

Special Lecture on Trust Law

Lecture No. 11

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Faculty of Law, University of Tokyo

Hideki Kanda

(Part 1)

Subject of Interest—“Commercial Trust”

1. Japanese trust business: characteristics and such viewed from statistics
2. General survey of laws and institutions concerning Japanese trust
3. Regulation for Japanese trust business
4. Japanese “commercial trusts” and major legal problems
 - (1) Principle points at issue
 - (2) Specific points at issue by type
 - Deposit type of commercial trust
 - Investment type of commercial trust
 - Conversion type (fluidization type) of commercial trust
 - Enterprise type of commercial trust
5. Topics in recent years

Regulation for Trust Business

(1) Outline of regulations

- Regulation on entry (opening business), ○ one on scope of business services (one on specialty, ○ adjustment with other fields), ○ one on deed, ○ one on financial affairs, ○ others

(2) Major provisions

- Acceptance of trust = business-oriented commercial transaction (Art. 502, item (xiii) of Commercial Law) = "trust business"
- Trust Business Act, the enforcement regulations for Trust Business Act, Ordinance for Enforcement of Trust Business Act
- Sideline Act, the enforcement regulations for Sideline Act, Ordinance for Enforcement of Sideline Act
- Special laws: Loan Trust Law, Law Concerning Securities Investment Trust and Securities Investment Companies, Law on Liquidation of Assets, others (Financial Products Exchange Law, Collateralized Bond Trust Law, Financial Products Sales Law, etc.), [the tax law being also important]

Need for Idea of “Commercial Trust Law”

- Trust Law and the Law-based trust theory are inadequate (= Particularly, the old Trust Law assumed civil trusts.)
- Although a majority of trusts carried out in Japan is commercial trusts, a discussion of legal principles worthy of the status was absent in the past. (=Civil trusts differ from commercial trusts.)

History of Building Legal System

- In recent years, a part of a theory of “commercial trust law” was actualized by special laws. (the revision in 2000 of “Law on Liquidation of Assets,” the revision in 2000 of “Law Concerning Securities Investment Trust and Securities Investment Companies ”, etc.)
- Ministry of Justice had been studying since Oct. 2004 a full-fledged revision of the existing Trust Law in Legislative Council’s Sectional Meeting for Trust Law, bill of which was introduced to a regular session of the Diet in the spring of 2006, passed in Dec. 8, 2006, and promulgated on Dec. 15, 2006 (Law No. 108).
- Financial Service Agency deliberated on/put in order the review (part 1 of the series) of business laws concerning trusts by setting up the trust working group in the second sectional meeting of Financial System Council’s Finance Subcommittee (Jul. 2003) ⇒ Bill was introduced in a regular session of the Diet in the spring of 2004, passed/ promulgated/ enforced in Dec. 2004. Combined with the above revision of Trust Law, the bill concerning the revision of Trust Business Act was introduced in a regular session of the Diet in the spring of 2006, which was passed as the improvement law on Dec. 8, 2006, and promulgated on Dec. 15 that year (Law No. 109).

Substance of Commercial Trust

- Civil trust = emphasis on the settlor's intent; commercial trust = insignificance in the settlor's intent
- Civil trust = emphasis on property in trust; commercial trust = emphasis on the scheme (Property in trust ordinarily changes daily.)
- Civil trust = trustee's roles being the management/ disposition of property; commercial trust = trustee's roles being more than these under normal conditions

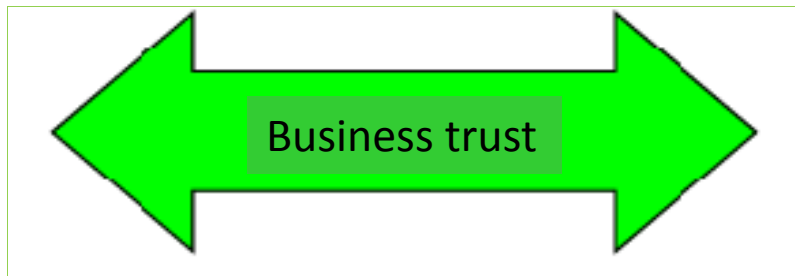
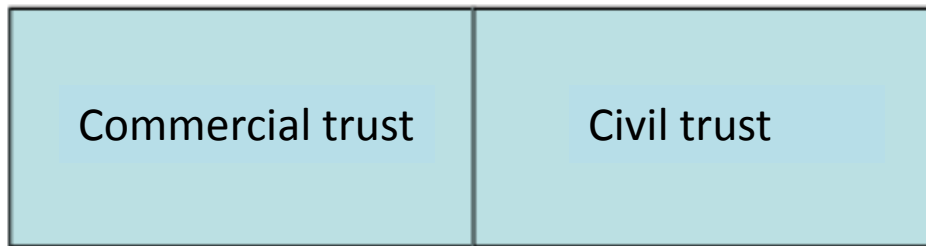
Approach to Commercial Trust Law = Typology

- What is conducted is the point. (= Focus on the economic substance in an arrangement)
 - Deposit type of commercial trust (e.g., loan trust)
 - Investment type of commercial trust (e.g., joint-operation money trust, investment trust)
 - Conversion type of commercial trust (e.g., trust for fluidization)
 - Enterprise type of commercial trust (e.g., land trust)

Future Prospect of Commercial Trust Law

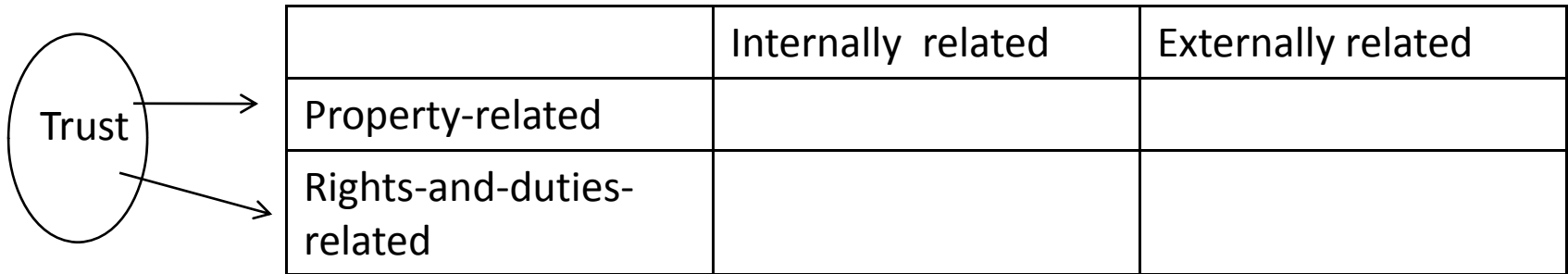
- (1) Establishment of Commercial Trust Law theory
 - Settlement of the theory upon which typology is founded
 - Settlement of appropriate rules in variety to adjust interests responding to market needs
- (2) Beyond commercial trust
 - Transversal improvement of “fiduciary duty”

Relationship among Civil Trust, Commercial Trust and Business Trust

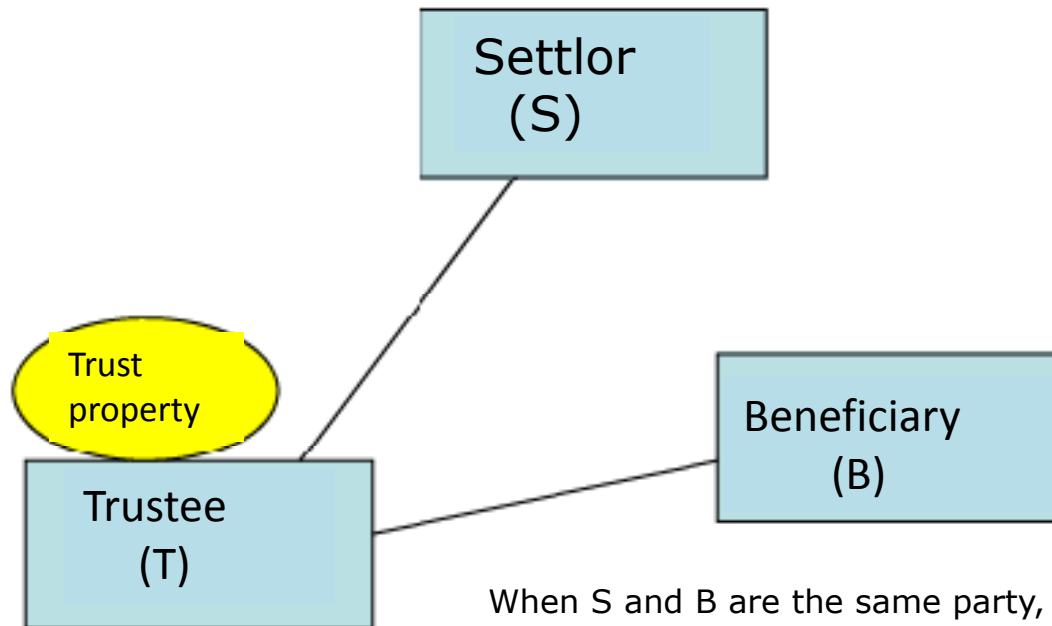


(Note) There are cases in which the commercial trust and business trust are used in the same meaning.

