar instruments such as agency and mandate. More importantly, in the design of settlors' retention of ownership, the trust does not play the role of tax planning in that the ownership of trust property is still in the hand of the settlor. Additionally, this design would be likely to cause a number of other problems if introduced in China.

Firstly, the retention of ownership is likely to cause settlors to have too much power, or even to be able to abuse their ownership. That is because except for the regulations stated in a trust contract, almost no rule regarding the control of the use of property is stipulated in the *Trust Law of China*. Even if restrictions on the settlor's power are regulated in the trust contract, those restrictions operate only at the level of obligation, but would not invalidate judicial acts.⁶⁷³ What makes it worse is that there is no equivalent provision regulating the settlors' obligation to remedy their breach of trust, as there is for trustees in article 22. Moreover, it is against the civil law principle of ownership that the settlor retains the ownership of trust property while the rights to possess, utilize, seek profit from and dispose of the property are granted to the trustee and beneficiary. In other words, the ownership cannot be retained when its four aspects of rights are all distributed to others.⁶⁷⁴

Furthermore, the design of settlors' retention of ownership may cause the trust property to be ownerless. This is because in some situations the ownership of trust property will be in a legal limbo such as upon the death of a settlor or upon his loss of capacity. This problem is created by the provisions of Chinese trust law. The reason a settlor's death or loss of capacity

⁶⁷³ Reid, "Conceptualising the Chinese Trust", *supra* note 189 at 11, n 46.

⁶⁷⁴ Yu, *How to Localize*, *supra* note 508 at 87.

will cause a legal limbo of ownership is reflected in two aspects: no provision of the settlors' replacement is regulated in law; and a trust will keep continuing in the absence of settlors. For instance, pursuant to article 52 of the *Trust Law of China*, a "trust will not be terminated due to the facts that the settlor or trustee dies, loses his capacity for civil conduct ... except it is otherwise stipulated in this Law or the trust documents".⁶⁷⁵ In other words, a trust cannot fail for a want of a settlor or a trustee, which is one of the essential differences between trust and contract.⁶⁷⁶ Therefore, in the absence of regulations of settlors' replacement, a legal limbo of ownership occurs when a trust keeps continuing while no new settlors succeed to the original one. In contrast, if trustees are entitled the ownership of trust property, when they die or lose their capacity, a new trustee, i.e. a new owner, can be assigned in a variety of ways as provisions regulate. Therefore, it will not cause a legal limbo. In common law, the appointment of trustees is pursuant to either the trust instruments or a court order.⁶⁷⁷ In China, according to article 40 of the Trust Law,

a new trustee shall be appointed according to the provisions in the trust documents; where there are no such provisions in the documents, the settlor shall make the appointment; where the settlor does not make the appointment or is incapable of doing so, the beneficiary shall designate one; where the beneficiary is a person with no or restricted capacity for civil conduct, his guardian shall, in accordance with law, make the appointment on his behalf.⁶⁷⁸

In addition, besides the legal limbo of trust ownership, another problem caused by the design of settlor's retention of ownership is that it conflicts with the regulation that trust property does not devolve upon the settlor's heirs when the settlor is not the sole beneficiary. The reason is that if the settlors retain the ownership of trust property, the trust property will naturally be

⁶⁷⁵ *Trust Law of China*, *supra* note 1, art. 52.

⁶⁷⁶ Smith, "Trust and Patrimony", *supra* note 2 at 337.

⁶⁷⁷ *Ibid.*

⁶⁷⁸ *Trust Law of China*, *supra* note 1, art. 40.

attributed to their heirs.⁶⁷⁹ However, according to article 15 of the *Trust Law of China*, the trust property shall not become the settlors' legacy or liquidation property except when the settlor is the sole beneficiary. It states:

Where, after a trust is created, the settlor dies or is dissolved or cancelled according to law, or is declared bankrupt, and the settlor is the sole beneficiary, the trust shall be terminated, and the trust property shall be his legacy or liquidation property; where the settlor is not the sole beneficiary, the trust shall subsist, and the trust property shall not be his legacy or liquidation property; but if the settlor is one of the co-beneficiaries and dies or is dissolved, or cancelled according to law, or is declared bankrupt, his right to benefit from the trust shall be deemed his legacy or liquidation property.⁶⁸⁰

In this case where there are multiple beneficiaries, the trust property does not devolve on the settlor's heirs. But then who holds it after the settlor's death?

C. Ownerless Trust Property

The third means of transitioning into a system of dual ownership into China is via implementation of ownerless trust property. This occurs when a settlor relinquishes his or her ownership of trust property. Thus, in this example, neither the settlor, trustee or beneficiary would retain title over the trust property. Concurrently, the trustee assumes the management and administration of the trust property. The reason for the design of ownerless trust property is to reconcile the civil law's requirement that ownership in civil law include benefit with the prohibition of the trustee benefitting from trust property. This design neatly gives effect to the theory that a trust is plainly a machinery of administration. As discussed in Chapter II, a prominent example of this solution is the patrimony by appropriation adopted in Quebec law,

⁶⁷⁹ *Law of Succession of the People's Republic of China*, (Adopted at the Third Session of the Sixth National People's Congress, promulgated by Order No. 24 of the President of the People's Republic of China on April 10, 1985, and effective as of October 1, 1985), art. 3.

⁶⁸⁰ *Trust Law of China*, *supra* note 1, art. 15.

over which none of the settlor, trustee or beneficiaries has the title of trust property. Unfortunately, different from the theory of patrimony in Quebec, China cannot introduce the concept of patrimony, or the theory of ownerless trust property, due to a number of ingrained conceptual hurdles with Chinese law. At least in the Chinese case, the binary system of real rights and personal claims is a less invasive solution.

Specifically, the theory of ownerless trust property leads to a number of difficulties in legal practice. For instance, it may be hard for judges and lawyers to accept that all the properties held under the trust are technically ownerless. Besides, if the trust had no owner, under whose name should the relevant property be registered? To whom should tax be charged? Who has the *locus standi* to bring an action for trespass to the trust property? All of these problems, practical in nature but nonetheless important in their legal consequences, weaken the attractions of ownerless trust.

Yet a more fundamental argument against the adding of patrimony is simply that it is alien to and superfluous in Chinese law. China has no history of patrimony, but does have categories of rights, i.e. real rights and personal claims. These categories of rights are substantially of the same nature as dual ownership. As a result, it is simply unnecessary to introduce a concept of patrimony in China. The cost or the disadvantages of adopting the ownerless patrimony theory, which is alien to Chinese law, might far outweigh the advantages of introducing the trust in China. Moreover, the uniqueness of the regulation of ownerless patrimony would cut China off from international practice since most civilian jurisdictions adopt the theory of trustee's ownership but only a few scholars support the theory of ownerless trust

property. Adopting the binary system of real rights and personal claims, and ascribing ownership to the trustees, however, is compatible with China's legal tradition and its existing legal framework.

D. Transfer Ownership to Trustees

The most widely recognized solution to the introduction of the trust into civilian jurisdictions is to transfer the ownership to trustees and subject them to a fiduciary duty. This is akin to the solution adopted by Scots law, and also allows the beneficiaries to enforce the trust agreement, as well as the fiduciary duties against the trustee, because generally the doctrine of privity is not recognized in civil law.⁶⁸¹

The reason to say transferred ownership is the most broadly accepted solution, is that this design has been considered, and, to some extent, 'vetted' in international and regional legal practice. For instance, the *Hague Trust Convention* recognizes the transfer of trust ownership to trustees although it does not clearly require that trustees are the owner of trust property. In article 2, it states that "(b) title to the trust assets stands in the name of the trustee or in the name of another person on behalf of the trustee." Moreover, it stipulates that trust assets are "placed under the control of a trustee" and "(c) the trustee has the power and the duty, in respect of which he is accountable, to manage, employ or dispose of the assets in accordance with the terms of the trust and the special duties imposed upon him by law."⁶⁸² Regionally, this solution has also been

⁶⁸¹ Chen, *supra* note 663 at 51.

⁶⁸² *Hague Convention*, *supra* note 200, art. 2.

adopted in Japan⁶⁸³, South Korea⁶⁸⁴, and Taiwan⁶⁸⁵. International experience has shown that transferring ownership to trustees has provided the best solution to the problem of settlor abuse and legal limbo of ownership of trust property in China.

