

# An Overview of PRC Trust Law and Trust Business

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China became the fifth Asian jurisdiction to adopt Trust Law in 2001, just after India (1882), Japan (1922), South Korea (1961), and Chinese Taiwan (1996). It is a good time to review the law, regulations and rules supporting the law, as well as the development of trust business in China, after more than ten years. The paper begins by providing the background information on the Trust Law, i.e., why it was enacted in 2001? Secondly, I shall brief main contents of Chinese trust law, with reference to relevant administrative regulations and rules whenever necessary. The third part of the paper focuses on the trust business in China, with examples of trust products in China. In part four, various theoretical debates on trust law in China will be presented and summarized. The paper ends with some proposals on the future of PRC trust law and trust business.

No revisions or judicial interpretations to or on trust law have even been made since the adoption of the 2001 Trust Law. That doesn't mean, however, that the 2001 Trust Law all stands by itself. There are

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several other laws, administrative regulations, as well as administrative rules adopted by the CBRC (China Banking Regulatory Committee) or other competent authorities to supplement the Trust Law, including but not limited to *Securities Investment Fund Law of the People's Republic of China* (adopted in 2003, as amended in 2012, and 2015 respectively); *Regulations on Financial Asset Management Companies* (State Council Order No. 297 [2000]); *Measures for the Administration of Trust Companies* (issued by CBRC No.2[2007], to replace the 2002 PBOC *Administrative Provisions on Financial Trust and Investment Institutions*), *Measures for the Administration of Trust Companies' Trust Plans of Assembled Funds* (CSRC Order No.3 [2007]), and *Measures for the Administration of Net Capital of Trust Companies* (CBRC Order No.5 [2010]); *Temporary Administrative Measures on the Investment Matters of National Social Security Fund* 《全国社会保障基金投资管理暂行办法》(Ministry of Finance, Ministry of Labor and Social Security Order No. 12 [2001]), *Interim Measures for the Administration of Commercial Banks' Personal Financial Management Services* (CBRC Order No. 2 [2005]), *Administrative Measures for the Securitization of Credit Assets* (CBRC No. 7 [2005]), *Administrative Measures on Securitization Business of Securities Companies and Fund Management Companies* 《证券公司及基金管理公司子公司资产证券化业务管理规定》(CSRC Announcement No. 49[2014]). The cores among them are the Trust Law, *Measures for the Administration of Trust Companies*, *Measures for the Administration of Trust Companies' Trust Plans of Assembled Funds*, and *Measures for the Administration of Net Capital of Trust Companies* (as colloquially called the “one law + three measures”).

## 1. Why Trust Law was Enacted in 2001

The trust business in China could be traced back to more than 100 years ago. The business diminished after 1949 in Mainland China until the first PRC trust company, CITIC<sup>1</sup>, was established in October 1979. In 1986, the PBOC issued *Temporary Administrative Provisions on Financial Trust and Investment Institutions* (《金融信托投资机构管理暂行规

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1 CITIC : 中国中信集团公司, 前称“中国国际信托投资公司”, 简称“中信公司”。

定》)。The business had its hey days until mid-1999s. By the end of 1995, there were 392 trust and investment companies nationwide. The assets of those companies totaled more than RMB 600 billion, accounting for approximately 10% of total financial assets of the country. In late 1990s, PRC trust business came across its first crisis. GITIC went bankruptcy in 1998. Meanwhile, Hainan ITIC (HITIC) defaulted on USD 370 million worth of Samurai bonds owed to Sumitomo Bank and other Japanese creditors, causing considerable tension among foreign investors. In 2000, the then regulator of the trust industry, the PBOC<sup>2</sup> ordered all trust companies to reapply for permission of business and to suspend their operation before they were granted new business license.

The Trust Law of China could only be understood against this background. The NPC Financial and Economic Commission started the drafting work in 1993, as part of the effort to clarify and secure the legality of the industry, so as to guarantee the sustainable development of the industry. In 1996, the draft law was submitted to the Standing Committee of the National People's Congress for first deliberation. The trust law, however, was not adopted until 2000 after three deliberations, when the PBOC accomplished the consolidation of the industry.

## **2. Main Contents of Chinese Trust Law 2001**

### **2.1 Creation of a Trust**

Trusts in China can be created either by contract or by will or other written documents. Establishing a trust by declaration of a settlor (or trustor) to become the trustee (self-trust) is not recognized by Chinese Trust Law.

#### **2.1.1 Creation by Contract**

A trust can be created by a contract between the settlor and the trustee, and this is the most common way of creating a trust in China.

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<sup>2</sup> In 2003, CBRC became of the new regulator of trust company.

According to the Trust Law, the contract has to be in writing and shall contain the following contents (art. 9): (1) purpose of the trust; (2) name and address of the settlor, trustee and beneficiary; (3) scope, type and status of the trust property; and (4) ways and methods by which the beneficiary receive the trust benefits.

The trust is created at the time when the contract is concluded between the settlor and trustee.

A trust property is necessary for creating a trust. The PRC trust law requires the certainty and legality of the trust property (art. 7), but it does not have to be transferred to the trustee at the time of the creation of the trust. Some properties such as real properties and special movable properties (e.g. motor vehicles and ships) are required to be registered according to laws, and trust would not come into effect until such registration is accomplished.

The contract is legally binding on both parties. As for the settlor, if the property is not transferred to the trustee at the time of the contract, he/she has a duty to transfer the trust property as agreed between the parties. The trustee owes a range of duties such as duty of loyalty even before he/she takes possession of the trust property. In short, trust creation is not a disposal of a property, it is an arrangements between the parties.

### **2.1.2 Creation of Trust by Will**

A trust created by will or other legal documents become effective upon the acknowledgment of the trust by the trustee (art. 8). In a trust created by will, if the person appointed by the testament refuses or does not have the capacity to act as trustee, the beneficiary may appoint other trustees. In the event that the beneficiary is a person without civil capacity or a person with limited capacity, his guardian shall appoint the trustee on his/her behalf according to law. Moreover, a testamentary trust shall also comply with the provisions of the PRC Succession Law.<sup>3</sup>

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<sup>3</sup> For more detailed discussion on potential conflicts between the two laws, see, e.g., Frances H. Foster, "The Dark Side of Trusts: Challenges to Chinese Inheritance Law", 2 WAUGSLR 151.

### **2.1.3 Creation of Trust by Other Written Documents**

Article 8 of PRC Trust Law allows the creation of trust by other written documents as provided by laws and regulations. In practice, however, other written documents are rarely used to create a trust.

## **2.2 Fundamental Structure of a Trust**

### **2.2.1 Independence of Trust Property**

A trust property does not have a status of legal entity, but it is independent and separated from the properties owned by the trustee and settlor. The management and operation of the trust property should comply with the terms of the trust agreement. The proceeds obtained by the trustee through administering, using or disposing of the trust property or by other means falls within trust assets (Art. 14 (2)), and the expenses incurred in managing trust property shall be borne by the trust property.