Situations Trust Law Covers: Concept of “Commercial Trust” is Required in Each Situation

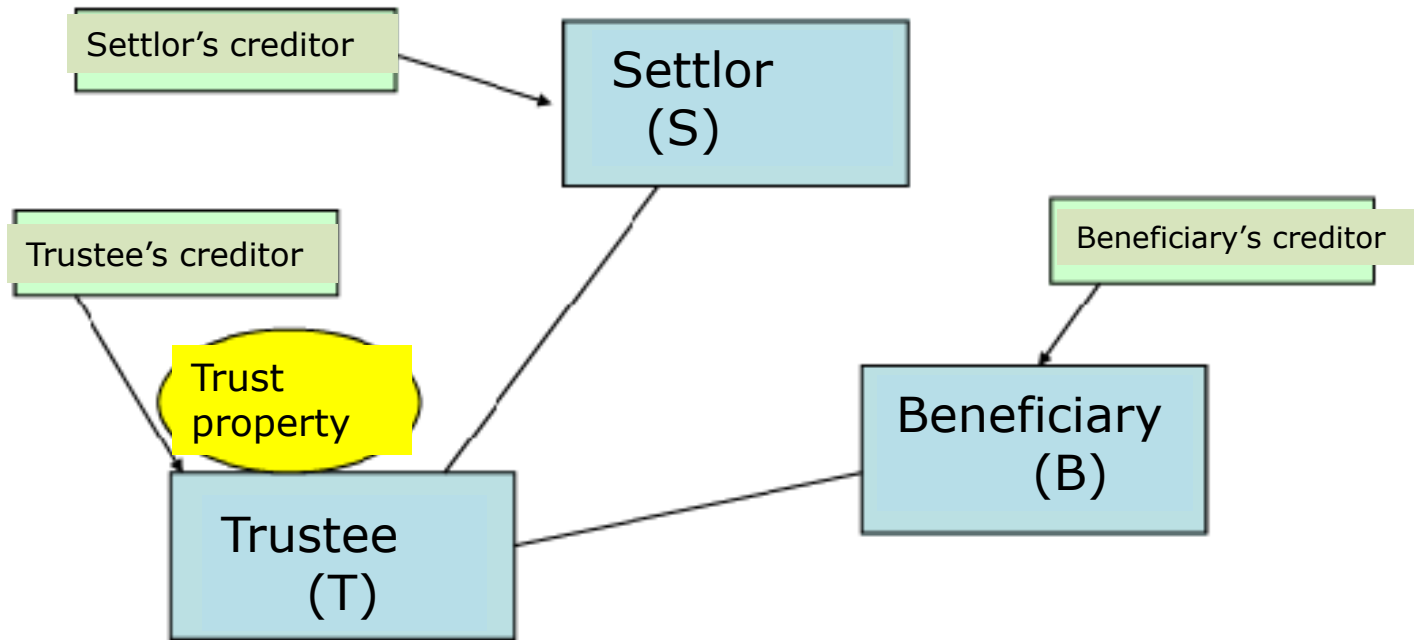


Parties of Trust



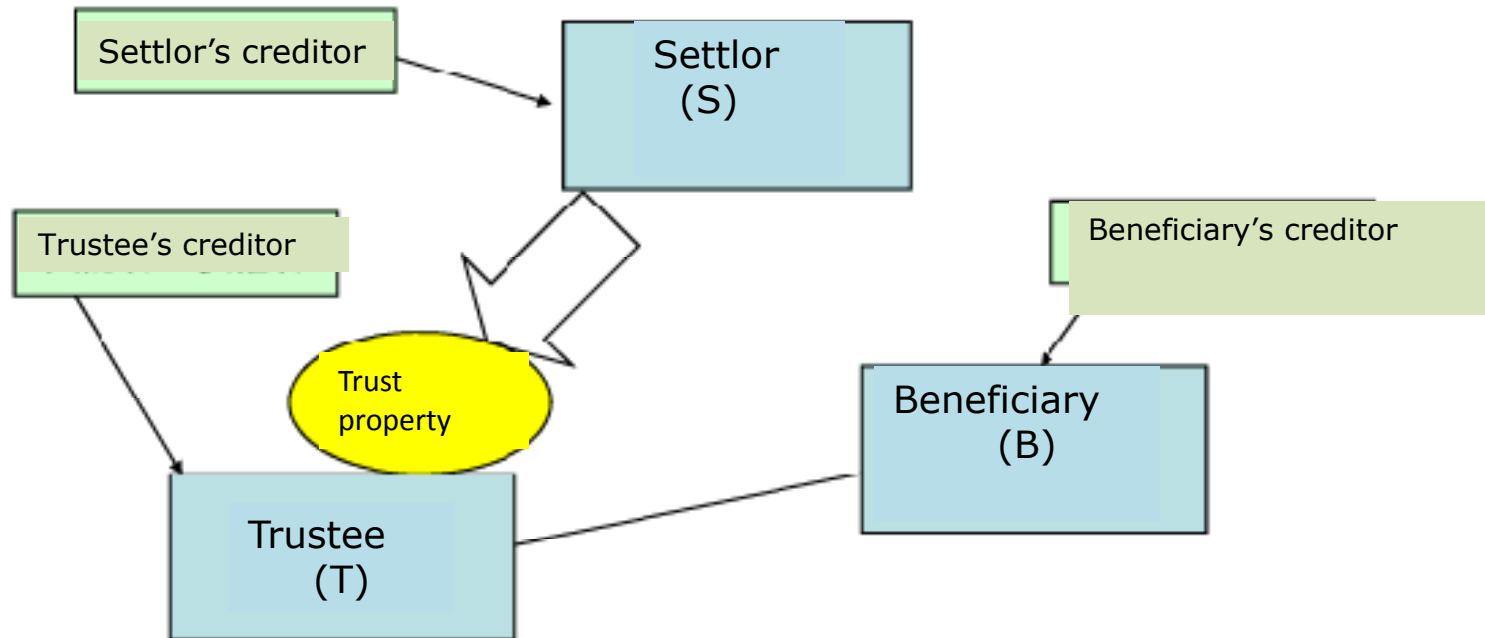
When S and B are the same party, it's called "self-interest trust," and when different, "trust for other's interest": most cases are actually the former in Japan.

Parties of Trust

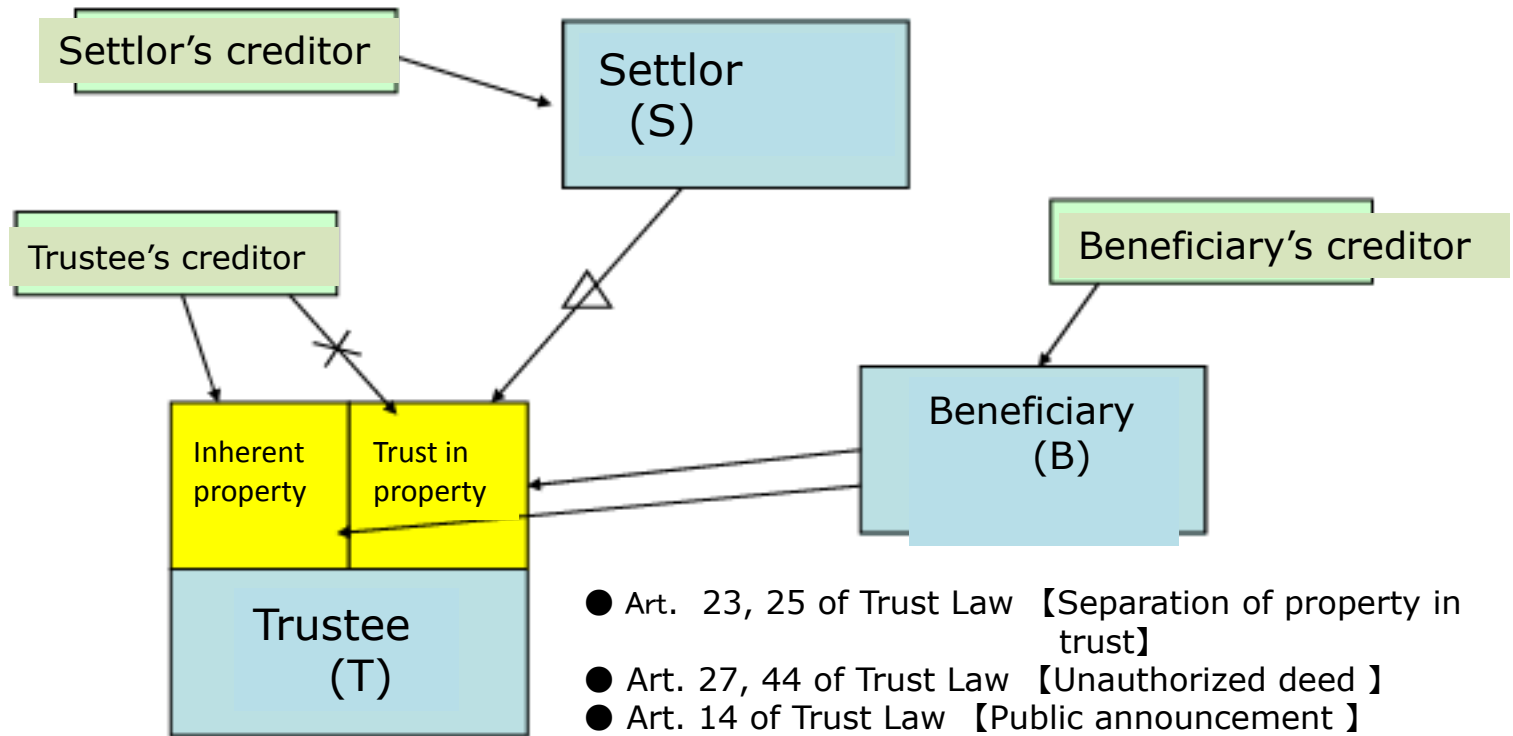


Completion of Trust

(Art. 3 & 4 of Trust Law)