In addition to being broadly accepted in legal practice, the solution of transferring trust ownership to a trustee is consistent and coherent with ownership theory in China. While the main right of a beneficiary is the enjoyment of the benefits incurred from the trust property, the trustee retains control over the way in which the property is used, even if that power is curtailed by the terms of the trust. Most significantly, he has the power to dispose of the property, a right not enjoyed by the beneficiary. In other words, the trustee has the right to alienate the property in such a way that concords most with the benefits typically accorded to owners in the civil system pursuant to the legal maxim *nemo plus juris ad alium transferre potest quam ipse habet* (no one can transfer more rights to another than he himself has). According to this maxim, alienation implies ownership; enjoyment on the other hand, which the trustee does not have in any case, does not.⁶⁸⁶ By virtue of the possibility for alienation therefore, the rights of the trustee fall best into the definition of ownership. Definitionally speaking therefore, the trustee is best suited as a candidate for the owner of trust property.

Another advantage of this solution, and another reason to adopt it in China, is that the entitlement of ownership gives a trustee the most leeway in administering the trust property. This is because, unlike an agent, the trustee is not required to disclose the existence of the trust when

⁶⁸³ *Trust Act of Japan*, Act No. 108 of 2006.

⁶⁸⁴ *Trust Act of the Republic of Korea*, Act No. 10924 of 2011 (with effect from 26 July 2012).

⁶⁸⁵ *Trust Law of the Republic of China*, promulgated on 26 January 1996; amended on 30 December 2009.

⁶⁸⁶ Chalmers, *supra* note 156 at 142.

entering into transactions, giving the trustee more discretion in his managing of trust properties. However, concern about this solution arises as to the beneficiaries' having less protection than their counterparts in common law, because the trustee's ownership is absolute in civil law. For example, in some jurisdictions, beneficiaries are not protected from either a trustees' bankruptcy or from the wrongful transfer of trust property to a third party.⁶⁸⁷ Giving a beneficiary the right to claim against a trustee as well as restricting the trustee's rights over the trust, are possible solutions to this concern. Both solutions, of course, would need to be found within the text of the trust agreement itself. Another big concern about this solution is how to prevent the property falling into the hands of trustee's creditors or heirs. In order to solve this problem, specific rules regarding the independence of the trust property⁶⁸⁸ must be established. Instead of adopting the rule of multiple patrimonies held by trustee, which is alien to the Chinese legal system, China recognizes the rule of independence that is consistent with its other rules.⁶⁸⁹

3. Design of the Binary System of Real Rights and Personal Claims in China

As analyzed above, although the theory of ownerless patrimony has several strengths, the binary system of real rights and personal claims is more in line with the Chinese legal framework, especially when combined with other legal mechanisms; for instance, the regulation of trust instruments, the principle of the independence of trust property, and the duty of care in civil law. This thesis argues that, in order to better fulfill the function of a trust function, especially its financial aspect, the binary system of real rights and personal claims should be

⁶⁸⁷ Ho, *Trust Law in China*, *supra* note 418 at 39. See n 58, the concept of fiduciary ownership under Dutch law.

⁶⁸⁸ *Trust Law of China*, *supra* note 1, art. 16.

⁶⁸⁹ Yiwei Shen, *The Rule of the Independence of Trust Property* (LLM Thesis, Ningbo University, 2010) [unpublished] [translated by author].

adopted and the unitary ownership should be attributed to the trustee in the form of *prima facie* ownership. With regard to the beneficiary, he would hold a right in the nature of ‘special personal claims’.⁶⁹⁰ Put simply, China ought to adopt a system in which the legal ownership mechanism, at least as known in a dual ownership system, would be interpreted as giving the trustee unitary ownership of the trust property while accommodating equitable ownership as a ‘special right of claim’ under the binary system of real rights and personal claims in China. The section A first indicates that the binary system of real rights and personal claims in China plays the same role as dual ownership. Sections B and C then provide a detailed explanation of the trustee’s real rights under Chinese law, as well as outline the beneficiary’s special personal claim under the same, respectively.

A. The Binary System of Real Rights and Personal Claims Plays the Same Role as Dual Ownership

The main intention of the trust institution is the financial management of trust property and the security of the beneficiaries’ interests.⁶⁹¹ To realise this intention, dual ownership was created in the common law to balance the trustee’s independent control over trust property and the beneficiaries’ enjoyment of trust benefits. In the same fashion, the binary system of real rights and personal claims splits property management in the form of *prima facie* ownership and

⁶⁹⁰ This concept of ‘special personal claims’ believes that the beneficiary’s rights should be explained as personal claims. But different from typical personal claims, the beneficiary’s rights are special because beneficiaries have some rights beyond the scope of personal claims, for instance, the right to supervise trust affairs or the right to revoke trustees’ disposal of trust assets. In addition, the theory of ‘special personal claims’ is distinguished from the theory of ‘special right’ which demonstrates the beneficiary’s right as a special kind of right that falls neither in the scope of real rights nor personal claims. Details of the theory of special personal claims will be explained in the next section.

⁶⁹¹ Yu, *How to Localize*, *supra* note 508 at 83.

beneficial enjoyments between trustees and beneficiaries. It grants unitary ownership to the trustees so as to enable them to maximize the property management function. Meanwhile, it imposes corresponding obligations, in particular fiduciary duties, on the trustees so as to ensure that they manage the trust property for the benefits of the beneficiary. Therefore, under the binary system, beneficiaries' interests are protected through their personal claims against the trustees. Moreover, trust property is immune from the personal creditors of the trustees, due to the principle of the independence of trust property.

As to why trustees' unitary ownership is defined as *prima facie* ownership, this thesis argues that it is because the trustee's ownership is actually limited to the right to control and administer the trust property. The trustees cannot obtain benefits arising from the property.⁶⁹² Moreover, as a result of the separation of trust property from the trustee's personal property, the trustee cannot arbitrarily dispose of trust property. This can be demonstrated in several ways: unlike a real owner, the trustees cannot freely abandon trust property but have duties to safeguard the trust property and exercise reasonable care over it,⁶⁹³ they have no right to put up trust property as collateral on their own personal obligation and⁶⁹⁴ they are not liable for any accidental losses of the trust property, or for costs awarded to a third party in an action against the trustees as legal owners of the trust property.⁶⁹⁵ Those differences between a trustee's ownership and real ownership are due to the fact that the real purpose of the trust is not to give the trust property to the trustees as a gift, but simply to authorize them to manage and administer

⁶⁹² Eileen E. Gillese & Martha Milczynski, *The Law of Trusts*, 2nd ed (Toronto: Irwin Law Inc., 2005) at 143.

⁶⁹³ Thomas & Hudson, *supra* note 88 at 284, 292.

⁶⁹⁴ Moffat, *supra* note 650 at 458.

⁶⁹⁵ See *Benett v Wyndham* (1862) De GF & J 259; *Re Raybould*, [1900] Ch 199.

the trust property for the benefit of the beneficiaries or a specified purpose.⁶⁹⁶ Therefore, obligations, especially fiduciary duties, are imposed on the trustees so as to ensure that they exercise their unitary ownership for the interests of beneficiaries or for the fulfillment of a certain purpose.

In addition, because of the similarity in nature, equitable ownership corresponds to a beneficiary's right under the binary system of real rights and personal claims in civil law. The similarities between the beneficial right and equitable ownership are that they both grant a beneficiary a right to obtain trust benefits, and a right to follow trust property. With regards to the right to trust benefits, its achievement relies on the trustee's payment in that the beneficiary is not entitled to the ownership and control of trust property. For example, in Quebec law, the rule is clear that the beneficiary's right is only against the trustee in his quality as trustee; it is a personal right against the trust patrimony.⁶⁹⁷

As to the similarities in the right to follow trust property in Canadian and British common law, when a trustee disposes of trust property in breach of the trust, based on their equitable ownership, beneficiaries not only have the right to claim damages but also a right to follow the trust property.⁶⁹⁸ The same is true for the beneficiary in Chinese law. It authorizes beneficiaries a right of claim in the internal legal relationship of trust, that is a right to claim damages against a trustee and request trustees to do certain acts. Meanwhile, in the external relationship, the beneficiary's right gives beneficiaries a right to annul trustees' disposition of

⁶⁹⁶ Gillese & Milczynski, *supra* note 692 at 6.

⁶⁹⁷ Smith, "Trust and Patrimony", *supra* note 2 at 352.

⁶⁹⁸ Gillese & Milczynski, *supra* note 692 at 172.

trust property when it is against their interests once a third party enforces the trust property.⁶⁹⁹ The beneficiary has a right to follow the trust property, both the original product and its derivatives, and to request the return or recovery of the property against third party transferees who are not *bona fide* purchasers for value without notice.

Therefore, although ownership in China is absolute and indivisible, it does not prevent the law from imposing obligations on the trustees or prohibit the trust instrument from specifying the rights and obligations of trust parties. As a result of this possibility and the principle of independence of trust property that protects the trust property against trustee's personal creditors, it is possible to apply the binary system of real rights and personal claims in China that accords the unitary ownership of trust property to a trustee, while granting beneficiaries the enjoyment of trust benefits and a right to claim against the trustee.