#### **2.2.1.1 Trust Property Legally Separated from the Properties Owned by the Trustee**

Trust property is treated as a property separated from the properties owned by the trustee. Thus the creditors of the trustee cannot claim against the trust property, nor shall such trust property be touched upon trustee's bankruptcy.

The segregation between the trust property and the trustee's property are publicized either by registration (for properties which shall be registered, art 10) or by separate management or separate accounting between the trust property and trustee's inherent property (art. 29).

#### **2.2.1.2 Trust Property Legally Separated from the Properties Owned by the Settlor**

A trust property is separated from settlor's other properties. In cases where the settlor is the only beneficiary, however, once the settlor dies, or is dissolved by liquidation, or is declared bankrupt, the trust will terminate and the trust property will be a part of bankruptcy estate.

The segregation between the trust property and settlor's other properties is publicized by registration for properties that shall be registered or title-transfer of the trust property from the settler to the trustee, or a custody of the trust property with a third party.

### **2.2.2 Beneficial Rights and its Nature**

A beneficiary under PRC trust law is a person who enjoys the beneficial rights of the trust. The beneficial rights are transferrable and inheritable, unless provided otherwise in the trust documents.

PRC trust law doesn't give a clear definition to the nature of the beneficial rights. Under the law, the beneficiary does not only have the right to accept the beneficial interest, but also has some other rights equivalent to that of the settlor's, including but not limited to, (1) right to be informed of the administration, use and disposition of, and the income and expenses relating to, the trust property; (2) the right to supervise the trustee on the management of the trust property (art. 20); (3) the right to ask the trustee to adjust the methods of management of the trust property if the methods prevents the achieving of the purposes of the trust or are not in compliance with the interests of the beneficiary due to special causes that are not foreseen when the trust was established (art. 21); (4) the right to apply to the people's court for withdrawing the improper disposition carried out by the trustee and the right to ask the trustee to revert the trust property or make compensation (art. 22); (5) the right to remove the trustee according to the provisions of the trust documents or apply to the people's court to remove the trustee, if the trustee disposes the trust property against the purposes of the trust or is at serious fault when managing, utilizing or disposing of the trust property (art. 23).

## **2.3 Administration of Trust**

### **2.3.1 Trustee's Power**

Under PRC trust law, the trustee has three general powers as follows: (1) managing the trust property and dealing with trust affairs; (2) entrusting a third party to handle the trust affairs; and (3) making an

objection to the people's court about enforcement of the trust property. The exact power of the trustee, however, shall be defined in accordance with the provisions of the trust documents and trust laws.

### **2.3.1.1 Trustee's Power to Handle the Trust Affairs and Manage the Trust Property**

When trustee handles the trust affairs, he/she shall fulfill the purpose of the trust on the beneficiary's behalf. There are also specific rules governing trusts where trustees are trust companies, for example, trust companies are prohibited from selling the trust properties for repurchase. The law-maker believes that selling trust properties for repurchase is mainly a way of financing rather than managing trust properties.

### **2.3.1.2 Trustee's Power to Raise an Objection to the People's Court Regarding Compulsory Measures Taken Against the Trust Property**

Article 17 of the Trust Law sets out circumstances where compulsory measures may be taken against the trust property, including: (1) where the creditors enjoyed the priority right to be paid out of the trust property before the creation of the trust 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 tax authorities claim taxes liabilities on the trust property; and (4) other circumstances prescribed by law.

In the event that compulsory enforcement measures are taken against the trust property in violation of provisions in the preceding paragraph, the settler, trustee and beneficiary shall have the power to object to the order of the People's Court.

### **2.3.1.3 Delegation of Trustee's Power to a Third Party**

A trustee shall handle the trust affairs himself. The trustee, however, may entrust a third party to handle such affairs on his behalf if the

trust documents provide so or such trustee has to do so under circumstances beyond his control (art. 30).

The Trust Law provides that 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 person in handling such affairs. In other words, the third party assumes no direct responsibility to the beneficiary. The rule applies to both natural person and trust company trustees.

### **2.3.2 Trustee's Duties**

Trustee shall comply with the provisions of the trust documents and handle the trust affairs for the best interests of the beneficiary, and he/she owes duty of loyalty and duty of care.

#### **2.3.2.1 Duty of Loyalty and Conflict of Interest**

The duty of loyalty is mainly concerned with (1) preventing conflict of interests and (2) preventing trustee from obtaining interest for himself/herself.

According to art. 26 of Trust Law, the trustee shall not use the trust property for the purpose of seeking his personal interest. Also, art. 27 prohibits the trustee from mixing the trust property with his/her own property. Art. 28 prohibits the trustee from conducting inter-transaction between his own property and trust assets (self-dealing) or between the trust assets of different settlors, unless: (1) it is otherwise stipulated in the trust documents; or (2) it is permitted by the settlors or beneficiary and such inter transaction is conducted at fair market value. If the trustee violates arts.27 or 28, he/she shall bear the liability to compensate damage caused by such violation.

If the trustee is a trust company, the provisions under Measures for the Administration of Trust Companies shall apply. Art 25 of the Measures states that trust companies shall make their best efforts to avoid conflict of interests. In cases where it is impossible to avoid conflict of



interests, the trust company shall either disclose such information to the settlor and the beneficiary or refuse to carry out such business. If the trust company engages in affiliated transactions, it has to report each transaction to CSRC in advance and disclose the relevant information in accordance with the relevant provisions and conducts the transaction at fair market value. Also, art. 34 of the Measures prohibits trust companies, among others, from (a) seeking unjust interests by taking advantage of his/her role as a trustee; (b) misappropriating trust property for any non-trust purpose; (c) promising that the trust property would suffer no loss or guaranteeing a minimum return; and (d) providing guarantee secured by trust property.

### **2.3.2.2 Duty of Care**

The trustee owes a duty of care in accordance with art.25 of the Trust Law. If the trustee's violation of duty of care (e.g. handling trust affairs improperly) causes damages to the trust property, the trustee may not request for payment of remuneration before restoring the trust property to its original status or having made compensations (art. 36).

The duty of care is different from the duty of loyalty as the former focuses on damage to the trust property incurred by the trustee's negligent conducts, whereas the latter is mainly concerned with conflict of interests.

### **2.3.3 Trust Administration Expenses**

The expenses incurred in managing trust shall be borne by the trust property, and if the trustee has paid in advance with his/her own property, the trustee has the priority right to seek payments from the trust property (art. 37). It is generally believed that the trustee's right of compensation takes precedence over the interests of the beneficiary and the general creditors of the trust property.

The Trust Law, however, is silent on the issue of whether the trustee's right takes priority over the mortgage and other real rights of security. Some scholars claim that in order to protect the safety of

transactions, the trustee's right of compensation must not be superior to secured creditors' rights. Besides, some commentators even argue that if the trustee is the legal owner of the trust property, it is illogical to give him priority over his own property.

