

## A REVIEW OF THE TRUST REGIME IN HONG KONG SAR

### COMMENTS OF HONG KONG BAR ASSOCIATION

1. The Hong Kong Bar Association has been provided with a paper dated 11.2.2022 by the Law Society of Hong Kong (“LSHK”) with a review on Hong Kong’s trust regime. The paper reviews various aspects of the trust law and makes various recommendations and proposals for reform so as to enhance the marketability of HK trusts and HK trustees over competing jurisdictions.
2. At this initial stage, the Bar does not express any firm view on the policy direction proposed by LSHK. Nevertheless, if the Administration is to consider reforming the law on trusts in Hong Kong, we believe that, in addition to the issues identified in the paper, one may also consider (1) the enforcement of exclusive jurisdiction clauses in trust deeds and (2) the suitability of firewall provisions in the divorce context.

#### Exclusive Jurisdiction Clauses in Trust Deeds

3. It is often the case, especially in trusts set up for private wealth management purposes, that the trust deed would include an exclusive jurisdiction clause (as well as a governing law clause) in favour of the chosen jurisdiction. This is an important aspect to ensure that disputes relating to the trust would be resolved in the chosen jurisdiction in accordance with the chosen law.
4. As the Bar understands it, the common law on such exclusive jurisdiction clauses involves a fair degree of uncertainty in when they will be followed.
5. In the context of a contract between the parties to the action, strong cause must be shown for the clause not to be enforced: **Donohue v Armco Inc** [2002] 1 All ER 749, §24 (Lord Bingham). This is based on the idea that the Court would usually enforce a contract clause freely entered into between the parties. Where the exclusive jurisdiction clause relied upon is in a trust deed, different

considerations apply. As explained by Lord Neuberger in **Crociani v Crociani** (2014) 17 ITELR 624 (a Privy Council decision on appeal from Jersey):-

- 5.1 It should be less difficult for a beneficiary to resist the enforcement of an exclusive jurisdiction clause in a trust deed than for a contracting party to resist the enforcement of such a clause in a contract. The weight to be given to such a clause in a trust deed is **less** than that in a contract: §35.
- 5.2 This is because, in a contractual context, a party to the contract has a contractual right to enforce the jurisdiction clause, and his right should only be displaced by strong reasons why an injunction enforcing the clause should not be granted: §34. But in the case of a clause in a trust, the court is not faced with the argument that it should hold a contracting party to her contractual bargain. While a beneficiary who wishes to take advantage of a trust can be expected to accept that he/she is bound by the terms of the trust, this is not a commitment of the same order as a contracting party being bound by the terms of a commercial contract: §36.
- 5.3 Where it is a beneficiary who wishes to avoid the clause and the trustees who wish to enforce it, “one would normally expect the trustees to come up with a good reason for adhering to the clause, albeit that their failure to do so would not prevent them from invoking the presumption that the clause should be enforced”: §36.
- 5.4 Further, in the case of a trust, unlike a contract, the court has an inherent jurisdiction to supervise the administration of the trust, and this is a significant distinction between contracts and trusts: §36.
- 5.5 He concludes at §37 as follows:

*“... while it is right to confirm that a trustee is prima facie entitled to insist on and enforce an exclusive jurisdiction clause in a trust deed, the weight to be given to the existence of the clause is less (or the*

*strength of the arguments needed to outweigh the effect of the clause is less) than where one contracting party is seeking to enforce a contractual exclusive jurisdiction clause against another contracting party..."*

6. In relation to the point made in §5.3 above, it is observed in **Lewin on Trust Vol. 1 (20<sup>th</sup> ed., 2019)** at §11-070 that:

*"... Presumably the good reason will usually have to be the suitability of the forum identified in the clause. Since, even in the absence of a jurisdiction clause, the greater suitability of England as a forum is a ground for the court to entertain the claim and, conversely the greater suitability of a foreign forum is a ground for it to decline to do so, it is not altogether clear whether the presence of the clause will now be of much practical effect."*

7. It appears that the factors that would be taken into account by the Court are in effect the *forum non conveniens* considerations: see **Lewin Vol.1**, §11-071; **Crociani**, §§40-47. These would require an analysis of connecting factors, such as factors affecting convenience and expense (e.g. availability of witnesses), the law governing the relevant transactions, and the places where the parties respectively reside or carry on business: **The Spiliada** [1987] 1 AC 460, 478A-B (Lord Goff). Indeed, it is not uncommon that the Courts would refuse to enforce an exclusive jurisdiction clause in a trust instrument: see **Crociani**, §§40-47; **EMM Capricorn Trustees Ltd v Compass Trustees Ltd** (2001) 4 ITELR 34, §§30-31.
8. The effect of these authorities would appear to be this: even if the trust deed of a Hong Kong trust contains an exclusive jurisdiction clause in favour of the Hong Kong courts in respect of disputes arising from the trust, this would at most produce a weak presumption in favour of the matter being heard in Hong Kong. The defendant could escape the effect of the exclusive jurisdiction clause simply by showing that a different forum is, all things considered, more suitable.

9. From the perspective of a settlor / trustee who drafted the exclusive jurisdiction clause expecting it to be given effect, this is plainly undesirable, as there is no certainty at all that the nominated forum would hear the case as they have wished.
10. The Bar believes that, in the context of LSHK's proposal, this is an aspect that statutory intervention may be considered. The statute may provide for strict enforcement of an exclusive jurisdiction clause in a Hong Kong trust, or presumptive enforcement which would be rebutted when strong cause is shown (like in the contractual context). Such a measure may enhance the certainty as to the forum for dispute resolution for HK trusts.