B. Accommodate Legal Ownership as Trustee's Unitary Ownership in China

As discussed earlier, it is better to retain the unitary ownership of trust property in China and entitle the ownership to a trustee, but not a settlor. In practice, this solution is the only one to have received judicial support, although given with hesitation and reservations. Moreover, in theory, it is suggested that the best method is to transfer the trust property to the trustee, subject to fiduciary and other obligations. In this case, the trustee is required to act for the best interests of the beneficiary. This design best fits the international common law conception of trusts into the Chinese legal framework while avoiding damage to the function and conception of the trust itself. Specifically speaking:

⁶⁹⁹ *Trust Law of China*, *supra* note 1, art. 49.

(1) Granting the trustee unitary ownership leads to no excessive expansion of trustee's rights

Because trustees in modern trust systems are engaged in a range of investment business activities, they are required to have more discretion than before in order to respond timely to rapidly changing markets. Nevertheless, as compared to the modern trustee's rights, the trustee's rights under traditional dual ownership are less extensive, in that they cannot necessarily meet the positive-management requirement of portfolio trusts. As a result of the limitations of trustee rights under the dual ownership system, they consequently hinder the development of trusts. Therefore, a moderate expansion of the trustee's rights via the granting and definition of trustee-based unitary ownership would appear to be a *de facto* necessity.

Under modern common law, a trustee's powers have expanded significantly. For example, in the United States, numerous attempts have been made to reform trust law and to expand trustees' rights to flexibly manage trust properties.⁷⁰⁰ Additionally, the status of the trustee has been changed by the expansion of his rights with the increasing use of trusts in commercial matters, especially in the area of mutual funds and pension funds.⁷⁰¹ For instance, the *Uniform Trust Code*⁷⁰² allows a trustee to "delegate duties and powers that a prudent trustee of comparable skills could properly delegate under such circumstances".⁷⁰³ This requires that the trustee exercises reasonable care, skill and caution in selecting and supervising the delegate. The *Uniform Trust Code* also stipulates a series of provisions "designed to protect the trustee from

⁷⁰⁰ Tianmin Zhang, *Trust Without Equity* (Beijing: CITIC Press, 2004) at 211 [translated by author].

⁷⁰¹ Grenon, *supra* note 383 at 249.

⁷⁰² National Conference of Commissioners on Uniform State Laws, *Uniform Trust Code* (Chicago: NCCUSL, 2005).

⁷⁰³ *Ibid.*, §807(a), (c). Insofar as delegation among co-trustees is concerned, however, the UTC provides for majority rule (§703(a)).

liability, including a limitation date on claims and reliance on an exculpatory clause”.⁷⁰⁴

(2) Granting the trustee unitary ownership would not undermine the beneficiary’s rights

A trustee’s unitary ownership would not undermine the beneficiary’s rights because beneficiary’s rights have always been very limited in traditional dual ownership systems. The reason for this is, as discussed earlier, the trust originated in the feudal system of medieval England, and was designed to circumvent the law, in such a way as to legally avoid tax, evade the law of forfeiture for treason and escheat by felony, sidestep the statutes of mortmain, or flummox a settlor’s creditors.⁷⁰⁵ Therefore, when the beneficiary’s rights were infringed, beneficiaries would not be able to take legal action in the common law courts. The beneficiary’s rights were merely an unenforceable hope that the trustee would decide to exercise his power in favour of that beneficiary. As a result of the trustee’s equity-based enforcement mechanisms, the performance of the ancient trust mainly depended on the trustees’ integrity, rather than on litigation or common law courts’ enforcement. The beneficiaries could only resort to a court of equity and use their equitable ownership to constrain the trustees’ common law ownership.

In comparison to the beneficiary’s rights in the traditional trust, the beneficiary’s rights under the binary system of real rights and personal claims in China are enhanced, since these rights are no longer simple moral rights, but rather rights protected by law. Even though today under common law trusts, the beneficiary’s right is also a legal right, the beneficiary’s rights in

⁷⁰⁴ *Ibid.*, §1008. It is not possible to exculpate a trustee completely. Pursuant to §1008(a)(1), no protection is available if the breach was “committed in bad faith or with reckless indifference to the purpose of the trust or the interests of beneficiaries”. Pursuant to §1008(a)(2), the clause will be unenforceable if it was inserted as a result of the abuse of a confidential or fiduciary relationship between the trustee and the settlor.

⁷⁰⁵ Oosterhoff, *supra* note 31 at 11.

Chinese trust law still appear relatively better protected. In China, the trust is not used to avoid tax or law, but used rather as a mechanism to facilitate investment banking, financing and property management.⁷⁰⁶ It requires a trustee to administer and dispose of trust assets as a manager for the benefits of the beneficiary. Perhaps more importantly, the beneficiary's right has a legal, rather than solely equitable, base, and the trust agreement itself between settlors and trustees is legally binding and enforceable.⁷⁰⁷

(3) Granting the trustee unitary ownership brings no change to the position of trust parties

Granting the trustee unitary ownership would not expand the trustee's rights or undermine the beneficiary's interests nor would it bring any change to the position of the settlor, the trustee, or the beneficiary. Firstly, the settlor's position is basically the same under the dual ownership system and the binary system of real rights and personal claims. Settlors in both of these systems lose their ownership of trust property. Additionally, their intervention in the management of the trust is mainly based on the provisions of the trust instrument between the settlor and the trustee.

With respect to the trustees, their rights and obligations are similar under the dual ownership and the binary system of real rights and personal claims. In both systems, trustees control, prudently manage and dispose of trust property. Additionally, both systems incur loyalty obligations for the beneficiary's best interests. In both cases, the rights construction is similar: in

⁷⁰⁶ Bihua Yuan, "Inheritance and Localization of Trust Law: A Comparative Study of Trust law" (2003) 6 Guangdong University of Business Journal 78 at 81 [translated by author].

⁷⁰⁷ *Trust Law of China*, *supra* note 1, art. 8.

common law, a trustee holds the ownership and actual control of trust property, whereas these rights are restricted by the beneficiary's equitable ownership.⁷⁰⁸ Likewise, under the binary system of real rights and personal claims, a trustee has *prima facie* (albeit of a unitary kind) ownership of trust property as long as his or her rights are restricted by the beneficiary's personal claims.

As to the beneficiary, his rights to obtain trust benefits, supervise trust management, and follow trust property transferred to a malicious third party are likewise substantially similar in both systems. In common law, although the beneficiary cannot directly control or manage trust property, he is entitled to equitable ownership, based on his right to claim against trustees.⁷⁰⁹ Similar to the enjoyment of equitable ownership, under the binary system, beneficiaries as a class are entitled to personal claims against trustees and supervise trust affairs based on the right of personal claims. In addition, they have a right to follow trust property once the property is transferred to a malicious third party. Under common law, beneficiaries can also follow trust property transferred from trustees to a third party, who is not the equity darling, despite the absence of the defined right of revocation.⁷¹⁰ Therefore, it seems that the common law right to follow trust properties actually corresponds to the civilian right of revocation. This can be proved by the similarity of third parties' defenses against beneficiary rights, which shows that even the position of a third party is not affected by the persistence of unitary ownership. For example, an innocent third party, in both dual ownership and the binary system, can confront a beneficiary following of trust property based on the defense that he or she paid consideration for the property

⁷⁰⁸ Gillese & Milczynski, *supra* note 692 at 158, 172.

⁷⁰⁹ *Ibid* at 172-74.

⁷¹⁰ Oosterhoff, *supra* note 31 at 36-37.

and did not know it was trust property when the transfer occurred.

In short, the design of the trustee's unitary ownership would cause no fundamental change of the position, the rights and obligations of the settlor, trustee and beneficiary in a dual ownership system. Indeed, the trustee's unitary ownership of the binary system of real rights and personal claims plays a similar function as the trustee's legal ownership of dual ownership in common law. In addition to the trustee's legal ownership, the beneficiary's equitable title is explained as a special personal claim in China.

C. Accommodate Equitable Title as a Special Personal Claim in China

As discussed in Chapter I, in English common law, a broadly accepted theory of the nature of the beneficiary's rights holds that the beneficiary's rights are predicated both on his personal rights against the trustees and on his proprietary interests in external relationship with third parties.⁷¹¹ By this reading, a beneficiary may bring proceedings *in personam* against the trustees for breaches of trusts. Such a claim may be subject to time limits imposed by a limitation statute. Moreover, a proprietary right may be instituted against the trustees to recover (trace) the trust property.⁷¹² There is no inconsistency between having both rights *in personam* and proprietary rights: both can easily coexist, although it may be necessary in certain cases to focus on one rather than the other.⁷¹³ Nevertheless, it is worth noting that having a proprietary interest in the trust does not mean the beneficiary holds an ownership of the trust property.