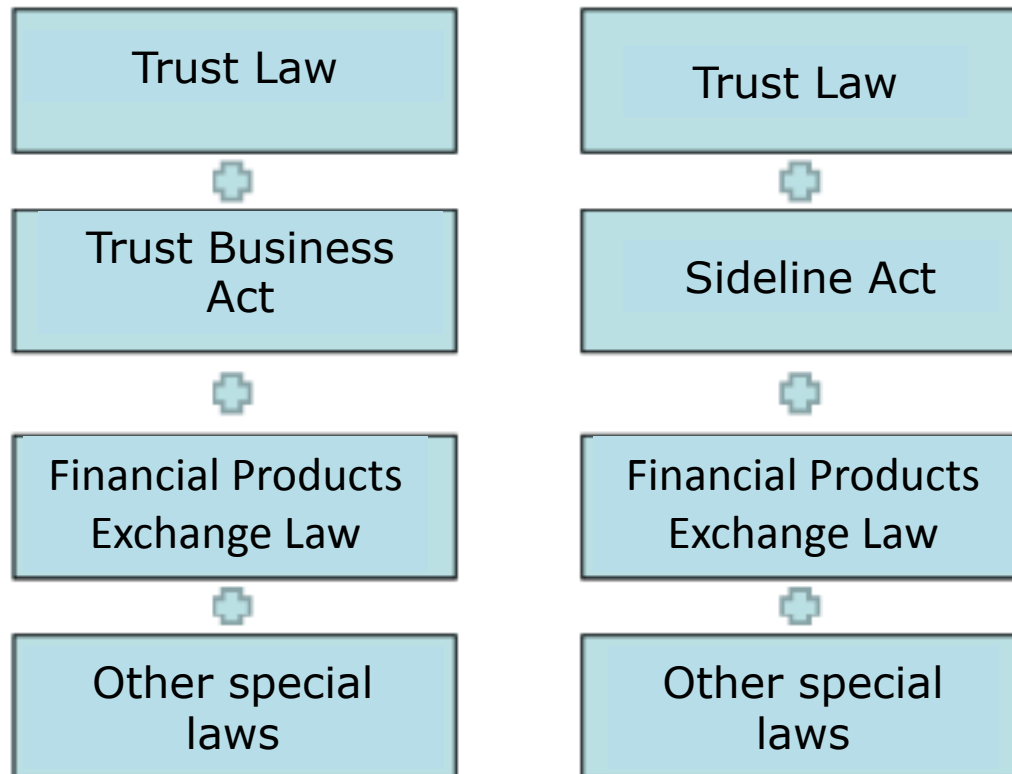


Trust: Relationship of Property



- Art. 23, 25 of Trust Law 【Separation of property in trust】
- Art. 27, 44 of Trust Law 【Unauthorized deed】
- Art. 14 of Trust Law 【Public announcement】
- Art. 34 of Trust Law 【Separate management】

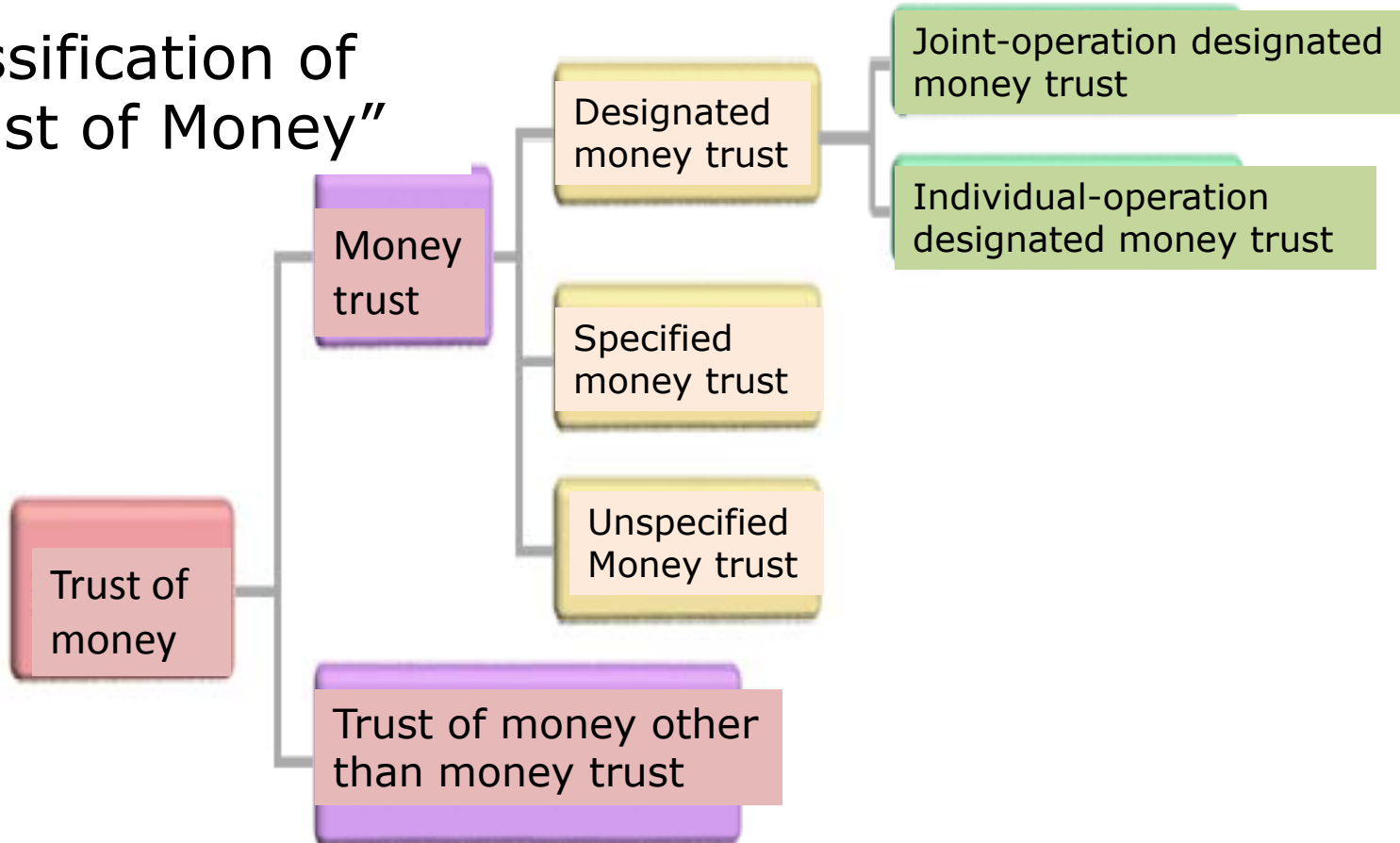
Legal Structure for Trust



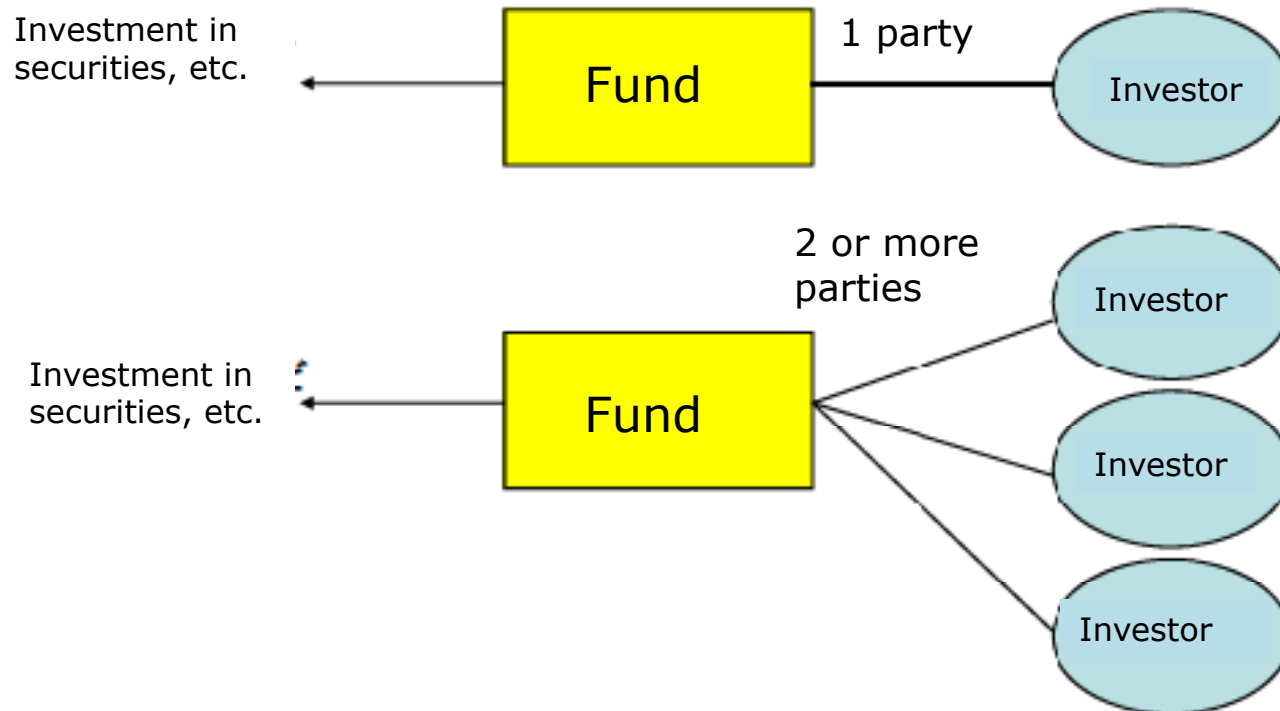
	Trust Law	Trust Business Act (2-I of Sideline Act to be applied correspondingly)
Care duty	29	28 II
Duty of loyalty	30, 31, 32, (33)	28 I, 29
Duty of separate management	34	28 III
Commission (duty of self-execution)	35	22, 23
Official notice	14	30
Separation of property	23, 25	
Unauthorized deed	27 (44)	

Note: There are stipulations in other specific special laws (the law on investment trusts, the law on fluidization of assets, Loan Trust Law, etc.).