## **2.4 Beneficiary**

### **2.4.1 Acquisition of Beneficial Interest**

If the settlor and the beneficiary are different persons, the issue of when and how the person designated as beneficiary in the trust instrument will acquire the status of beneficiary will arise. In the case of a contract for the benefit of third party, the third party acquires the right at the time when he/she consents to accept the right created. Different from the general rules on contract creating rights for a third party, the beneficiary enjoys the beneficial right of the trust from the date when the trust comes into effect, unless otherwise provided in the trust documents (art. 44). As stated in art. 46 of the Trust Law, the beneficial rights of the trust may be abandoned by the beneficiary. In the event that beneficiary is unable to repay debts, the beneficial interests can be used to pay off such debts, unless restricted by the laws, administrative regulations or the trust documents (art. 47). By virtue of art.48, the beneficial rights of the trust can be transferred and inherited according to the Trust Law, unless otherwise restricted in the trust documents.

### **2.4.2 Beneficiary Right to Supervise the Trust**

The beneficiary has the right to supervise the trust, i.e., how the trustee handles the trust affairs or manages the trust property. The rights enjoyed by beneficiary include the right to (1) require disclosure (art. 20); (2) revoke the deal between the trustee and a third person under certain conditions (art. 22); (3) request for the trust property to be restored to its original status or for compensation of damages (art. 22); (4) dismiss the trustee (art. 23); (5) raise objections to the compulsory enforcement measures taken against the trust property (art. 17); and (6) request the trustee to adjust the management methods of the trust

property (art. 21), etc.

It is worth noting that in this respect, the settlor enjoys the same rights as that of the beneficiary, and if the beneficiary and the settlor hold different opinions about how the rights shall be exercised, the beneficiary may bring an action in court. In practice, however, this rule is very inefficient as litigation is costly and time consuming. The majority view among scholars is that those rights shall be exercised according to beneficiary's opinions, unless otherwise provided by the law or the trust documents. Some commentator even goes further to criticize that Trust Law overemphasizes the protection of the settlor and fails to address the coordination between the settlor and beneficiary, resulting in insufficient protection of the beneficiary.

## **2.5 Modification of a Trust**

The Chinese Trust Law allows modification or change of the administration of the trust, trustees, and the rights of beneficiaries. The default rules on modification of a trust, however, can easily be superseded by provision in trust documents.

### **2.5.1 Modification of Administration**

As to modification of administration, art. 21 provides that if, as the result of special causes that are not foreseeable when the trust was established, the original method for administering the trust is not conducive to achieve the purpose of the trust, or is in conflict with the beneficiary's interest, the settlor or the beneficiary has the right to instruct the trustee to adjust the methods of management of the trust property (art. 49). Again, the problem of possible disagreement between the settlor and the beneficiary would appear.

In the context of charitable trusts, the power to make such instruction is exercised by the competent authorities. Article 69 states, in a similar vein, that if circumstances unforeseeable at the time of the creation of the trust have occurred, the competent authority may amend the terms of the trust in order to accord with the purpose of the trust.

## **2.5.2 Modification of Trustees**

### **2.5.2.1 Removal of Trustees**

A trustee may be compulsorily removed only under limited circumstances. Article 23 provides that if the trustee disposes the trust property against the purpose of the trust or is grossly negligent in his or her administration, use, and disposal of the trust property, the settlor has the power to remove the trustee according to the provisions of the trust documents or to apply to the people's court to remove the trustee. Art. 49 grants the beneficiaries the same power.

Art. 68 states that a trustee of a charitable trust, who violates the trust obligations or does not have the capacity to perform his or her duties, shall be replaced by the competent authority.

### **2.5.2.2 Termination of Trusteeship**

Trusteeship would terminate on any one of the grounds set forth in art. 39 of the Trust Law, namely: (1) the trustee dies or is declared dead; (2) the trustee is declared as a person without civil capacity or a person with limited civil capacity according to law; (3) The trustee appointment is cancelled according to law or the trustee is declared bankrupt; (4) the trustee is dissolved or the trustee loses legal qualification; (5) The trustee resigns or is dismissed; and (6) other circumstances provided by laws and regulations.

Upon the occurrence of one or more of above-mentioned circumstances, the original trustee's successor, executor, administrator, guardian or liquidator is required to take due care of the trust property and assist the new trustee to take over the trusteeship. If there are other trustees, they shall manage the trust affairs or trust property (para. 2, art. 39).

### **2.5.2.3 Appointment of New Trustees**

Upon the termination of trusteeship, art. 40 provides that a new trustee shall be appointed according to the provisions of the trust documents; in absence of such provisions, the settlor shall appoint a new

trustee; if the settlor fails to appoint or doesn't have the capacity to appoint a new trustee, the beneficiary shall make the appointment; or if the beneficiary is a person without civil capacity or a person with limited civil capacity, his guardian shall appoint the new trustee on his behalf according to law.

In accordance with paragraph 2 of the same article, “the new trustee shall inherit the rights and obligations of managing the trust affairs of the former trustee.”

It is worth noting that paragraph 1 of art. 40 only apply to appointing a new trustee to replace an outgoing one. It does not authorize the appointment of additional trustee(s), nor does any other provision of the Trust Law confer such power.

### **2.5.3 Modification of the Rights of Beneficiaries**

According to art. 51 of the Trust Law, the settlor may change or even dispose of the beneficiary's right in one of the following circumstances: (1) the beneficiary seriously infringes upon the rights of the settlor; (2) The beneficiary seriously infringes upon the rights of any of the other joint beneficiaries; (3) with the approval of the beneficiary; and (4) other circumstances prescribed in the trust documents.

Moreover, the settlor may revoke the trust under circumstances 1, 3, or 4.

## **2.6 Termination of a Trust**

One important aspect, which renders the trust superior to other legal devices such as contract or agency, is that it continues in force notwithstanding the death, dissolution, shutdown, or bankruptcy of the parties establishing a trust. Under PRC Trust Law, the grounds whereby a trust may be terminated are the decisions made by the parties to the trust, the impossibility or unfeasibility of its continuation, and its nullification by the People's Court. Once any such ground exists, provisions that facilitate the process of termination and the vesting of the

trust property to appropriate individuals will apply. A charitable trust, however, may be terminated on other grounds.

### **2.6.1 Grounds for Termination**

Grounds for termination of trust can be found in various articles of PRC Trust Law. Accordingly, (1) if the settlor dies or is dissolved according to law, or is cancelled or declared bankrupt according to law, and if the settlor is the only beneficiary, the trust shall terminate and the trust property shall be deemed as his heritage or liquidation property (art. 15); (2) the trust shall terminate if all beneficiaries renounce their beneficial rights of the trust (para. 2, art. 46); (3) where the settlor is the only beneficiary, the settlor or his/her successor may rescind the trust, unless otherwise provided in the trust instrument (art. 50).

Last but not least, art. 53 provides that the trust shall terminate under any of the following circumstances: (1) any of the causes for termination as prescribed in the trust documents happens; (2) the existence and continuance of the trust goes against the purposes of the trusts; (3) the purposes of the trust have already been realized or cannot be realized; (4) the parties of the trust agree to terminate the trust after negotiation; (5) the trust is withdrawn; or (6) the trust is rescinded.

### **2.6.2 The Effects and Process of Termination**

Upon the termination of the trust, the trust property shall be vest to the person stipulated in the trust instrument; if there are no relevant provisions in the trust documents, the attribution of the trust property shall be determined in the following order: (1) the beneficiary or his/her successor; (2) the settlor or his/her successor.