⁷¹¹ Thomas & Hudson, *supra* note 88 at 26.

⁷¹² Mohamed Ramjoin, *Text, Cases and Materials on Equity and Trusts*, 4th ed (Oxon: Routledge Cavendish, 2008) at 539.

⁷¹³ Thomas & Hudson, *supra* note 88 at 160.

China cannot simply adopt the common law's theory of the nature of the beneficiary's rights. In order to appropriately accommodate equitable ownership in China, a study of the nature of beneficiary's rights and equitable ownership in that country is important. In academia, three theories arise as to the characteristics of equitable ownership in Chinese law: real right theory, personal claim theory, and the theory of co-existing real rights and personal claims.⁷¹⁴ Using comparative studies to ground its analysis, this thesis has argued in favour of the personal claim theory, and posits that equitable ownership should be explained as a special personal claim in China. In order to support this position, this section first examines and criticizes the other two theories before coming to the analysis of the personal claim theory.

(1) Challenges of the real right theory and the theory of co-existing real rights and personal claims

(a) Challenges of the real right theory

Most legal scholars have rejected the claims of the theory of real rights. For instance, Reid rejects this theory and states that it can lead the public to believe that the beneficial interest of a beneficiary over the trust property is a right *in rem*.⁷¹⁵ This thesis agrees with Reid's objection and acknowledges that the real right theory faces a number of challenges in China. First, the beneficiary's right does not satisfy the definition of real right (物权) in the *Property Law of China*. Article 2, paragraph 3 of the *Property Law of China* stipulates a real right as "the exclusive right of direct control over a specific thing in accordance with law, and includes

⁷¹⁴ Reid, "Conceptualising the Chinese Trust", *supra* note 189 at 12-16.

⁷¹⁵ *Ibid* at 14, n 59.

(exhaustively) ownership, usufructuary rights, and security rights.”⁷¹⁶ Nevertheless, the *Trust Law of China* grants the beneficiary no exclusive right to manage or control the trust property. Moreover, the beneficiary’s right cannot be viewed as a usufructuary right since a usufructuary right requires the possession of the relevant property.⁷¹⁷ As noted, because in trusts it is the trustee rather than the beneficiary who holds the possession of trust property, this right would appear to be immediately precluded. In a similar vein, the beneficiary’s right is not a security right because a security right gives a secured creditor a priority over unsecured creditors in having his claim be paid with the trust property.⁷¹⁸ However, the beneficiary has no priority against other trust creditors except for the personal creditors of a trustee due to the independence of trust assets.⁷¹⁹

Furthermore, even if we admit the beneficiary’s right as a real right, the right is not attributed to a specific type of real rights. Pursuant to article 5 of the *Property Law of China*, “[t]he varieties and contents of real rights shall be prescribed by law.”⁷²⁰ Nevertheless, the beneficiary’s right is not expressly or implicitly regulated as a type of real right by the *Trust Law of China* or other legislations. In order to avoid recognizing the beneficiary’s right as a right directly enforceable against trust property, the *Trust Law of China* stipulates that the legal bases of the enforcement of the beneficiary’s rights are the trust documents but not the laws⁷²¹.

⁷¹⁶ *Property Law of China*, *supra* note 532, art. 2.

⁷¹⁷ Xianzhong Sun, *Property Law* (Beijing: Law Press, 2008) at 79 [translated by author].

⁷¹⁸ Zejian Wang, *Principles of Personal Claims* (Beijing: Beijing University Press, 2009) at 13 [translated by author].

⁷¹⁹ Dagang Chen, *Trust Law and the Innovation of Trust System in China* (Shanghai: Lixin Accounting Publishing House, 2003) at 113 [translated by author].

⁷²⁰ *Property Law of China*, *supra* note 532, art. 5.

⁷²¹ *Trust Law of China*, *supra* note 1, art. 9: The following items shall be stated clearly in the written documents required for the creation of a trust: ... (5) the form and means through which the beneficiary gains benefits from the trust.

Moreover, although article 5 of the *Property Law of China* does not prevent legislation from creating new types of real rights, it is still difficult to classify the beneficiary's right as a real right because of the instability inherent in the nature of (typically fungible) trust property. As noted in Chapter III, the form in which a particular property which makes up the trust fund is liable to change from time to time dependent on the trustee's management. For example, a property could readily be converted from cash to securities depending on the trustee's management decisions. Moreover, if the beneficiary's right is viewed as a real right, it will result in assets held in charitable trust becoming ownerless, since the beneficiary in a charitable trust is uncertain. As a consequence, the beneficiary's right cannot be defined as a real right. The Chinese trust law does not recognize it as a real right, at least not until the trust is terminated and the ownership is transferred to the beneficiary.

(b) Challenges of the theory of co-existing real rights and personal claims

Another theory regarding the nature of equitable ownership is the theory of co-existing real rights and personal claims. This theory intends to create an in-between right, which is neither complete real right nor personal claim. It grants a beneficiary a right to prevail against creditors of trustees, which also provides a neat doctrinal explanation for the immunity of trust property from those creditors' claims.⁷²²

This theory or similar ideas has been proposed by several commentators to accommodate the equitable ownership in the Chinese trust law. For instance, Professor Ho holds that a beneficiary has a *sui generis* right, which has features of a real right, such as enforceability

⁷²² Reid, "Conceptualising the Chinese Trust", *supra* note 189 at 15.

against the trustee's creditors, successors and some transferees.⁷²³ Additionally, Tony Honoré states that if a trustee has the right of management, a beneficiary has the right of enjoyment. That right of enjoyment, would, according to Honoré, include at least the 'exclusionary' right provided for it by article 16 of the *Trust Law of China*, that is to say, the right to exclude trust property from the claims of private creditors.⁷²⁴ Rebecca Lee goes even further than this conception of exclusionary rights and argues that "[d]espite the fact that the beneficiary holds only one incident of ownership, this does not prevent him being recognized as the owner where appropriate."⁷²⁵ It is worth noting however, that the beneficiary's 'form of (property) ownership right' is not a right over the property in a trust, but only an indirect right arising from the right of trustees in relation to the trust property. In addition, she notes that the right of exclusion, which constitutes the beneficiary's core proprietary right under the trust, explains the doctrinal requirement of keeping trust assets separate from the inherent property of the trustee so that they are immune from the claims of third parties.⁷²⁶

The theory of co-existing real rights and personal claims takes a bold step in the theoretical ideas of the nature of equitable ownership. This effort, however, is not fully successful. The weakness of this theory is that the type of right belonging to both real rights and personal claims has never been recognized in civil law systems. Additionally, with respect to Honoré and Lee's argument that the beneficiaries' interest has a real right nature because the beneficiaries have the 'exclusionary' right, the right to exclude trust property from the claims of private creditors, this thesis instead posits that the nature of real right is not the only explanation

⁷²³ Ho, *Trust Law in China*, *supra* note 418 at 117.

⁷²⁴ See Tony Honoré, *Making Law Bind: Essays Legal and Philosophical* (Oxford: Clarendon, 1987) at ch 8.

⁷²⁵ Lee, "Conceptualizing the Chinese Trust", *supra* note 605 at 667.

⁷²⁶ *Ibid.*

for the beneficiary's exclusionary right. The rule of the independence of trust property can simply explain it.

(2) Analysis of the personal claim theory

The personal claim theory, which has been broadly accepted in civilian jurisdictions, states that the nature of the beneficiary's right is a personal claim against the trustee.⁷²⁷ This theory implies that the ownership of trust property is granted to trustees. Under this theory therefore, trust properties in charitable trusts will not become ownerless when beneficiaries are uncertain. Compared with the other two theories mentioned above, this thesis' major premise appears to be close to the personal claim theory. Where the thesis differs from the personal claim theory is in its assertion that the beneficiary's right has a broader meaning as compared to a typical personal claim. Notwithstanding these differences however, China is not prevented from adopting the personal claim theory and interpreting equitable ownership as a special personal right. Why this is the case is explained below.