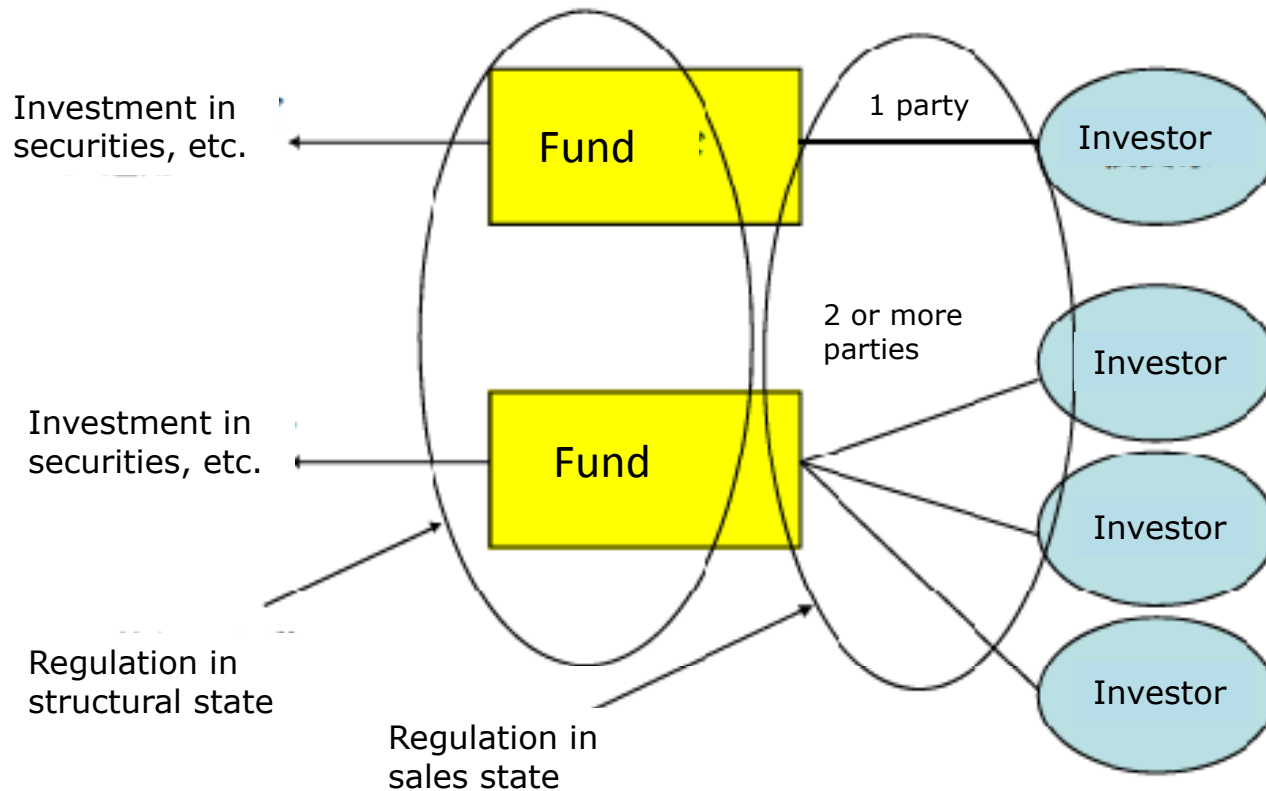
Classification of "Trust of Money"



Number of Investors



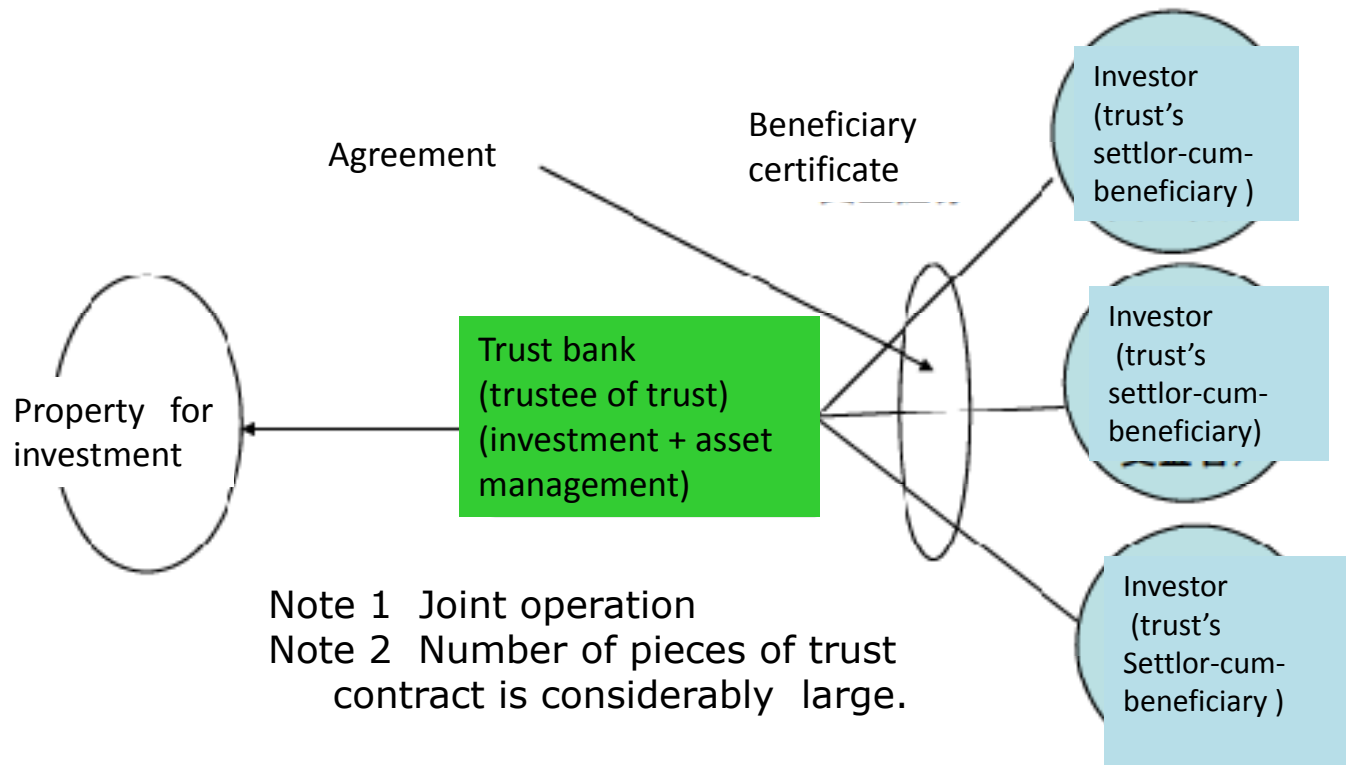
Structural Regulation and Sales Regulation