After the property goes to the final recipients upon the termination of trust, any enforcement against the trust property in accordance with art. 17 of the Trust Law shall be enforced against the recipients (art. 56). It is worth noting, however, that in the interim period when the relevant properties are being transferred to these recipients, the trust is deemed to continue to exist, and the beneficiaries are deemed to be

the owner of the trust property (art. 55).

Upon the termination, the trustee is required to prepare a liquidation report on his or her administration of the trust, which needs to be approved by the beneficiaries or the recipients stated in the first paragraph of this section (art. 58). Upon approval, the trustee is released from liabilities arising from matters dealt with in the liquidation report, though he or she continues to remain liable for the wrongful acts he or she had committed during the administration of trust affairs or trust property.

If there is unclaimed remuneration or compensation on trust property upon the termination of trust, the trustee may retain the trust property or make claims to the person who has the right to own the trust property (art. 57).

## **2.7 Public (Charitable) Trusts**

### **2.7.1 Public Purposes**

To be qualified as a public trust, a trust must be established for one of the specified charitable objectives set forth in the Trust Law. According to art. 60, those objectives include: (1) helping poor people; (2) helping disaster victims; (3) assisting the disabled; (4) developing education, technology, culture, art and physical education undertakings; (5) developing medical and sanitation undertakings; (6) developing environment protection undertakings and maintaining the environment; and (7) developing other public undertakings of the society.

### **2.7.2 Special Approval by the Competent Authority**

Alike other trusts, public trusts can be created by a written contract, a written will or other written documents in China. According to art. 62, however, the creation of public trusts and appointment of trustees for such trusts shall be approved by regulatory authority of relevant public undertakings (hereinafter referred to as “competent authority”), and all the trust property of public trust and its proceeds must not be

used for non-public purposes (art. 63).

### **2.7.3 Trust Supervisor**

Each public trust must have a “trust supervisor”, who should be specified in the trust instrument. If there are no relevant provisions in the trust documents, the competent authority shall appoint the trust supervisor (art. 64). The roles of the trust supervisor are twofold: first, he or she is to approve the trustee’s annual reports (art. 67) and, if the trust terminates, the liquidation report (art. 71); secondly, the trust supervisor has the power to bring an action in a court or carry out other legal acts in his own name in order to protect the interests of the beneficiary (art. 65).

### **2.7.4 The Competent Authority’s Power to Modify the Trust**

#### **2.7.4.1 Power to Change the Trustee**

Article 68 of the Trust Law provides that the competent authority shall change the trustee if the trustee of a public trust violates the trust obligations or doesn’t have the capacity to perform his or her duties. Furthermore, the charitable trustee must not resign without approval of the regulatory agency of public undertakings (art. 66).

#### **2.7.4.2 Power to Change the Terms of Trust**

Article 69 of the Trust Law stipulates that where circumstances unforeseeable at the time of the establishment of the trust arise, the competent authority has the power to amend the terms of a charitable trust in accordance with the trust purpose.

### **2.7.5 Termination of Public Trust**

Article 72 specifies that upon the termination of the public trust, if there is (1) no person who has the right to own the trust property or (2) it is the unspecified general public that have the right to own the trust property, the trustee shall, with the approval of the competent authority, utilize the trust property for the original purposes of public interests



or similar purposes, or transfer the trust property to a public organization that has similar purposes or other public trusts.

### 3. Trust Businesses in China + Case Studies

According to art. 4 of Trust Law, an entity that is to carry out trust as its business, i.e., to administer trust affairs and manage trust property as trustee for purpose of running business and collecting remunerations, must acquire a license for the trust business. Currently, in addition to trust companies, which are under the supervision of CBRC, securities companies and their subsidiaries, commercial banks, fund management companies and their subsidiaries, insurance assets management companies, PE management companies are also penetrating into the trust business.

#### 3.1 The Development of Trust Industry Between 2001 and 2014

##### 3.1.1 An Overview

Immediately after the adoption of Trust Law in October 2001, the PBOC publicized *Measures on Administration of Trust and Investment Companies* and *Contemporary Measures on Administration of Pecuniary Trust of Trust and Investment Companies* in 2002, in an attempted to reform the sector by enhancing regulatory oversight and establishing a framework for punishing companies operating outside of the law. The two measures dramatically restricted the business scope of TICs.<sup>4</sup> Despite their dramatically reduced operating scope, TICs quickly rebounded and by the end of 2004 the sector had assets totaling RMB 278.4 billion.

In 2003, the CBRC took over supervisory and regulatory oversight of the trust sector. Immediately afterwards, the CBRC started a new round rule-making and industry restructuring and managed to reduce the number of TICs to a more rational level by January 2005. In 2009, the CBRC revised the 2007 *Measures for the Administration of Trust Companies' Trust Plans of Assembled Funds* by allowing individual investors with

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<sup>4</sup> In particular, TICs were no longer allowed to borrow from abroad, guarantee minimum returns, or take deposits of any sort.

investments equal to, or in excess of, RMB 3 million to be regarded as institutional investors and thus not counted in the cap of 50.<sup>5</sup> This has in turn prompted trust companies to offer their more exclusive, high-return products to individual investors who invest more than RMB 3 million.

China's trust business is making great progress these years. From 2007 to 2014, assets under trust management raised rapidly from 1 trillion to 14 trillion. Having been enjoying fast growth for almost a decade, the trust sector experienced an obvious structural change in 2014, evidenced by the slowdown of growth, decline in performance, and increasing risk in particular areas such as real estate. The whole picture, however, is not all negative.

By the end of 2014, the growth of asset scale and business performance (total revenue, total profit and per capita profit) of 68 trust companies slowed down substantially. The trust industry, however, still achieved steady growth. In contrast to the decline in operating efficiency of trust companies, profits for beneficiaries increased steadily in 2014.

In terms of risk-control, in spite of scattered default events in trust loans and investments, the whole industry continued to maintain a good record in risk management and managed to immune from regional or systematic risk,<sup>6</sup> thanks to the continuous construction of the three risk

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5 Only qualified investors can invest in trust plan of assembled funds (or collective pecuniary trust). A qualified investor must satisfy one of the following conditions and has the capacity to identify, judge and undertake the corresponding risks of a trust plan: (1) a natural person, legal person or any other organization established according to law whose minimum investment in a trust plan is RMB 1 million yuan or more; (2) a natural person whose aggregate individual or family financial assets exceed RMB 1 million yuan at the time when he/she subscribes the trust plan and who can provide the relevant property certificate; (3) a natural person whose annual income exceeds RMB 200,000 yuan or a couple whose annual income exceeds RMB 300,000 yuan for the last three years. The number of natural persons investing in a one trust plan may not exceed 50, while the number of natural persons with a single entrustment of more than RMB 3 million yuan and qualified institutional investors is won't be counted in the 50 cap.