(a) Beneficiary's right has a broader meaning than typical personal claims

The reason to say that a beneficiary's special personal right has a broader meaning than typical personal claims is, first that, under Chinese law some of the beneficiary's rights are beyond the scope of personal claims. Examples of this expanded scope include the rights to supervise trust affairs, challenge courts' enforcement, accept a trustee's resignation and rescind a trustee's disposition of trust property in violation of trust purposes. Moreover under Chinese law,

⁷²⁷ Haiyong Yu, "China's Reception of the Dual Ownership of Anglo-American Trust" (2010) 3 Modern Law Science 159 at 159 [translated by author].

beneficiary's right is stronger than a typical personal claim such as a contractual right or a debt. For instance, the trust properties are immune from the claims of the trustee's personal creditors due to the segregation of property from the trustee's personal assets.⁷²⁸

Furthermore, and different from the typical personal claims that bind two parties in a creditor-debtor relationship,⁷²⁹ is the fact that in China a beneficiary's right can affect a third party's right in trust property. Proof of this assertion is found in articles 22 and 49 of the *Trust Law of China*, which stipulate that a beneficiary can request the People's Courts to annul the trustee's disposal of trust property against trust purposes, and, consequently, ask the trustee to restore the trust property or offer compensation in the event of a breach of trust.⁷³⁰ Although the beneficiary's claim is not directly against a third party, it can affect the third party's rights in trust property by annulling trustee's transfer of the property to the third party. Professor Smith in his "Trust and Patrimony" holds a similar position in the common law: holding that the beneficiary's only rights are those held in the rights of his trustee. That said, he notes that some beneficiary rights sometimes have effects on third parties, a claim substantiated by his remark that "some transferees of the trust property cannot take it unencumbered by the claims of the beneficiary. In particular, in what the common law considers only a special case of this general principle, the creditors of the trustee cannot take trust property".⁷³¹ Consequently, by virtue of its effect on third parties, the beneficiary's special personal claims depart from the principle of typical personal claims, which hold that the creditor-debtor relationship only binds the relevant

⁷²⁸ *Trust Law of China*, *supra* note 1, art. 16.

⁷²⁹ Wang, *supra* note 718 at 15.

⁷³⁰ *Trust Law of China*, *supra* note 1, art. 49, para 2: If the trustee conducts any of the acts listed in the first clause of Article 22 and any of the joint beneficiaries applies to the people's court for withdrawing the disposition, the ruling of cancellation made by the people's court shall be of equal effect to all of the joint beneficiaries.

⁷³¹ Smith, "Trust and Patrimony", *supra* note 2 at 343.

parties but not a third party.

(b) The difference between a beneficiary's right and a typical personal claim does not prevent the introduction of personal claims theory into China

Although the beneficiary's right is not exactly the same as a personal claim, the difference between them does not prevent the introduction of personal claim theory into China. As professor Smith argues "[t]his idea is not alien to the civil law, which also recognizes that while a personal obligation does not create a real right but only a claim against a particular debtor, nonetheless it is possible that there might be claims in delict against third parties who wrongfully interfere in the performance of an obligation".⁷³² In China, even though the format of the beneficiary's rights is new, this type of right is not completely novel to Chinese law. There is a well-accepted class of personal claims enforceable against third parties, such as the personal claim regulated in article 74 of the *Contract Law of China*. In general however only real rights are exigible against third parties. Moreover, the beneficiaries' right to supervise trust affairs and annul a trustees' wrongful disposal of trust property, both of which are beyond the scope of personal claims, can be interpreted as the appurtenance and the preservation of the personal claims respectively in Chinese law. This is for the following reasons:

Firstly, jurists have interpreted the beneficiary's right to supervise trust affairs as the appurtenance of personal claims.⁷³³ It is suggested that although the right of supervision directly falls into neither personal claims nor real rights, it is in essence derived from the beneficiary's

⁷³² *Ibid.*

⁷³³ Yu, "China's Reception", *supra* note 727 at 164.

personal claims to ensure that the trustee carries out the terms of the trust. Namely, the right to supervise is an appurtenance of the beneficiary's personal claims against the trustee. The reasons to support this opinion are that the right of supervision must be transferred along with the transfer of beneficiaries' personal claims. It is a legal rule in Chinese law that a beneficiary may not convey her personal claim while retaining the right of supervision. In the same fashion, once the beneficiaries waive their personal claims, the right of supervision must also be waived. In other words, a beneficiary cannot hold the right of supervision if he has already waived his personal claims.⁷³⁴ From the perspective of its function and position therefore, the right of supervision is in a subordinate position, to support and realize the beneficiaries' personal claims. Thus, the right to supervision is essentially an auxiliary and derivative right of the personal claims which are the beneficiary's core rights. The relationship between the beneficiary's personal claims and the right of supervision can therefore be described as that between a principal claim and its appurtenance.

Secondly, with regards to the beneficiary's right to annul the trustee's disposal of trust property against the trust purpose, this thesis believes that this right exists to preserve the beneficiaries' personal claims. This right comes from the nature of a creditor's right to revoke, rather than a right of recovery based on real rights.

Some scholars in China argue that the beneficiary's right of revocation is a real right.⁷³⁵ Their reasoning derives from the similarity in regulations between the right of recovery in real rights and the right of revocation in trusts. The rule of recovery is regulated in article 34 of the

⁷³⁴ Yu, *How to Localize*, *supra* note 508 at 111.

⁷³⁵ See Wen & Feng, *supra* note 618.

Property Law of China, states that “[w]here a realty or chattel is under an unauthorized possession, the right holder may require the returning of the original object”.⁷³⁶ The right of revocation in the trusts holds that a beneficiary has a right to follow the trust property and annul a trustee’s disposal of it in breach of trust purpose. Consequently, the beneficiary can request the return of property or compensation as if the disposition never happened. This is deemed as the effect of the revocation. In China, the right of revocation is stipulated in article 22, paragraph 1 of the *Trust Law of China*. This article and paragraph stipulate that:

Where the trustee disposes of the trust property in breach of the purposes of the trust, or causes losses to the trust property due to his departure from his administrative duties or improper handling of trust business, the settlor shall have the right to apply to the People’s Court for annulling such disposition and the right to ask the trustee to restore the property to its former state or make compensation. Where a transferee of the said trust property accepts the property while knowing the violation of the purposes of the trust, he shall return the property or make compensation.⁷³⁷

These regulations present similarities between the right of recovery under the real rights regime and the right of revocation in trusts. However, it is ignored that the right of recovery in real right is not the only analogue of the beneficiaries’ right of revocation, and the real right is not the only basis of the right of revocation. In fact, the right to annul the trustee’s wrongful disposal can also be based on personal claims. Likewise, and pursuant to the right of revocation in personal claims, a creditor may also request the court to annul a debtor’s disposal of property or right when it jeopardizes the realization of personal claims. As regulated in article 74, paragraph 1 of the *Contract Law of China*:

Where the obligor waives its creditor’s right against a third party that is due or assigns its property without reward, thereby harming the obligee’s interests, the obligee may petition the People’s Court for cancellation of the obligor’s act. Where the obligor

⁷³⁶ *Property Law of China*, *supra* note 532, art. 34.

⁷³⁷ *Trust Law of China*, *supra* note 1, art. 22.

assigns its property at a low price which is manifestly unreasonable, thereby harming the obligee's interests, and the assignee is aware of the situation, the obligee may also petition the People's Court for cancellation of the obligor's act.⁷³⁸

It can be seen therefore the right of revocation is not necessarily based on real rights, but can also be exercised by a creditor exercising his personal claims when his interests are harmed by debtors.

This thesis argues that the beneficiary's right of revocation is in the nature of a creditor's revocation right but not a recovery of real rights. That is because, on one hand, in contrast to the recovery of real rights of which the purpose is to resume the control of property,⁷³⁹ the right of revocation in the trust aims mainly at preserving the trust property instead of controlling them. Even when the trust property is returned to the trust as a result of the beneficiary's right of revocation, it reverts back to the control of the trustee while the beneficiary still has no power over the trust property. On the other hand, unlike the right of recovery of real rights, the beneficiary's right to annul trustees' act is irrelevant to the trust property. This power to annul is instead the same as the characteristic of a creditor's right to annul. For example, when a trustee releases the debts in the trust property, the beneficiary's right to annul this disposal can only be by a creditor's right to annul for the reason that an application of the recovery of real rights requires the trustee to dispose of the trust property.⁷⁴⁰ By contrast, a creditor's right to annul can be used to preserve the trust property.⁷⁴¹ As a result, it is more reasonable to characterize the beneficiary's right to annul trustee's disposal as a creditor's right of revocation, rather than a right of recovery in real rights.

⁷³⁸ *Contract Law of China*, *supra* note 426, art. 74.

⁷³⁹ Liming Wang, *Property Law Research* (Beijing: China People's University Press, 2007) at 201.

⁷⁴⁰ *Ibid* at 204.

⁷⁴¹ Wang, *supra* note 718 at 190.