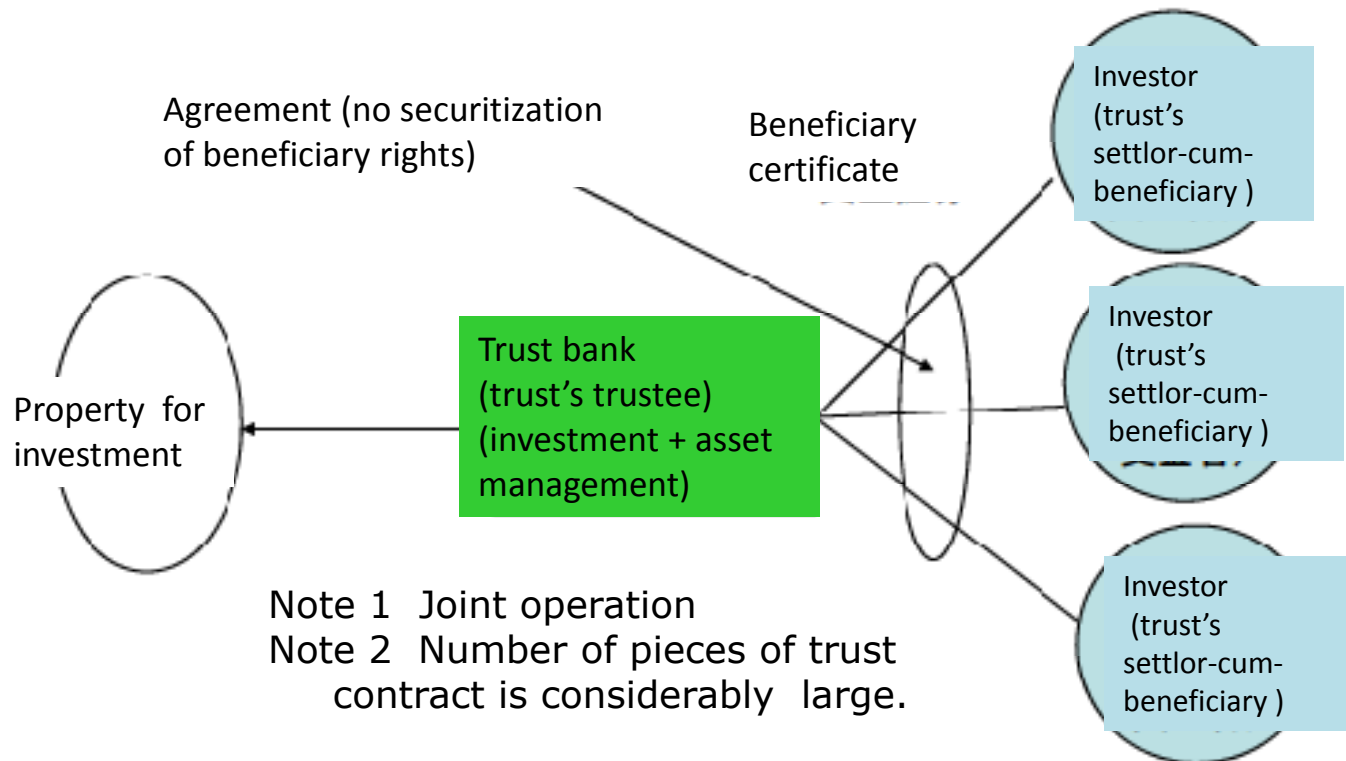
Various Laws and Institutions

Number of investors	Example	Structural stage	Sales stage: Financial Products Sales Law being applied all the time
1 party	Securities investment advisor Fund trust Individual-operation trust	None in principle Sideline Act Ditto	Financial Products Exchange Law Ditto, or Sideline Act Ditto, or Sideline Act
2 or more parties	Investment trust/investment corporation Joint-operation money trust Investment business association	Investment Trust Law Sideline Act None, or Law on limited liability investment business association	Financial Products Exchange Law Ditto, or Sideline Act Ditto