6 It is reported that till the end of 2014, there are 369 projects with hidden risks, involving 78.1 billion, accounting for 0.56%, lower than the bad loan level in bank industry, compared to the data at the end of the second quarter of 2014, the amount (917 million), proportion (0.73%) of the risk projects have both declined.

defense line: capacity cushion, market-based risk disposal capacity, and establishment of industry stability mechanism<sup>7</sup>.

### 3.1.2 The Constitution of Trust Assets

Pecuniary trusts still dominate. In the end of 2014, the size of pecuniary trusts was RMB 13.04 trillion, accounting for 93.28% of the total trust assets nationwide; while the scale of non-pecuniary property trusts was RMB 0.94 trillion, accounting for 6.72% of the total. Starting from 2010, the percentage of non-pecuniary trust assets in the whole trust assets, however, has been presenting a slow but stable rise, 4.86% in 2010, 3.55% in 2011, 6.50% in 2012, 5.49% in 2013, and 6.72% in 2014.

Pecuniary trusts can be further classified into single-settlor pecuniary trusts and collective pecuniary trusts (or trust of assembled funds). In a single-settlor pecuniary trust, there is only one investor (settler), while in a collective pecuniary trust, there are two or more investors. In a typical single pecuniary trust, the client of the trust company set the tone for the trust. In contrast, a collective pecuniary trust is designed by the trust company, and the fees are significantly higher. In other words, the CPT is a standard products sold to multiple investors, while the SPT is a product tailored to individual client's requirements. According to China Trustee Association, by the end of third quarter of 2014,

Table1: Business Data of Trust Companies (3rd Quarter 2014)

|                            |             |              |
|----------------------------|-------------|--------------|
| Collective Pecuniary Trust | Amount      | 377142758.80 |
|                            | Composition | 29.13%       |
| Single Pecuniary Trust     | Amount      | 841783840.75 |
|                            | Composition | 65.01%       |
| Non-cash Property Trust    | Amount      | 75905198.84  |
|                            | Composition | 5.86%        |

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<sup>7</sup> The CBRC worked hard to promote "Eight Mechanisms" in trust industry in the year of 2014, namely "Corporate Governance Mechanism", "Product Registration System", "Classification Management Mechanism", "Capital Constraint Mechanism", "Mechanism of Social Responsibility", "Restoration and Disposal Mechanism", "Industry Stability Mechanism" and "Regulatory Evaluation Mechanism".

SPTs accounted for nearly 65.01% of the trust assets under management, while the proportion of CPTs and PMTs were just approximately 29.13% and 5.86% respectively (see Table 1).

### 3.1.3 The Declining Trust for Financing Purpose

The proportion of financing trust (debt trust) in the year 2014 continued to decline and dropped to below 40% for the first time (33.65%), compared to the historically highest percentage (59.01% in 2010), and 47.76% at the end of 2013. At the same time, the proportion of investment trusts and property management trust is steadily increasing. In 2014 investment trust (equity trust) accounted for 33.70%, 9.83 percent higher than the historically lowest proportion (23.87% in 2010), 1.16% above the proportion 32.54% in the end of 2013. Property management trusts accounted for more than 32.65% in 2014, exceeding 30% for the

Table2: Business Data of Trust Companies (3rd Quarter 2014)

|                                       |             |              |
|---------------------------------------|-------------|--------------|
| Infrastructure                        | Amount      | 265774744.88 |
|                                       | Composition | 21.8%        |
| Real Estate                           | Amount      | 126530983.17 |
|                                       | Composition | 10.38%       |
| Securities (Stocks)                   | Amount      | 43014276.16  |
|                                       | Composition | 3.53%        |
| Securities (Public Offering Funds)    | Amount      | 13003992.85  |
|                                       | Composition | 1.07%        |
| Securities (Bonds)                    | Amount      | 110660867.41 |
|                                       | Composition | 9.08%        |
| Financial Institutions                | Amount      | 191781898.83 |
|                                       | Composition | 15.73%       |
| Industrial and Commercial Enterprises | Amount      | 314723951.2  |
|                                       | Composition | 25.82%       |
| Others                                | Amount      | 153435885    |
|                                       | Composition | 12.59%       |

first time, an 19.90% rise compared to the historically lowest percentage in 2011 (12.75%), and an increase of 12.95% compared to 19.70% at the end of 2013.

### 3.1.4 Major Investment Fields of Trust

As for year 2014, the five major investment fields of trust are, industrial and commercial enterprises, infrastructure, financial institutions, securities market, and real estate development. Statistics show that at the end of the fourth quarter of 2014, RMB13.04 trillion trust money was invested in those five major areas. Table 2 shows a more detailed statistics in the third quarter of 2014.

### 3.1.5 The Launch of Trust Service to Wealthy Families

In 2013, there are about three trust companies which had started to provide the family trust service. The business will certainly grow in China some day in the future. For the moment, however, family trust business is small in scale. The business will have to be carried out in compliance with the Marriage Law and Succession Law, in addition to trust law.

## 3.2 Case Studies

### 3.2.1. Real Estate Trust

Strictly speaking, real estate trust is not a legal term. In practice,

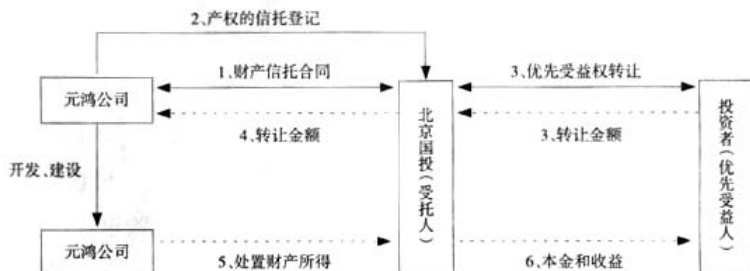


图1 “盛鸿大厦”信托项目操作流程

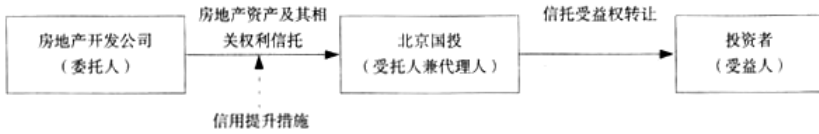


图2 财产(房地产)信托业务模式

any trust that is designed to raise money to finance the development of real estate can be called a real estate trust. A real estate trust can be pecuniary trust or property trust. Real estate trust may finance a real estate development by lending the project company (debt trust) or contributing new capital into the company (equity trust). Most real estate trusts in China are debt trust.

The diagrams above show the transaction structure of “Shenghong Mansion” trust, which take the form of property trust. As shown in the diagram, the deal is carried out in the following steps: (1) Yuan Hong Co. Ltd. entrusted its real estate development project-Beijing Shenghong Mansion (with a market value of 0.41 billion RMB) to Beijing International Trust Co. Ltd. to establish a property trust, with Yuan Hong Co. Ltd. as the settlor and the sole beneficiary. (2) The beneficiary rights in the Trust were divided into two tranches, superior beneficiary rights and general beneficiary rights. Yuan Hong kept the general beneficiary rights and assigned the superior beneficiary rights (approximately 0.25 billion RMB) via Beijing International Trust Co. Ltd (agent) to investors (superior beneficiaries of the trust). (3) Beijing International Trust Co. Ltd, the trustee, contracted with Yuan Hong Co. Ltd., to have Yuan Hong manage the trust property, the project of Beijing Shenghong Mansion. All the profits earned from the project were put into a special bank account opened by Beijing International Trust Co. Ltd. for the trust plan.