#### Suitability of Firewall Provisions in the Divorce Context

11. In LSHK's proposal at §§28-29, it is proposed that firewall provisions be introduced to protect trust assets from claims arising from the claimant's personal relationship with the settlor or beneficiaries. In a number of other jurisdictions, there are extensive firewall provisions, which are widely considered to be primarily targeted at, foreign judgements and orders made in the divorce context.
12. In many jurisdictions, as is the case in Hong Kong, the family court has wide powers to redistribute the family wealth amongst the divorcing spouses. In Hong Kong, the matrimonial court has the power to set aside dispositions made by a party with the intention of defeating a claim for financial provision: s.17(1)(b) of the Matrimonial Proceedings and Property Ordinance (Cap 192) ("**MPPO**"). This "anti-avoidance" power may be invoked to nullify a disposition into trust: **Lewin Vol. 2**, §51-026.
13. The court also has the power to order a variation of any "nuptial settlement" for the benefit of the parties and / or their children: MPPO s.6(1)(c). The following principles guide the exercise of this power:
  - 13.1 The meaning of "nuptial settlement" is extremely wide. It has no formal limitation, and covers any arrangement or disposition which makes some

form of continuing provision for both or either of the parties to the marriage in that capacity, with or without provision for their children: **Brooks v Brooks** [1996] AC 375, 391G-H (Lord Nicholls); **N v N and F Trust** [2005] EWHC 2908, §33 (Coleridge J).

- 13.2 A trust could be a nuptial settlement. Thus, in the event of a divorce, trust assets could be the subject of a variation order. As explained by Mostyn J in **BJ v MJ** [2011] EWHC 2708 at §7:

*“For bona fide trusts, a key distinction is between nuptial and non-nuptial settlements. If the trust is a nuptial settlement then notwithstanding that the assets are legally held by third parties as trustees, and that yet further third parties may be beneficiaries along with the husband, the trust assets fall within the court’s dispositive powers under s24(1)(c) Matrimonial Causes Act 1973 [the equivalent of MPPO s.6(1)(c)] ... The variation powers extend to making outright provision to the applicant, and may even be exercised where the trust is offshore, although, following well-established principle, the court will be unlikely to make a variation order where both the trust and its assets are overseas unless it is satisfied that the order would be implemented by the court exercising effective control over the trust ...”*

- 13.3 Once a trust is found to be a nuptial settlement, there is no limit on the extent of the power to vary or on the form any variation can take. Thus, it is within the court’s power to vary by wholly excluding a beneficiary from the trust, or transferring some asset to a non-beneficiary free from all trusts: **Ben Hashem v Al Shayif & Ors** [2008] EWHC 2380, §290 (Munby J). The Court has in the past exercised this power by pulling out trust assets and placing them into a separate fund for the benefit of a spouse: see **E v E (Finacial Provision)** [1990] 2 FLR 233.

- 13.4 The power to vary serves an important function. Financial provision that is appropriate so long as the parties are married will often cease to be appropriate when the marriage ends. Thus, unless variations are made to its terms, the interest of the parties and/or their children may be underserved. The power to alter the terms of a nuptial settlement is available in order to promote their best interests: **Brooks**, 392B-C (Lord Nicholls).
14. There are no doubt similar powers for courts in some other jurisdictions. Plainly, the purpose of these powers is to protect the other spouse, whose claims for financial provision may otherwise be frustrated or significantly reduced. It is self-evident that such powers given to the family courts seek to protect and promote the interest of the divorcees and / or their children as serving an important policy objective – so much so that it takes precedence over the need to preserve the integrity of a private trust. The interests at stake in the law of divorce are obviously many and varied.
15. The introduction of blanket firewall provisions into the Trustee Ordinance (Cap 29) may nevertheless mean that, insofar as a Hong Kong trust is the subject, foreign orders seeking to achieve the same policy objective (eg foreign anti-avoidance / variation orders) could be met with automatic non-recognition and unenforceability: **Lewin Vol. 1**, §§12-195 to 12-196. This has to be carefully considered in conjunction with the multifarious policy objectives of our divorce law.
16. It is not apparent that there would necessarily be good policy reasons to distinguish between foreign divorces (as to which the firewall provisions would apply) and Hong Kong divorces (as to which the firewall provisions would not apply). The Bar believes that careful consideration must be given to whether the protection or promotion of HK trusts can be a justification for treating Hong Kong divorces and foreign divorces differently. This is particularly so given that very often parties involved in Hong Kong divorces have connections with multiple jurisdictions such that they can and do resort to the divorce jurisdictions in Hong Kong and elsewhere, concurrently or sequentially.

17. Finally, in this context, any legislative intervention should also consider how the courts would actually approach such firewall provisions. An example of a summary of a possible approach can be found in **Re IMK Family Trust** 2008 JLR 250 at §§71-76:

17.1 The firewall provisions would mean that the local court would not directly enforce a foreign judgment affecting the local trust.

17.2 But the foreign judgment is a circumstance to be taken into account by the trustee exercising its discretion under the trust, and in turn the court if the court is asked to approve the trustee's decision. Thus, it is open to the trustee (and the court) to take into account the foreign judgment and to give effect to it in exercising their discretion. This would not be contrary to the firewall provisions.

17.3 But this is not possible where the foreign judgment has the effect of varying the very terms of the trust. This is because the trustee must act in accordance with the terms of the trust when exercising its discretion.

17.4 The above position means that the effect of firewall provisions may, depend on their drafting, be limited. These nuances should also be considered if one is to consider legislative intervention in this area.

Hong Kong Bar Association

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