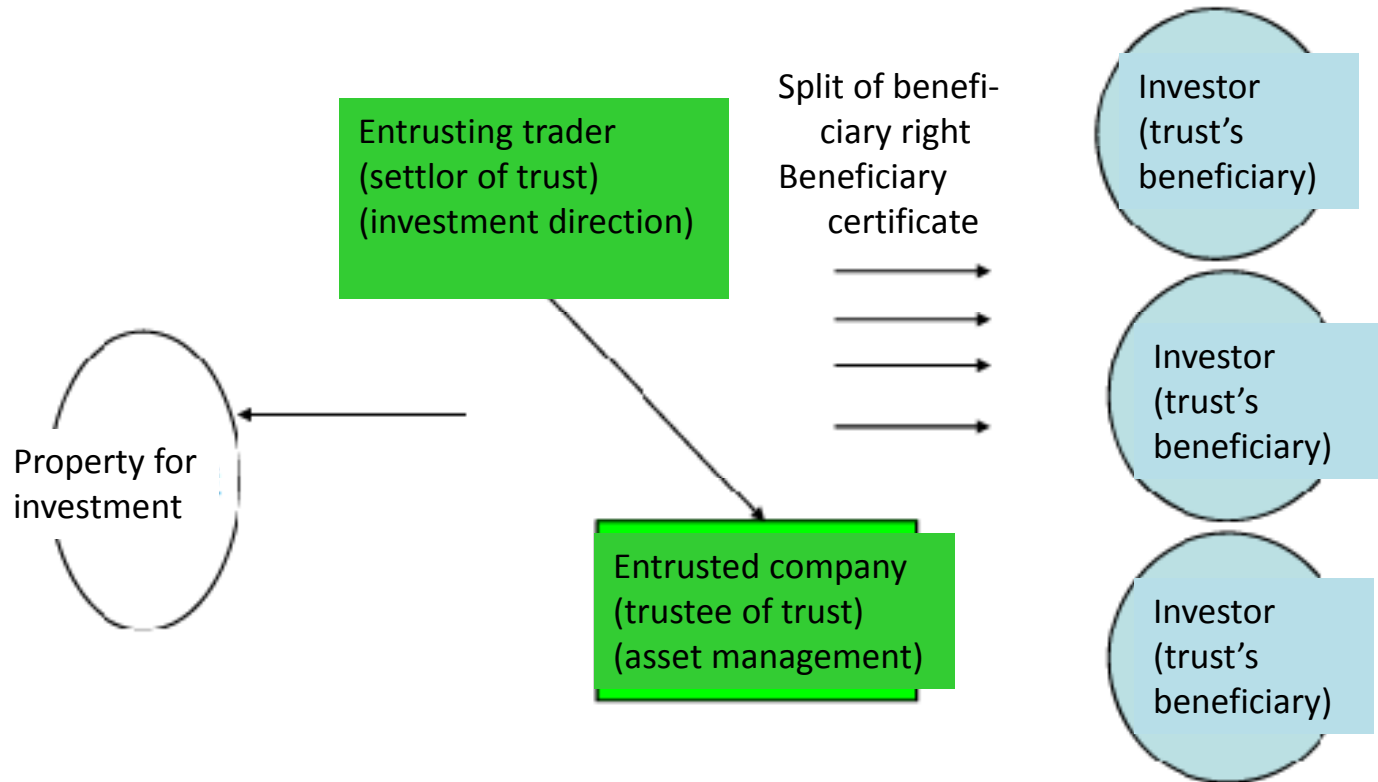
Loan Trust



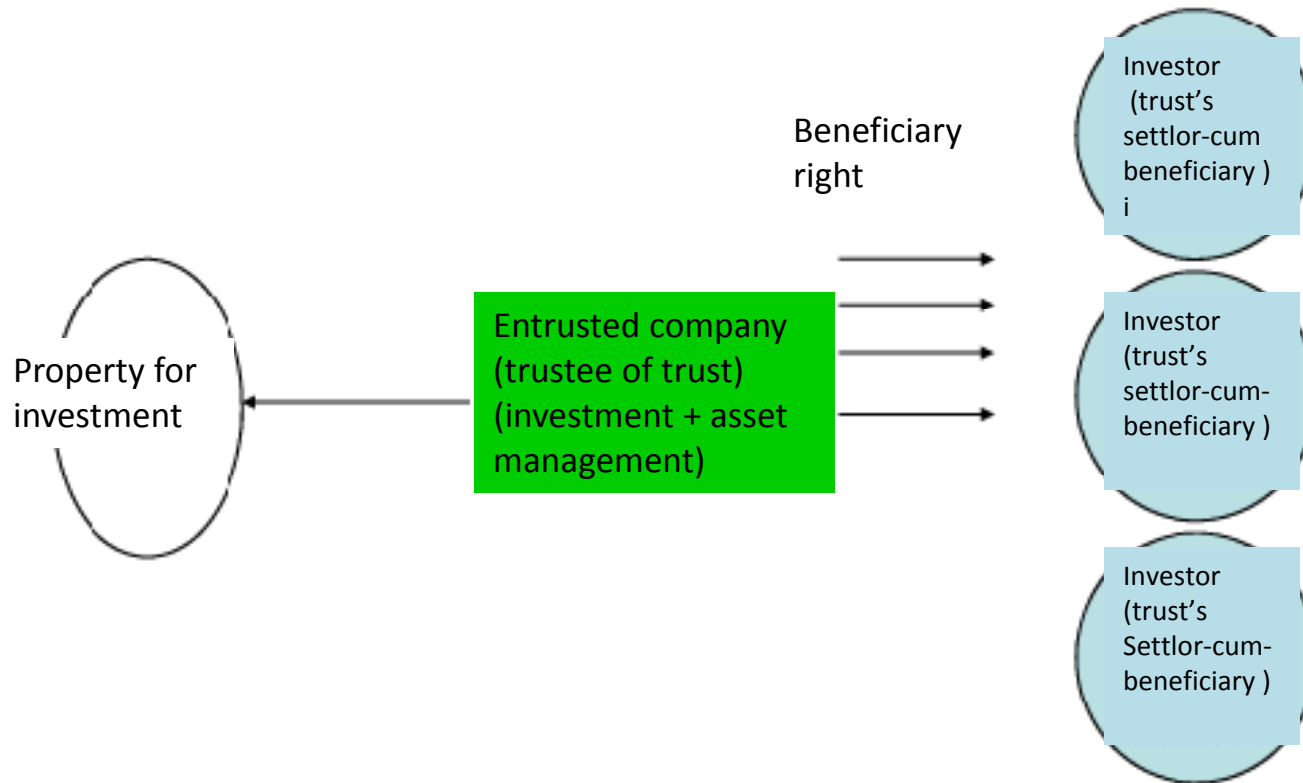
Joint-Operation Designated Money Trust



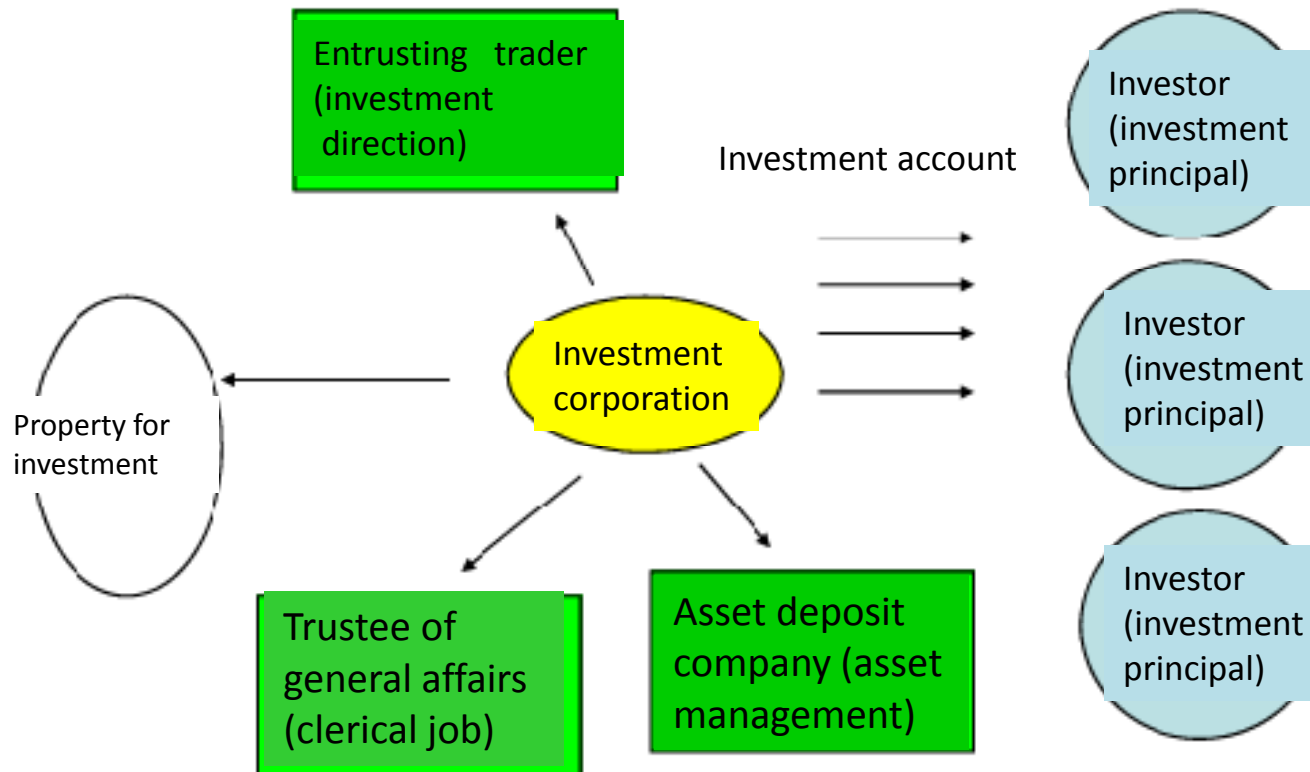
Investment Trust: Settlor-Directed Type



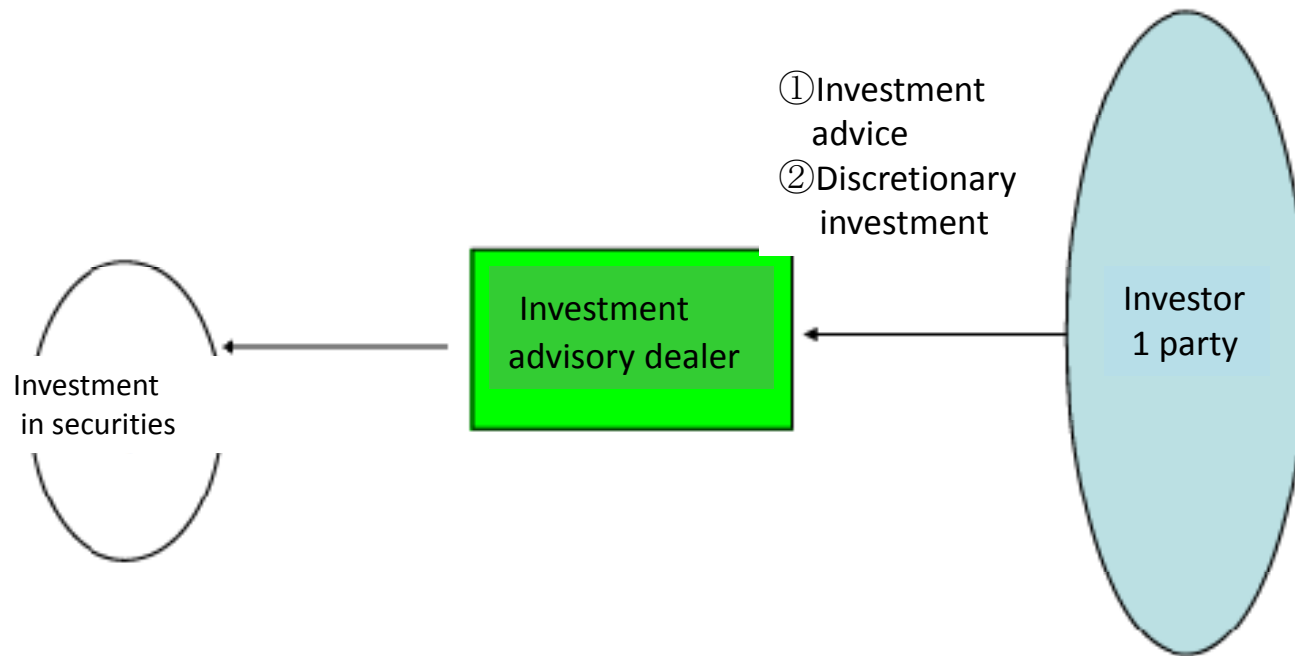
Investment Trust: Settlor-Undirected Type