A key feature of the deal is the tranches of beneficiary rights, by giving the investors the superior tranche, the settlor actually provided a kind of personal guarantee. What is uncertain in the deal, however, is

what was assigned from the settlor to the trustee, i.e., the trust property. Is it the whole mansion project, or the right to profits from the operation of the project? It certainly makes more sense to have the mansion project rather than just entitlements to its profits as trust property. The problem, however, is that registration of trust real property is yet to develop in China. Article 10 of the Trust Law requires trust registration before a trust of real property can come into effect. That explains why many trust of the same line in China will take the form of pecuniary trust rather than property trust, and why in those deals, extra credit enhancement mechanisms will have to be provided.

### 3.2.2 REITs?

#### 3.2.2.1 Overview

While in the U.S., REITs may take the form of a trust, a corporate or other organizational structure, so far as it meets various tests on assets, sources of income, distribution of profits, etc., in many other jurisdictions such as Taiwan, Hong Kong, Australia, and Japan, REITs takes the form of trust.

China has yet to develop public REITs.<sup>8</sup> The real estate trust in China is different from REITs in at least two perspectives: (1) unlike REITs, real estate trusts in China are mainly debt trust to finance project on development, while in many jurisdictions, REITs are prohibited or restricted from investing in developing project. (2) Most of real estate trust plans are tailored for a single specific project and normally will be completed in a couple of years, while REITs in most jurisdictions are on-going operation and invest in various project. Actually, in most jurisdictions REITs are not allowed to concentrate its investments to a single project.

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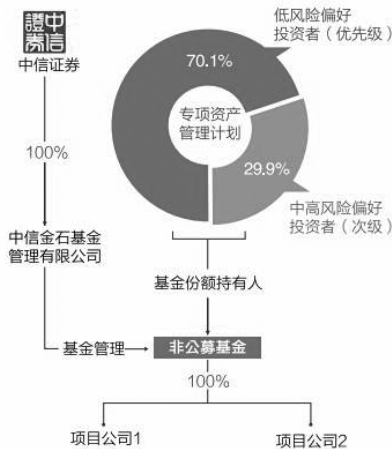
<sup>8</sup> It is reported that Penghua Qianhai Vanke Securities Investment Fund (“鹏华前海万科REITs封闭式混合型发起式证券投资基金”) succeeded its registration with the CSRC on June 8, 2015. The fund, however, are not public REITs.

### 3.2.2.2 CITIC “QI HANG”

Diagram 3 demonstrates the basic transaction structure of “Qi Hang” Plan (a 3-5 years plan). As shown in diagram 3, the deal was carried out in the following steps: (1) Project company 1 and project company 2 were established to own Beijing CITIC Securities Mansion (value at RMB 3.502 billion) and Shenzhen CITIC Securities Mansion (valued at RMB 1.503 billion) respectively. The two project companies are 100% controlled by CITIC. (2) CITIC established CITIC Golden Stone Fund (“Fund”) with a registered capital of RMB 100 million. The Fund took over CITIC’s equity in project companies 1 & 2 at a price little bit higher than RMB 5.04 billion. (3) The Fund paid the price by the money raised from issuing fund units to investors. The fund units were divided into different tranches, with superior RMB 3.65 billion tranche for investors who subscribed at least RMB 5 million each, and inferior RMB 1.56 billion for investors who subscribed at least RMB 30 million each. (4) On May 21, 2014, the fund units were traded in a special trading platform

Diagram 3

#### 中信启航专项资产管理计划交易结构



资料来源：中信证券



for institutional investors under the aegis of Shenzhen Stock Exchange.

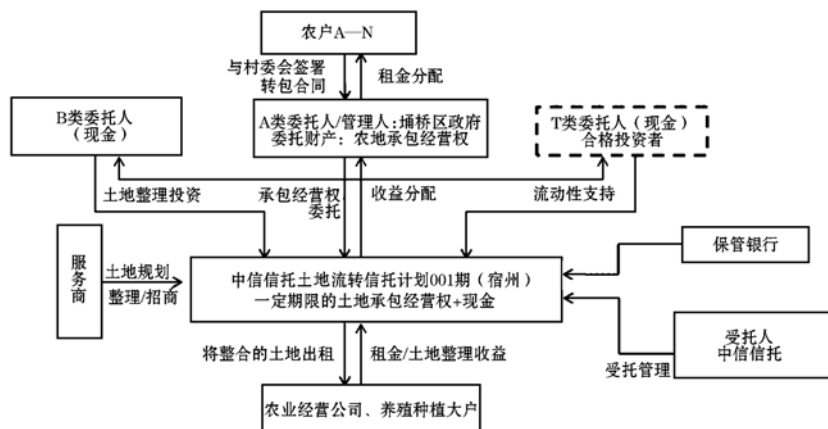
As for the distribution of profits from the two project companies, it is agreed that Fund takes 1.5% from the money received as management fee each year; while 70% of the rest goes to the superior-unit-holders and 30% goes to the inferior-unit-holders. By the end the trust plan, if there is an appreciation in the trust assets of the plan, the superior-units-holders are entitled to 10% of the appreciation in cash, while the inferior-units-holders will share 90% of the appreciation in cash or in other forms.

While Qi Hang is yelled as a deal most alike REITs, given that the units are only traded in a platform only open to qualified investors. It has still a long way to go and many obstacle to overcome before it can be converted into public REITs.

### 3.2.3 CITIC Trust of Farmers' Contracted Management Rights on Rural Agricultural Land in Suzhou City, Anhui Province

As shown in Diagram 4, there are two trusts, one PT between the Yongqiao district government and CITIC, one pecuniary trust between various qualified investors and the CITIC; or, in CITIC's statements, two

Diagram 4



class of settlors, one entrust management rights on farmers' contracted land to CITIC, the other (B class & T class) settlors entrust their money to CITIC. I shall try to explain the deal structure as two trusts.

The structure of the PT on farmer's contracted agricultural land can be summarized as follows: (1) The government of Yongqiao District, Suzhou city in Anhui Province, entrusted the right to manage the land, which involved 891 acres of land owned by Zhumiao Village and Taqiao Village of Zhuxianzhuang town of Yongqiao District, to CITIC Trust. The trust where the government of Yongqiao District is the settlor and the beneficiary on behalf of the right-holders (individual farmers) while CITIC serves as trustee will last for 12 years. (2) The Yongqiao district government obtains authorization to entrust the 891-acre-land to CITIC by a three-tier contract arrangement, one between farmers in the two villages and the respective village committee, i.e., Zhumiao village committee and Taqiao village committee, authorizing the committees to assign management rights on farmers' contracted agricultural land on behalf of them, the second between the two village committees and the government of Zhuxianzhuang town, authorizing the town government to assign management rights on farmers' contracted land, the third between the town government and the government of Yongqiao District, authorizing the district government to assignment management rights on farmers' contracted land. (3) Agricultural companies rent land from the trustee and pay rents to the trustee.