Based on the above analyses of the characteristics of beneficiary rights, we may define beneficiary rights in the Chinese system of trust law as a special personal claim consisting of three parts: the main claim (personal claims), appurtenance (right of supervision), and the debt security (right of revocation). These three parts achieve substantially the same conceptual function as the common law notion of equitable ownership.

In sum therefore, dual ownership would not be an obstacle preventing the notion of the trust from being incorporated into the Chinese legal system. Instead of insisting on the trust's conceptual nature, it is more important to find or design a legal device that plays the same role of dual ownership. Such a device in China could be the binary system of real rights and personal claims, which accommodates legal ownership as the trustee's unitary ownership of trust property, and interprets equitable title as the beneficiary's special personal claims. These, coupled with the amendment suggestions to the *Trust Law of China* proposed in Chapter III, are the recommendations this thesis makes to Chinese law in order to solve the uncertainties of the *Trust Law of China* and to make trust management more efficient.

CONCLUSION

In the common law, the law of trusts has derived from the jurisprudence of equity courts. Although dual ownership, trustee's legal ownership and beneficiary's equitable title, is considered as in the nature of common law trusts, it does not follow that the trust cannot exist without the duality of ownership, as it does in civilian jurisdictions, where ownership is absolute and indivisible. Dual ownership, it will be recalled, is simply a result of the differences of courts. The term refers solely to the real nature of the function of the trust, which is to grant trustees exclusive control, management and administration of trust property, and to entitle the beneficiaries the right to enjoy the benefits of the trust.

Precisely because of the trust's value in commerce, attempts have been made in various common law jurisdictions over the last century to simplify or to renovate the law of trusts, even as a number of civilian jurisdictions, pure or mixed, introduced the trust into their legal system. These efforts have had mixed success, and there is little literature from a comparative law perspective surrounding the issue of trusts. Part of the reason for this neglect during the 20th century was the common view among scholars that the common law and the civil law conceptions of trust, where they existed, were so different so as to render a study of trusts useless. In the 21st century, however, trusts will become the future of comparative law precisely because of the apparent impossibility of introducing trusts into civilian systems.⁷⁴² In this thesis, the comparative studies of the trust in common law and in civil law, in particular the ownership of trust property, demonstrate that it is possible, and necessary for China to introduce the real

⁷⁴² Smith, "Mistaking the Trust", *supra* note 73 at 804.

common law trust.

China introduced the trust and promulgated its first trust law in 2001 in the form of the *Trust Law of China*. However, the *Trust Law of China* avoids answering the key question of how to understand and introduce dual ownership, namely, who is entitled to the trust property, and how to explain the nature of the beneficiary's right, i.e. whether it is a real right or a personal claim. Moreover, the *Trust Law of China* adopts a narrow concept of trust, and its relevant provisions are painted too broadly to be of much use. As Professor Ho says: "China has entered the trust system from the deep end by introducing the trust as a legal device for sophisticated investment funds, and for 'capital trusts' in the financial arena. [Whereas], [i]n all common law jurisdictions and most traditional civil law jurisdictions, the trust is used initially in the context of intergenerational management of wealth."⁷⁴³ As both Ho and this thesis note therefore, there remains much room for amendment and reform in Chinese trust law.

Based on the principle that the incorporation of trust ownership should focus on institutional functions, rather than on concepts, this thesis believes that China should retain its unitary ownership and adopt the binary system of real rights and personal claims in the introduction of the trust. Doing so would define ownership in the Chinese system along the lines of the common law's conception of ownership as the trustee's unitary, but still *prima facie*, ownership and interpret the beneficiary's equitable title as a special personal claim against trustees. Likewise, it would also deem the trustee the owner of trust property in external relationships so as to allow for the convenient and efficient management and administration of

⁷⁴³ Ho, *Trust Law in China*, *supra* note 418 at 14.

trust property. In regards to the internal relationship of the trust, doing so would also commit trustees to maintain fiduciary duties to the beneficiaries in order to ensure that trustee's administration would be conducted for the best interests of the beneficiaries. The beneficiaries, in turn, would have the right to enjoy the trust property in the nature of a personal claim. Different from other legal devices, such as the notion of patrimony by appropriation in Quebec law, this proposal of the introduction of trusts best fits into the Chinese legal system and causes no damage to the function of the trust under common law.

It is hoped that this thesis will not only give rise to a heated discussion relating to the introduction of trusts in civilian jurisdictions, but also give rise to a reassessment of dual ownership of the trust in common law and to the manner in which it can best be renovated and understood in order to meet the needs of economic globalization, the development of international finance, and China's accession into the international market.

ANNEX

Trust Law of the People's Republic of China (Order of the President No.50)⁷⁴⁴

Order of the President of the People's Republic of China

No.50

The Trust Law of the People's Republic of China, adopted at the 21st Meeting of the Standing Committee of the Ninth National People's Congress of the People's Republic of China on April 28, 2001, is hereby promulgated and shall go into effect as of October 1, 2001.

Jiang Zemin

President of the People's Republic of China

April 28, 2001

Trust Law of the People's Republic of China

*(Adopted at the 21st Meeting of the Standing Committee of the Ninth National People's Congress
on April 28, 2001)*

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⁷⁴⁴ The author changes the spelling of settler to settlor in the governmental translation.

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Chapter I

General Provisions

Article 1 This Law is enacted in order to regulate trust relationship, to standardize trust acts, to protect the lawful rights and interests of the parties involved in a trust, and to promote the healthy development of trust undertakings.

Article 2 For purposes of this Law, trust refers to that the settlor, based on his faith in trustee, entrusts his property rights to the trustee and allows the trustee to, according to the will

of the settlor and in the name of the trustee, administer or dispose of such property in the interest of a beneficiary or for any intended purposes.

Article 3 This Law shall be applicable to the settlors, trustees, and beneficiaries (hereinafter collectively referred to as the “parties concerned”) that engage in civil, business or public welfare trust activities within the People’s Republic of China.

Article 4 With regard to trustees that engage in trust activities in the form of trust institutions, the State Council shall formulate specific measures for the organization and administration of such institutions.

Article 5 When carrying out trust activities, the parties concerned must obey laws and administrative regulations and observe the principles of voluntariness, fairness and good faith, and they may not impair the interests of the State and the public.

Chapter II

Creation of a Trust

Article 6 A trust shall be created for lawful trust purposes.

Article 7 To create a trust, there must be definite property under the trust, and such property must be the property lawfully owned by the settlor.

For purposes of this Law, the property includes the lawful property right.

Article 8 The creation of a trust shall take the form of writing.

The form of writing shall consist of trust contracts, testament, or other documents specified by laws and administrative regulations.

Where a trust is created in the form of trust contract, the trust shall be deemed created when the said contract is signed. Where a trust is created in any other form of writing, the trust is deemed created when the trustee accepts the trust.

Article 9 The following items shall be stated clearly in the written documents required for the creation of a trust:

- (1) purposes of the trust;
- (2) the names and addresses of the settlor and trustee;
- (3) the beneficiary or beneficiaries;
- (4) the scope, types and status of the assets under trust; and
- (5) the form and means through which the beneficiary gains benefits from the trust.

In addition to the items mentioned above, the period of the trust, the methods for the administration of the property under trust, remuneration payable to the trustee, manner for appointing another trustee, the cause for termination of the trust, etc. may be stated clearly.

Article 10 Where laws or administrative regulations stipulate that registration formalities shall be gone through for the creation of a trust, such formalities shall be gone through accordingly.

Anyone who fails to go through the registration formalities prescribed in the preceding paragraph shall go through the formalities as required; otherwise, the trust shall have no effect.

Article 11 Under any one of the following circumstances the trust shall be invalid:

(1) The purposes of the trust constitute a violation of laws or administrative regulations, or impair public interest.

(2) The property under trust cannot be fixed;

(3) The settlor creates the trust with unlawful property or with property which, according to this law, may not be used for creating a trust;

(4) The trust is created specially for the purpose of taking legal actions or for recovering debts;

(5) The beneficiary or beneficiaries cannot be determined; and

(6) Other circumstances stipulated in laws or administrative regulations.

Article 12 Where a settlor creates a trust to the detriment of the interest his creditors, the creditors shall have the right to apply to the People's Court for revoking the trust.

Where the People's Court revokes the trust according to the provisions of the preceding paragraph, the benefits already derived from the trust by the bona fide trustee shall not be affected.

The right of application prescribed in the first paragraph of this Article shall be terminated if it is not exercised within one year beginning from the date the creditor knows of or should know of the reasons for the revocation of the trust.

Article 13 For the creation of a testamentary trust, the provisions in the Law of Succession concerning testamentary succession shall be observed.