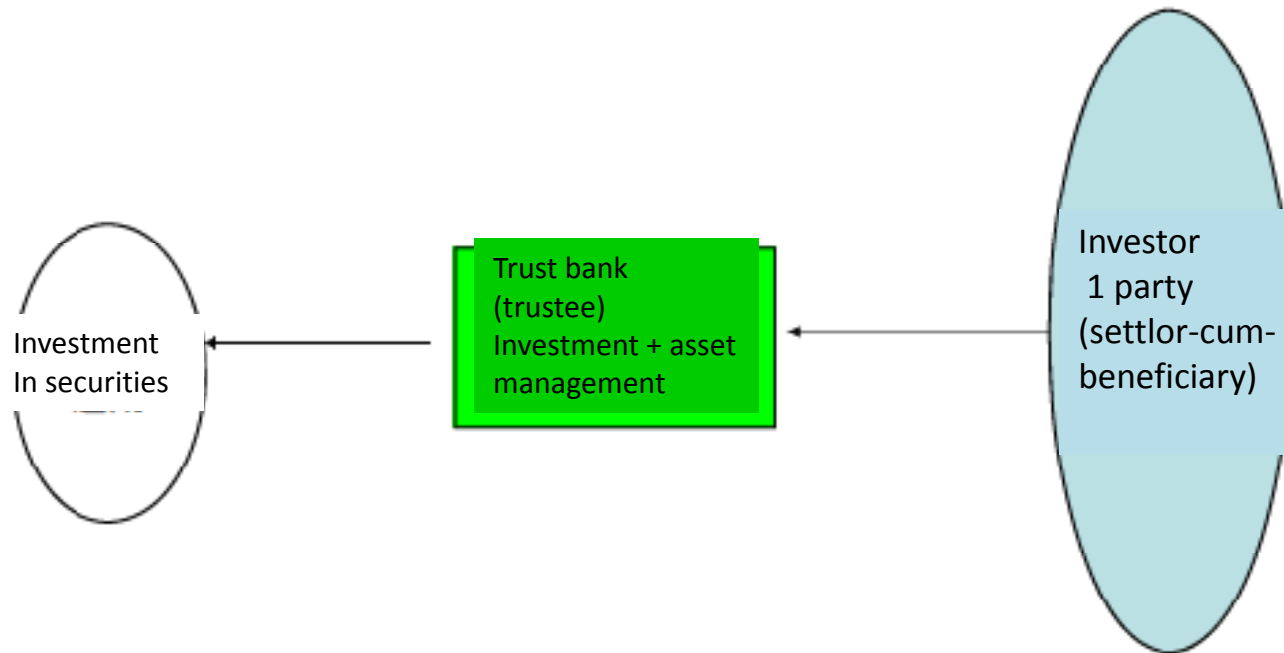
Investment Corporation



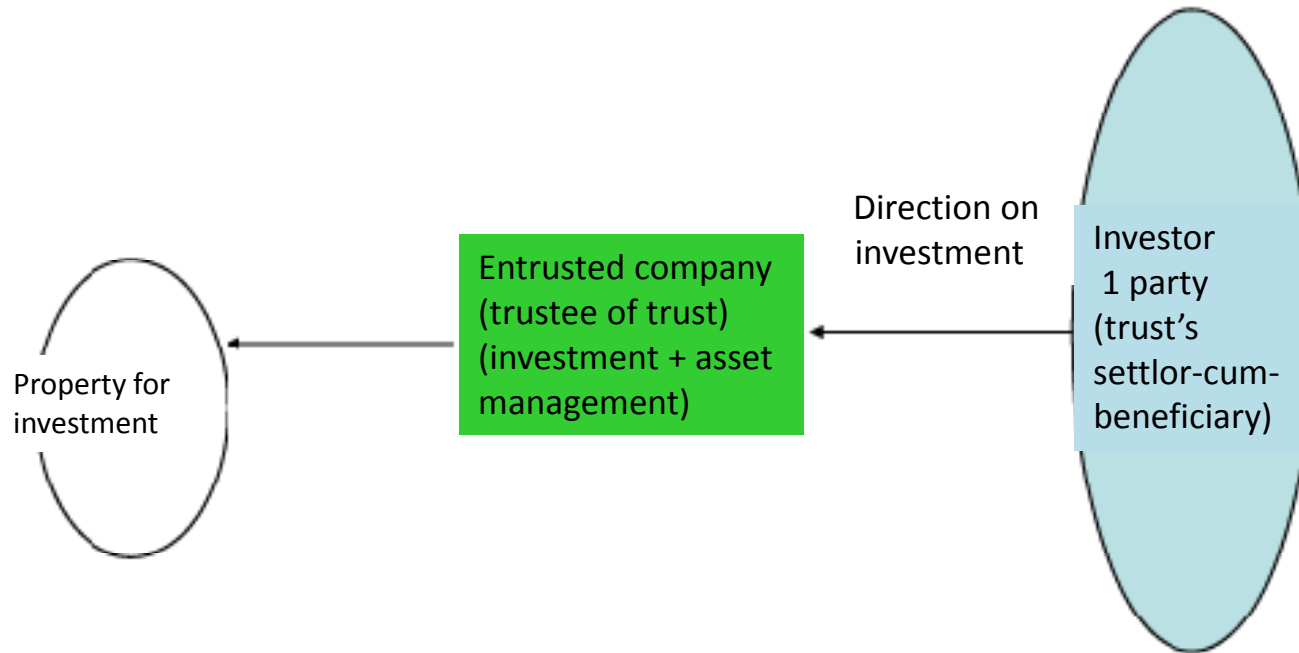
Investment Advisory Business



Fund Trust/Individual-Operation Designated Money Trust

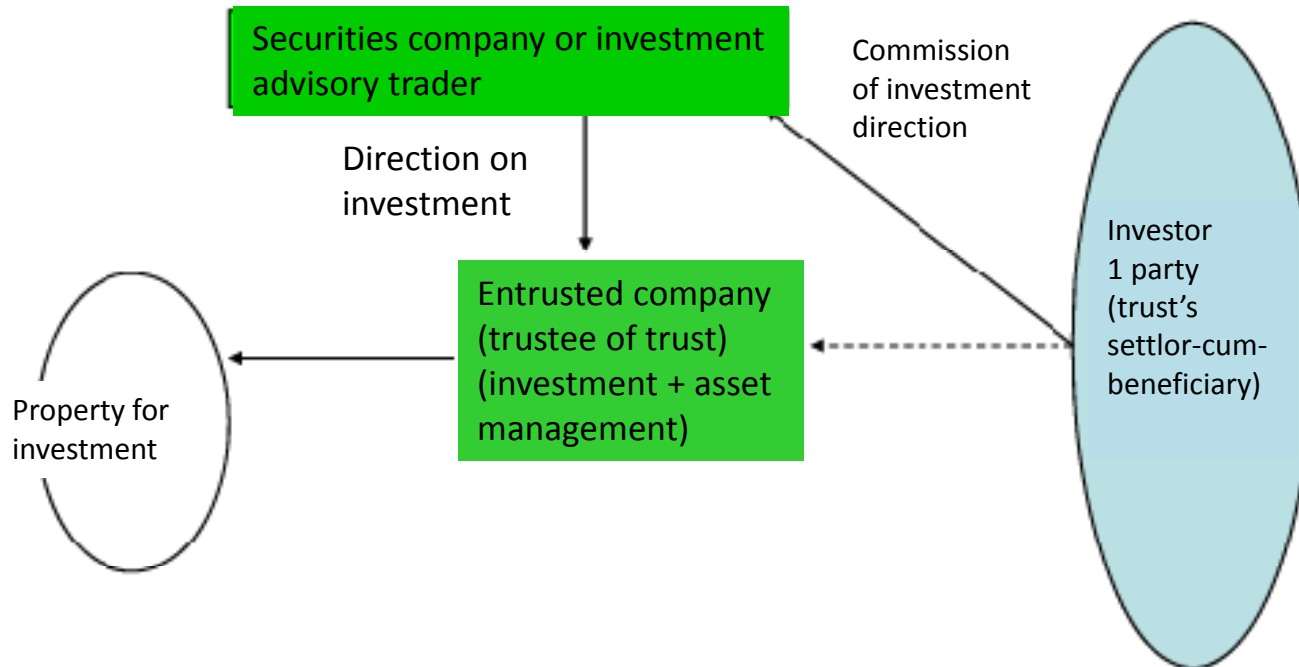


Specified Money in Trust Prototype



Specified Money in Trust

Business Specified Money in Trust



Loan Trust

○ Structure (diagram)

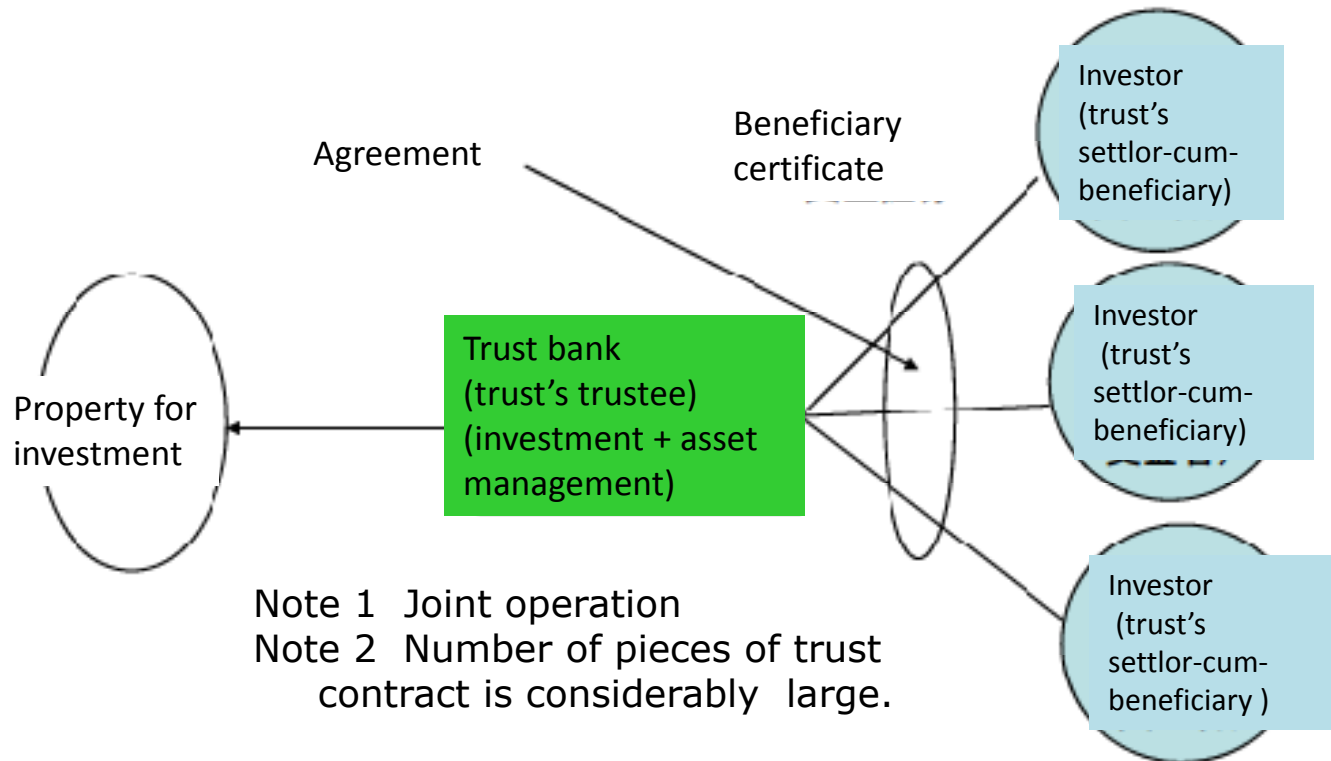
○ Special law = Loan Trust Law

○ Agreement

○ Some points at issue

- Q1: What are the number of agreements and that of trust contracts (trust deeds), respectively, in loan trust? Who are the settlor and the beneficiary under Trust Law?
- Q2: Is it not approved without legal stipulations to express beneficiary rights on securities under private statute? What about it in case of a loan trust?
- Q3: In a loan trust, what happens with the settlor's position when the beneficiary right is transferred?
- Q4: Is an agreement valid which stipulates that the trustee isn't held responsible for anything as long as the one adheres to the care duty of good administration?
- Q5: In a loan trust, are replacements of losses/interest practiced? What are projected returns? What is a special retainage system for? Why is Deposit Insurance Law applied?
- Q6: In a loan trust, in case there is some beneficiary raising an objection at the time of changing the agreement, does the trustee buy out the beneficiary right of such party with its inherent property (bank account) or property in trust (trust account)? Theoretically, which is reasonable?
- Q7: What is a "bank account loan" stipulated in the agreement? Is it not against the trustee's duty of loyalty? Is it different from an own-bank deposit in the U.S.?
- Q8: Is it not against the trustee's duty of loyalty to conduct a derivatives trading stipulated in the agreement between an inherent property and a property in trust?
- Q9: In a loan trust, is it approved to invest a property in trust in securities?