In the PT, there are two classes of settlors. Class B settlor entrusted their money to CITIC, which lent the money to agricultural companies for land improvement, while class T settlors entrusted their money to CITIC, to secure the liquidity of the trust plan.

CITIC made the above-described two trusts into a scheme, where there are three classes of beneficial rights, class A, class B, class T. The income of the trust are to be distributed roughly in the sequences of A, B and T.

The major obstacle in the deal is the prohibitive provisions in China law preventing farmers from assigning their contract rights to manage the agricultural land to a third party. In this deal, CITIC stated that the trust property is not the contracted right to manage the land as a whole, but the right to manage the land only. Right to manage the land, however, is unclear under Chinese law, although at policy level, it is already decided that farmers are entitled to transfer right to manage the land on their contracted agricultural land.

## **4. Some Fundamental Theoretical Problems**

### **4.1 Compatibility of Trust in the Civil Law System in Terms of the Ownership of the Trust Property and the Nature of Beneficiary Right**

#### **4.1.1 Does Entrustment Necessarily Result in the Transfer of Title?**

The common law jurisdiction position that the trustee owns legal title on trust property while the beneficiary has the equitable title is identified as one of the most severe obstacles preventing civil law countries from adopting trust. The dual titles on one property violate an inherent principle of civil law called “Bestimmtheitsgrundsatz”, i.e., one title on one property.

PRC Trust Law avoids the obstacle by adopting a vague term in its art. 2, which reads as follows: “the settlor entrusts certain property rights it owns to the trustee and the trustee manages or disposes of the property rights in its own name in accordance with the intentions of the settlor and for the benefit of the beneficiary or for specific purposes.” As the trust property is “entrusted” rather than “transferred” or “disposed”, it is not necessarily that the legal title goes to the trustee. By the vague expression, the lawmakers managed not to answer the title issue.

Scholars hold different views on whether the title is transferred by “entrustment”. The first view is that the settlor owns the trust prop-

erty and the trustee manages the trust property on behalf of him. The second view is that trust property is independent property with certain purpose and without owners. The third opinion is that the beneficiary owns the trust property; since the beneficiary will get the interests of the trust property at last and he/she has some substantive claims same as the settlor (arts. 20-23).

#### **4.1.2 The Nature of Beneficial Right**

The nature of beneficial right is a subsequent question arising out of the debate on who hold the title of trust property. Again, art.44 of PRC Trust Law uses a vague term “beneficial right”, to avoid defining the nature of beneficial rights.

As mentioned in previous part, under PRC Trust Law, however, the beneficiary not only has the right to accept trust benefits, but also has some substantive claims same as the settler. Those provisions lead to the debate on the nature of beneficiary rights. Scholars proposed three different understandings of the nature of beneficiary rights, i.e., the personal rights (creditor’s right) position, the rights in rem (or ownership) position, and the new type of right position. Those who hold the third view argue that the beneficiary right has both natures of creditor’s rights and right in rem, similar to shareholder’s right.

As professor Nomi rightly pointed in his excellent notes on Japanese Trust Law, most of the debates around the issue, are only of theoretical nature, because the law makers always have the privilege of listing specific rights for the beneficiary without defining the nature of beneficiary right.

#### **4.2 When Does a Trust Come into Effect?**

As mentioned before, alike the position of Japanese trust law, trust is regarded as an arrangement between the parties. According to para. 3, art. 4, “[w]here a trust is established in the form of written contract, such a trust shall be deemed established when the trust contract is concluded. As for trust created by other written documents, the trust is

deemed established when the trustee promised the trust.”

Art. 10 of the Trust Law, however, creates confusions on the point. Art. 10 requires the registration of trust for trust of which the trust property are those which the law or administrative regulations requires so, including, but not limited to: real property, motor vehicles, aircrafts, ships, stock rights and IP rights. According to art. 10, if the parties didn't apply for such registration, they shall apply later, otherwise the trust won't come into effect.

More than a decade after the adoption of Trust Law, the trust registration mechanism is yet to be established in China. The majority view is against the position of art. 10. It is argued that the effect of the registration is to make the trust valid against the public.

### **4.3 Shall the Trustee's Liability to Third Parties be Limited to the Trust Property?**

It is clear under PRC trust law that trustee's liability to pay trust benefits to the beneficiaries is restricted to the trust property (art. 34). This is certainly an appropriate position. The question is whether the trustee's liability to third party arising out of his administration of trust affairs shall also be limited to the trust property. PRC trust law obviously takes the “yes” position. Paragraph 1 of art. 37 of the law reads as follows: “The fees paid and debts owing to a third party by the trustee due to the administration of the trust affairs shall be borne by the trust property. If the trustee effects such payment in advance with his own existing property, he shall have the prior right to be compensated by the trusted property.”

There are arguments against the position of art. 37. Many people take the view that normally, the property in the name of the trustee includes trustee's inherent property and the trust property, and when a third party deals with the trustee, the third party might not be aware that the trustee is handling the trust affairs for a specific trust plan. It is therefore unfair to limit the trustee's liabilities to the trust property.

In this regards, the publication requirements in Japan on limited liability trust might be a proper way to solve the problem.

## 5. The Future of Trust Law and Trust Business in China

### 5.1 Another Round Restructuring of Trust Business in China?

As evidenced by various statistics given in section 3, trusts in China are nowadays more a source of financing, supplementing banking and securities industries, or to be more accurately, standing along with banking and securities industries.

The growing role of trust companies in sourcing funds to industries is not without problem. Since 2012, there have been a number of high profile defaults and near defaults by trust companies. As part of the efforts to solve the problem, on April 8, 2014, the General Office of CBRC issued *Guiding Opinions on Risk-regulating-and -supervising of Trust Companies* (中国银行业监督管理委员会办公厅关于信托公司风险监管的指导意见关于信托公司风险监管的指导意见 (银监办发[2014]99号, hereinafter the No. 99 Guidance) . The No. 99 Guidance, naming risks faced by trust business as shadow-banking business risk, calls among other things, for the trust industry to strengthen their capacity to provide bespoke family trust services to China's wealthy families, for the establishment of registration and information system of trust products, and to classify trust companies into different classes according to their qualification and track record, and to license companies in different classes for different trust businesses.

The No. 99 Guidance might denote another round of the restructure of trust companies nationwide. The focus of the restructuring, according to the reporter's reading of the document, will be internal rather than external. In other words, trust companies in China are encouraged to enhance its internal control and risk-management capacity, and to adjust their business in accordance with their capacity and inherent capital.