Where the person designated in a testament refuses or is unable to act as a trustee, the beneficiary shall appoint another person as the trustee; where the beneficiary is a person who has no civil capacity or limited capacity for civil conduct, his guardian shall appoint the trustee on his behalf. If there are other provisions in the testamentary instrument for governing the appointment of a trustee such provisions shall prevail.

Chapter III

Trust Property

Article 14 The property obtained by the trustee due to a trust accepted is trust property.

The property obtained by the trustee through administering, using or disposing of the trust property or by other means falls within trust assets.

No property the circulation of which is prohibited by laws and administrative regulations may be deemed trust property.

The property the circulation of which is restricted by laws and administrative

regulations may be deemed trust property upon approval given, in accordance with law, by the competent department concerned.

Article 15 The trust shall be differentiated from other property that is not put under trust by the settlor. Where, after a trust is created, the settlor dies or is dissolved or cancelled according to law, or is declared bankrupt, and the settlor is the sole beneficiary, the trust shall be terminated, and the trust property shall be his legacy liquidation property; where the settlor is not the sole beneficiary, the trust shall subsist, and the trust property shall not be his legacy or liquidation property; but if the settlor is one of the co-beneficiaries and dies or is dissolved, or cancelled according to law, or is declared bankrupt, his right to benefit from the trust shall be deemed his legacy or liquidation property.

Article 16 The trust property shall be segregated from the property owned by the trustee (hereinafter referred to as his “own property”, in short), and may not included in, or made part of his own property of the trustee.

Where the trustee dies or the trustee as a body corporate is dissolved, removed or is declared bankrupt according to the law, and the trusteeship is thus terminated, the trust property shall not be deemed his legacy or liquidation property.

Article 17 No compulsory measures may be taken against the trust property unless one the following circumstances arises:

(1) where, before the creation of the trust, the creditors enjoyed the priority right to be paid with the trust property and may exercise this right according to law;

(2) where the creditors demand repayment of the debts incurred by the trustee in the course of handling trust business;

(3) where taxes are levied on the trust property itself; and

(4) other circumstances prescribed by law.

Where compulsory measures are taken against the trust property in violation of the provisions in the preceding paragraph, the settlor, trustee and beneficiary shall have the right to raise their objections to the People's Court.

Article 18 The claims arising from the administration or disposition of trust assets by the trustee may not be used to offset the liabilities incurred by the trustee's own property.

The claims arising from the administration and disposition of the trust assets of different settlors may not be used to offset the liabilities incurred by the trustee likewise.

Chapter IV

The Parties Concerned in a Trust

Section 1

The Settlor

Article 19 The settlor shall be a natural person, a legal person, or an organization established in accordance with law, that has full capability for civil conduct.

Article 20 The settlor shall have the right to know the administration, use and disposition of, and the income and expenses relating to, his trust property, and the right to request the trustee to give explanations in this regard.

The settlor shall have the right to check, transcribe or duplicate the trust accounts related to his trust property and other documents drawn up in the course of dealing with trust business.

Article 21 If, due to special reasons unexpected at the time the trust is created, the methods for administering the trust property are not favorable to the realization of trust purposes or do not conform to the interests of the beneficiary, the settlor shall have the right to ask the trustee to modify such methods.

Article 22 Where the trustee disposes of the trust property in breach of the purposes of the trust, or causes losses to the trust property due to his departure from his administrative duties or improper handling of trust business, the settlor shall have the right to apply to the People's Court for annulling such disposition and the right to ask the trustee to restore the property to its former state or make compensation. Where a transferee of the said trust property accepts the property while knowing the violation of the purposes of the trust, he shall return the property or make compensation.

Where the settlor does not exercise the right of application prescribed in the preceding paragraph within one year beginning from the date he comes to know or should have known the reason for annulling the disposition, such right shall cease to exist.

Article 23 Where the trustee disposes of the trust property against the purposes of the

trust or commits gross negligence in administering, using or disposing of the trust property, the settlor shall have the right to dismiss the trustee according to the provisions in the trust documents or apply to the People's Court for dismissing him.

Section 2

The Trustee

Article 24 The trustee shall be a natural person or legal person who has full capability for civil conduct.

Where there are other provisions governing qualifications of a trustee laid down in laws or administrative regulations, those provisions shall prevail.

Article 25 The trustee shall abide by the provisions in the trust documents and handle trust business for the best interests of the beneficiary.

In administering the trust property, the trustee shall be careful in performing his duties and fulfill his obligations with honesty, good faith, prudence and efficiency.

Article 26 Except obtaining remuneration according to the provisions of this Law, the trustee may not seek interests for himself by using the trust property.

Where the trustee, in violation of the provisions of the preceding paragraph, seeks interests for himself by using the trust property, the interests gained therefrom shall be integrated into the trust property.

Article 27 The trustee may not convert the trust property into his own property. Where the trustee converts the trust property into his own property, he shall restore the trust property into its former state; where losses are caused to the trust property, he shall bear the responsibility to pay compensation.

Article 28 The trustee may not conduct inter transaction between his own property and trust assets or between the trust assets of different settlors, unless it is otherwise stipulated in the trust documents or is consented by the settlors or beneficiary and the inter transaction is conducted at fair market price.

Where the trustee, in violation of the provisions in the preceding paragraph, causes losses to the trust property, he shall bear the responsibility to pay compensation.

Article 29 The trustee shall administer the trust property separately from his own property and keep separate accounting books, and he shall do the same with regard to the trust property of different settlors.

Article 30 The trustee shall handle trust business himself, but may entrust another person to handle such affairs on his behalf where the trust documents provide otherwise or he has to do so for reasons beyond his control.

Where the trustee, in accordance with law, entrusts another person to handle trust business on his behalf, he shall bear the responsibility for the acts committed by that person in handling such affairs.

Article 31 Where there are two or more trustees in the same trust, they are co-trustees.

The co-trustees shall handle trust business jointly, but where the trust documents stipulate that the trustees may separately handle certain specified affairs, such stipulations shall prevail.

If the co-trustees disagree with each other when handling trust business jointly, the matter shall be dealt with in accordance with the provisions in the trust documents; where there are no provisions in this regard in the documents, the settlor, beneficiary or the party interested shall make a decision.

Article 32 The co-trustees who incur debts to a third party in the course of handling trust business shall bear joint and several responsibilities for clearing the debts. The intention expressed by the third party to any one of the co-trustees shall be equally effective to the other co-trustees.

Where one of the co-trustees disposes of the trust property against the purposes of the trust or causes losses to the trust property due to his departure from his administrative duties or his improper handling of trust business, the other co-trustees shall bear joint and several responsibility for compensation.

Article 33 The trustee shall keep complete records of the trust business handled.

The trustee shall, at regular intervals every year, report to the settlor and beneficiary on the administration and disposition of the trust property and the income and expenses relating to

the property.

The trustee shall, in accordance with law, have the obligation to keep confidential minutes relating to the settlor, the beneficiary and trust business handled.

Article 34 The trustee shall have the obligation to pay the beneficiary benefits from the trust with the limits of the trust property.

Article 35 The trustee shall have the right to obtain remuneration as agreed in the trust documents. Where there is no such agreement in the documents, a supplementary agreement may be made with the consent given by the parties concerned after consultation; in the absence of a prior or supplementary agreement, no remuneration may be asked for.

The agreed remuneration may, with the consent given by the parties concerned after consultation, be increased or decreased.

Article 36 Where the trustee disposes of the trust property against the purposes of the trust or causes losses to the trust property due to his departure from his administrative duties or his improper handling of trust business, he may not ask to be paid before he restores the property to its former state or makes compensation.

Article 37 The charges paid and the debts owed to a third party by the trustee in the course of handling trust business shall be borne by the trust property. Where the trustee effects such payment in advance with his own property, he shall have the priority right to be paid with the trust property.

The debts owed to a third party or the losses suffered by himself as a result of his departure from his administrative duties or his improper handling of trust business shall be borne by him with his own property.

Article 38 After the creation of a trust, with the consent of the settlor and beneficiary, the trustee may resign. Where there are other provisions in this Law governing the resignation of the trustee of a public welfare trust, those provisions shall prevail.

Where the trustee resigns, he shall, before another trustee is appointed, continue to perform the duties of administering the trust business.

Article 39 Under one of the following circumstances, the trustee's appointment shall be terminated:

- (1) he dies or is declared dead according to law;
- (2) he is declared to be a person with no or restricted capability for civil conduct;
- (3) his trusteeship is removed or he is declared bankrupt;
- (4) his trusteeship is dissolved in accordance with law or he forfeits his legal qualifications;
- (5) he resigns or is dismissed; or
- (6) other circumstances stipulated in laws or administrative regulations.

When the trustee's appointment is terminated, his successor, or the supervisor of heritage, guardian or liquidator shall keep the trust property, and help the new trustee to take over the trust business.

Article 40 Where the trustee's appointment is terminated, a new trustee shall be appointed according to the provisions in the trust documents; where there are no such provisions in the documents, the settlor shall make the appointment; where the settlor does not make the appointment or is incapable of doing so, the beneficiary shall designate one; where the beneficiary is a person with no or restricted capacity for civil conduct, his guardian shall, in accordance with law, make the appointment on his behalf.

The new trustee shall take up the rights and obligations of the former trustee in the handling of trust business.

Article 41 Where the trustee is found to be under one of the circumstances listed in subparagraphs 3 to 6 of the first paragraph Article 39 of this law and his appointment is thus terminated, he shall produce a report on the trust business handled and go through the formalities for the handing over of the trust property and affairs to the new trustee.

Upon acceptance of the report, mentioned in the preceding paragraph, by the settlor or beneficiary, the original trustee shall be exempted from the liability for issues listed in the report, except for the illegitimate acts committed by him.

Article 42 Where the appointment of one of the co-trustees is terminated, the trust property shall be administered and disposed of by the rest of the trustees.

Section 3

The Beneficiary

Article 43 The beneficiary is the person that enjoys the right to benefit from a trust. He may be a natural person, legal person or an organization established according to law.

The settlor may be a beneficiary and may also be the only beneficiary under the same trust.

The trustee may be a beneficiary but may not be the only beneficiary under the same trust.

Article 44 The beneficiary shall enjoy the right to benefit from a trust beginning from the date the trust becomes effective, unless otherwise stipulated in the trust documents.

Article 45 The co-beneficiaries shall enjoy the benefits from a trust according to the provisions in the trust documents. Where no percentage or methods for distribution of the benefits from the trust are specified in the documents, all the beneficiaries shall enjoy the benefits equally.

Article 46 The beneficiary may give up the right to benefit from a trust.

Where all the beneficiaries give up the right to benefit from a trust, the trust shall be terminated.

Where some of the beneficiaries give up the right to benefit from a trust, the right given

up shall go to the person in following order of precedence:

- (1) the persons specified in the trust documents;
- (2) the other beneficiaries; and
- (3) the settlor or his successor.

Article 47 Where the beneficiary cannot repay the matured debts, his right to benefit from a trust may be used to repay the debts, except this is restricted by provisions in laws, administrative regulations and trust documents.

Article 48 The beneficiary may, in accordance with law, transfer his right to benefit from a trust or have the right succeeded to, except this is restricted by provisions in the trust documents.

Article 49 The beneficiary may exercise the rights that the settlor enjoys as stipulated in Article 20 through 23 of this Law. If the beneficiary, while exercising the said rights, holds views differing from those of the settlor, he may apply to the People's Court for decision.

Where the trustee commits the act listed in the first paragraph of Article 22 of this Law and one of the co-beneficiaries applies to the People's Court for annulling the disposition of the trust property, the decision made by the People's Court to such an effect shall be effective to all the co-beneficiaries.

Chapter V

Modification in and Termination of a Trust

Article 50 Where the settlor is the only beneficiary, he or his successor may revoke the trust. Where it is otherwise provided for in the trust documents, the provisions there shall prevail.

Article 51 After a trust is created, the settlor may replace the beneficiary or dispose of his right to benefit from the trust under one of the following circumstances:

- (1) the beneficiary commits a major tort against the settlor;
- (2) the beneficiary commits a major tort against the other co-beneficiaries;
- (3) the change or disposition wins the consent of the beneficiary; and
- (4) other circumstances stipulated in the trust documents.

Under one of the circumstances listed in subparagraphs (1), (3) and (4) in the preceding paragraph, the settlor may revoke the trust.

Article 52 A trust will not be terminated due to the facts that the settlor or trustee dies, loses his capacity for civil conduct, the trusteeship is dissolved or canceled according to law or he is declared bankrupt, neither will it be terminated due to the fact that the trustee resigns, except it is otherwise stipulated in this Law or the trust documents.

Article 53 Under one the following circumstances, a trust shall be terminated:

- (1) the cause for its termination specified in the trust documents arises;

- (2) the continuance of the trust goes against the purposes of the trust;
- (3) the purposes of the trust have been realized or cannot be realized;
- (4) the parties concerned, through consultation to terminate it;
- (5) the trust is cancelled;
- (6) the trust is revoked.

Article 54 Where a trust is terminated, the trust property shall be owned by the person specified in the trust documents; where there are no such specifications in the documents, the following order of precedence shall be applied for determining the ownership:

- (1) the beneficiary or his successor; and
- (2) the settlor or his successor.

Article 55 After the ownership of the trust property is determined according to the provisions in the preceding Article, the trust shall be deemed subsisting while the trust assets are being transferred to the owner, and the owner shall be deemed the beneficiary.

Article 56 Where a trust is determined, the People's Court takes compulsory measures with regard to the original trust property according to the provisions of Article 17 of this Law, the owner shall be deemed the person against whom the measures are taken.

Article 57 When, after a trust is terminated, the trustee, in accordance with the

provisions of this Law, exercises the right to request for remuneration or to obtain compensation from the trust property, he may have a lien on the property or raise the request to the owner of the property.

Article 58 Where a trust is terminated, the trustee shall make a liquidation report on the trust business handled. Where the beneficiary or the owner of the property has objections to the report, the trustee shall be exempted from the liability for issues listed in the report, except for the illegitimate acts committed by him.

Chapter VI

The Charitable Trust

Article 59 The provisions in this Chapter are applicable to public welfare trusts where there are no provisions in this Chapter with regard to some matters, the provisions in this Law or other related laws shall be apply.

Article 60 A trust created for one of the following purposes in the interest of public welfare is a public welfare trust:

- (1) relief for the poor;
- (2) relief assistance to people suffering from disasters;
- (3) helping the disabled;
- (4) developing education, science, technology, culture, art and sports;

(5) developing medical and public health undertakings;

(6) developing undertakings for the protection of the environment and maintaining ecological environment; and

(7) developing other public welfare undertakings.

Article 61 The State encourages the development of public welfare trusts.

Article 62 A public welfare trust shall be created and its trustee shall be appointed with approval by relevant public welfare undertaking administration authority (hereinafter refer to as the “public welfare administration authority, in short”).

Without approval by the public welfare administration authority, no one may carry out activities in the name of a public welfare trust.

The public welfare administration authority shall support activities conducted by welfare trusts.

Article 63 No property under a public welfare trust or the income from it may be used for non-public welfare purposes.

Article 64 Trust supervisors shall be appointed for public welfare trusts.

Trust supervisors shall be specified in the trust documents. Where there are no such specifications, they shall be designated by the public welfare administration authority.

Article 65 The trust supervisor shall have the right, in his own name, to file a lawsuit or the other legal acts in the interests of the beneficiary.

Article 66 No trustee of a public welfare trust may resign without the approval of the public welfare administration authority.

Article 67 The public welfare administration authority shall inspect the trustee as to how he handles the public welfare affairs and disposes of the property.

The trustee shall, at least once a year, makes a report on the trust business handled and the status of assets disposed of, and upon acceptance by the trust supervisor, the report shall be submitted to the public welfare administration authority for examination and approval, and the trustee shall announce the report.

Article 68 Where the trustee for a public welfare trust goes against his obligations under the trust, or is unable to perform his duties, the public welfare administration authority shall replace the trustee.

Article 69 If, after a public welfare trust is created, an event unforeseeable at the time of the creation of the trust occurs, the public welfare administration authority may, on the basis of the purposes of the trust, revise the related articles in the trust document.

Article 70 Where a public welfare trust is terminated, the trustee shall, within 15 days from the date the cause for the termination arises, report to the public welfare administration authority the cause for its termination and the date the trust is terminated.

Article 71 Where a public welfare trust is terminated, the trustee shall make a liquidation report on the trust business handled and, upon acceptance by the trust supervisor, submitted it to the public welfare administration authority for examination and approval, and the report shall be announced by the trustee.

Article 72 Where, upon termination of a public welfare trust, there is no owner of the trust property, or such owner is not a specified member of the general public, the trustee shall, upon approval by the public welfare administration authority, use the trust property for purposes similar to the original ones, or transfer it to public welfare organizations or other public welfare trusts having similar purposes.

Article 73 Where the public welfare administration authority violates the provisions of this Law, the settlor, trustee and beneficiary shall have the right to file a lawsuit at the People's Court.

Chapter VII

Supplementary Provisions

Article 74 This Law shall go into effect as of October 1, 2001.

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