## 5.2 China Trust Security Fund

The No. 99 Guidance called for the establishment of China Security Fund, as a mechanism to protect the clients and to safeguard the sustainable development of the whole industry. On December 10, 2014, CBRC and Ministry of Finance jointly issued *Administrative Measures of China Trust Security Fund* (《信托业保障基金管理办法》(银监发[2014]50号)). According to the Measures, China trust security fund shall be a mutual fund; a limited liability company-China Trust Security Fund Limited Liability Company shall be established to manage the fund. The major sources of fund are contribution from trust companies. The fund shall be used to pay for: (1) the reorganization of trust companies in administrative liquidation procedures; (2) reorganization of trust companies in bankruptcy procedures; (3) the liabilities and debts of trust companies which are ordered to close or dissolve due to their illegal operation; (4) liquidity support of trust companies; and (5) other necessary items.

On December 19, 2014, China Trust Security Fund Limited Liability Company was established in Beijing.

The fund will certainly have some impact on the industry.

## 5.3 Proposals of China Trustee Association on the Amendments of Trust Law

China Trustee Association is pushing hard to make necessary amendments to the Trust Law. In 2014, the Association published draft amendments, proposing : (1) to redefine trust businesses (or commercial trust operations) by applying trust law to trust businesses carried out by other financial institutions (securities companies and their subsidiaries, commercial banks, fund management companies and their subsidiaries, insurance assets management companies, PE management companies and etc.); (2) to clarify the meaning of “assign to” in article 2 of the Trust Law; (3) to allow declared trust (or self-trust); (4) to clarify the issue of when does a trust come into effect, in particular, whether transfer of property is required for a trust to come to effect; (5) to establish a prop-

er trust registration system; (6) to clarify the liabilities of trustee to the person who entrusted with trust affairs; (7) to specify the standards of trustee's duties, in particular the standards for duty of care; (8) to clarify the meaning of “the regulatory agency of relevant public undertakings” (有关公益事业的管理机构) under art. 62 of Trust Law.

Those proposals are not necessary all in the right tracks. And so far as the reporter is aware about, Trust Law may not be amended in the near future. The problems identified by the association behind those proposals, however, shall be paid special attention to.

#### 5.4 Anxin Trust Co. Ltd. Vs. Kunshan Chungao Investment and Development Co. Ltd (安信信托昆山纯高资产收益权信托案)

The Case (hereinafter referred to as Kunshan Chungao case) is recognized as a landmark case in 2013.

As shown in Diagrams 5 & 6, there are two transactions between the disputed parties. Those deals are carried out in the following sequences: (1) In September 2009, Kunshan Chungao Investment and Development Co. Ltd. (hereinafter referred to as Kunshan Chungao) and

Diagram 5: In the Eyes of Kunshan Chungao

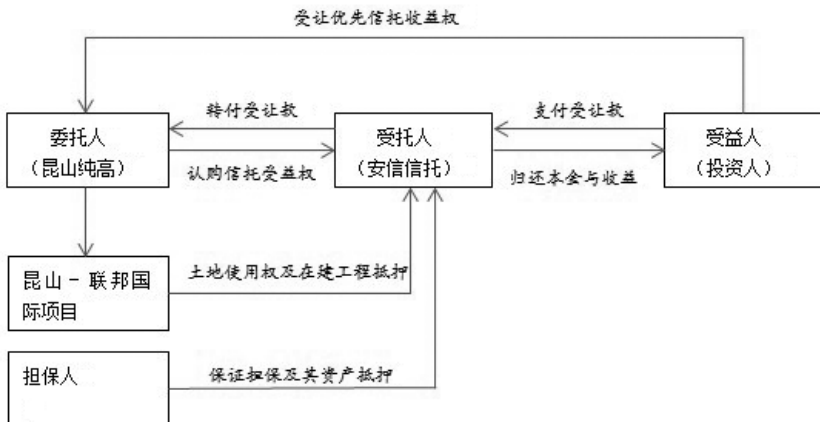
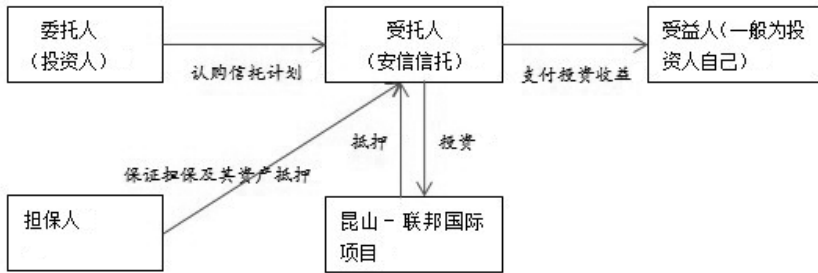




Diagram 6: In the Eyes of Anxin Trust



Anxin Trust Co. Ltd. (hereinafter referred to as Anxin Trust) signed “Right to the Income from Assets of Kunshan· Federal International Project Trust Contract” (昆山·联邦国际资产收益财产权信托合同, hereinafter referred to as Property Trust Contract). Under the contract, Kunshan Chungao, the settlor, entrusted its right to the income from Assets of Kunshan· Federal International Project (hereafter referred to as “right to the income”) to Anxin Trust to set up a PT. The right to the income was valued at RMB 627 million. The beneficiary’s rights were classified into two tranches. Kunshan Chungao held the general beneficiary rights itself, while the superior beneficiary rights were sold to public investors at a price higher than RMB 215 million. To secure the beneficiary rights of public investors, Kunshan Chungao agreed to mortgage the assets of the projects, namely, the land use rights and buildings (including those under construction) to the trustee. (2) To facilitate the registration of mortgage, the two parties entered into a Trust Loan Contract (hereinafter referred to as “loan contract”) on the same day of signing the PT contract, and registered the mortgage to secure the lender’s rights accordingly.

Kunshan Chungao kept performing its payment obligations but failed to meet the payment requirements in September 2012. Anxin Trust brought an action against Kunshan Chungao on the basis of the loan contract, claiming for the payment of remaining loan principal

(RMB 128.4 million), and a liquidated damage of RMB 5.385 million. Kunshan Chungao only agreed to bear the default liabilities of the property trust contract because the loan contract was only signed to facilitate the mortgage registration and therefore not binding. Under the property trust contract, Kunshan Chungao was only obliged to pay a penalty of RMB 10 million.

The court of first instance, Shanghai Second Intermediate People's Court<sup>9</sup>, held that, on the one hand, the loan contract was signed after the conclusion of the property trust contract; on the other hand, evidences showed that the parties were performing the property trust contract, rather than the loan contract, and therefore the dispute between the parties shall be a business trust dispute government the property trust contract. The court therefore decided in favor of KunShan Chungao. The appellate court Shanghai High People Court<sup>10</sup> supported the court of the first instance in its judgment: (1) the dispute between the parties shall be solved on the basis of the property trust contract; (2) the mortgage and personal guarantee shall be valid and enforceable.

The court further held that right to the income of assets is qualified to be the trust property. That is a great relief for the business. As mentioned in the previous part, due to the lack of trust registration system, and more importantly, due to business considerations (the settlor in most circumstances is not willing to transfer the full title of the real estate development project to the trustee for tax reasons, etc.), and therefore in most real estate trusts in the form of PT, the trust property is the right to the income of the real property, rather than the real property.

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9 上海市第二中级人民法院 (2012) 沪二中民六 (商) 初字第7号民事判决。

10 (2013) 沪高民五 (商) 终字第11号民事判决书。