Loan Trust (repeat)



Loan Trust (sequel)

Q1: What are the number of agreements and that of trust contracts (trust deeds), respectively, in loan trust? Who are the settlor and the beneficiary under Trust Law?

●As for the definition of a loan trust, refer to Art. 2 of Loan Trust Law.

Art. 2 of Loan Trust Law: The term "loan trust" in this Law shall mean a money trust in which a trustee, based on one trust contract, jointly invests the money accepted on the basis of the trust contract which said trustee concludes with a large number of settlors mainly by means of loan or bill discounting, and shall be expressed in the form of the beneficiary right pertaining to subject trust contract.

Loan Trust (sequel)

Q2: Is it not approved without legal stipulations to express beneficiary rights on securities under private statute? What about it in case of a loan trust?

Loan Trust Law

Art. 1: The purpose of this Law is, by seeking the protection of the beneficiary, as well as by transubstantiating the beneficiary right of a loan trust to the beneficiary certificate, to make investments by general investors easy, with which to be instrumental in smooth supplies of long-term funds into fields necessary for a sound development of the nation's economy.

Art. 2: ①The term "loan trust" in this Law shall mean a money trust in which a trustee, based on one trust contract, jointly invests the money accepted on the basis of the trust contract which said trustee concludes with a large number of settlors mainly by means of loan or bill discounting, and shall be expressed in the form of the beneficiary right pertaining to subject trust contract.

②The term "beneficiary certificate" in this law shall mean a certificate to express the beneficiary right founded on a trust contract pertaining to a loan trust, which the trustee issues in accordance with the stipulations of this Law.

Art. 8: ①The transfer or execution of the beneficiary right based on a trust contract pertaining to a loan shall be practiced with a beneficiary certificate, except for expressing with a registered beneficiary certificate.

Loan Trust (sequel)

Q3: In a loan trust, what happens with the settlor's position when the beneficiary right is transferred?

- Art. 10 of Loan Trust Law. What about the case of a beneficiary certificate under Trust Law (called a beneficiary-certificate issuance trust; infra Art. 185 of Trust Law)? Refer to Art. 215 of subject Law. In addition, under Trust Law, conversion into securities (under private law) is optional (cf. Art. 185 of Trust Law).

Loan Trust Law

Art. 8: ① The transfer or execution of the beneficiary right based on a trust contract pertaining to a loan trust shall be practiced with a beneficiary certificate, except for expressing with a registered beneficiary certificate.

Art. 10: A party who acquires a beneficiary certificate, through its acquisition, shall succeed the rights and duties of a settlor involved in a trust contract pertaining to said beneficiary certificate. In this situation, the stipulations in Art. 8, para. (1) shall be applicable to the execution of a settlor's rights.

Loan Trust (sequel)

Q4: Is an agreement valid which stipulates that the trustee isn't held responsible for anything as long as the one adheres to the care duty of good administration?

● Art. 212, para. (1) of Trust Law as for the case of a beneficiary-certificate issuance trust. How will it be in a loan trust? How does an agreement for a loan trust read?

Trust Law—Art. 212: In a beneficiary-certificate issuance trust, despite the stipulations in the conditional clause of Art. 29, para. (2) the duty in the text of subject subsection cannot be relieved in accordance with the regulations on the deed of trust.

Trust Law—Art. 29: A trustee must conduct trust affairs answering the purpose of a trust. On conducting trust affairs, a trustee must act with the care of a good administrator. However, when there is a separate rule concerning the deed of trust, a trustee is to act with the care prescribed therein.

Following regulations are applicable to a loan trust: Art. 10, para. (5) of Loan Trust Law, Trust Law's Chapter 8 (excluding Art. 185, 187, para. (4) of Art. 190, Art. 192, para. (2) of Art. 195, para. (2) of Art. 200, Art. 206, 207, conditional clause in para. (1) of Art. 208, Art. 209, 210, and 212 through 215). [The rest is omitted.]

Regulations on a loan trust agreement (example)

Art. xx (Care Duty of Good Administration): This company shall not be liable for any damage from whatever cause so long as it accomplishes trust affairs answering the purpose of this contract with the care of a good administrator.

Loan Trust (sequel)

Q5: In a loan trust, are replacements of losses/interest practiced? What are projected returns? What is a special retainage system for? Why is Deposit Insurance Law applied?

- [Omission]

Loan Trust (sequel)

Q6: In a loan trust, in case there is some beneficiary raising an objection at the time of changing the agreement, does the trustee buy out the beneficiary right of such party with its inherent property (bank account) or property in trust (trust account)? Theoretically, which is reasonable?

- Art. 6, para. (6) of Loan Trust Law (Art. 11 of the same Law for the case of so-called “withdrawal before maturity”). In Trust Law, refer to Art. 103, particularly Art. 104, para. (11), (12).

Loan Trust Law

Art. 5: Trust companies and other of similar nature, upon changing a trust agreement approved in accordance with the regulations in the preceding section, shall file with the Prime Minister an application for approval specifying items intended for change and their reasons, and receive the approval.

Art. 6: ① A trustee, when approved on the change of a trust agreement by the Prime Minister in accordance with the regulations in the preceding section, shall immediately announce publicly that a rightful claimant of a beneficiary certificate, who is opposed to contents of the change or the changes, should express dissent within a certain period of time.

② The period in the preceding clause may not be shorter than one month.

③ When a rightful claimant of a beneficiary certificate does not express dissent within the period stated in the para. (1), subject rightful claimant shall be considered to have accepted such changes.

④ A rightful claimant of a beneficiary certificate who has expressed dissent may request a trustee to buy out subject beneficiary certificate at a fair price which would have been set if such changes had not taken place.

⑤ Stipulations provided in Art. 103, para. (7) and Art. 104, para. (1) through (19) shall be applied in case a request is made on the basis of the preceding clause. In this situation, necessary changes of the wording of phrases shall be provided by the Cabinet Order.

⑥ A trustee, in case a request is made in pursuance of the stipulations in the para. (4), shall buy out with its inherent property a beneficiary certificate having to do with subject request.

Art. 11: A trustee with its inherent property may buy out subject beneficiary certificate at the market value in the limited case in which a year or more has elapsed since a beneficiary certificate has been issued, except for the case stipulated in Art. 6, para. (6).

Loan Trust (sequel)

Q7: What is a “bank account loan” stipulated in the agreement? Is it not against the trustee’s duty of loyalty? Is it different from an own-bank deposit in the U.S.?

Example of an agreement stipulation: Art. xx (Investment)

- (1) This company shall manage a property in trust solely in the method of loan or bill discounting.
- (2) This company, in addition to the preceding clause, when the need for reserve requirements and such is acknowledged, may invest a property in trust in securities and trust beneficiary rights (including ones setting this company as the trustee), and in the bank account of this company (in which case, the interest is accrued at the rate shown in this company’s store).
- (3) This company, with respect to surplus money and fund during or after the expiration of the term of the trust contract, despite each of the preceding clauses, in addition to the methods prescribed in the preceding clauses, may invest in call loans or bank deposits.
- (4) This company may donate the trust money to a loan-trust investment-fund account where this is operated jointly together with the trust money pertaining to other trust contracts of the same objective.
- (5) This company may invest securities attached to a property in trust into loaning.
- (6) This company, in order to be prepared for price fluctuations of a property in trust and for exchange rate fluctuations, as well as to contribute to its efficient management, may carry out futures trading, index futures trading, option transaction, swap transaction (including forward foreign exchange contract).
- (7) This company, when deemed appropriate by this company, may carry out the transactions—required for the effective use of a trust property such as ones stated in the preceding clause, foreign exchange transactions, and dealings of securities (including commissions of these)— with this company’s bank account or companies that are in the parent-child relationship with this company.
- (8) This company may obtain money on loan by using a property in trust as security. The money borrowed shall be managed in the same methods as this money in trust.
- (9) This company, when deemed appropriate by this company, may offset a credit of loan attached to a property in trust against a debt not attached to a property in trust, or to enter into an agreement on an offset with a debtor of subject loan (including an agreement on an offset originated by a debtor).

Loan Trust (sequel)

Q8: Is it not against the trustee's duty of loyalty to conduct a derivatives trading stipulated in the agreement between an inherent property and a property in trust?

Example of an agreement stipulation: Art. xx (Management)

- (6) This company, in order to be prepared for price fluctuations of a property in trust and for exchange rate fluctuations, as well as to contribute to its efficient management, may carry out futures trading, index futures trading, option transaction, swap transaction (including forward foreign exchange contract).
- (7) This company, when deemed appropriate by this company, may carry out the transactions—required for the effective use of a trust property such as ones stated in the preceding clause, foreign exchange transactions, and dealings of securities (including commissions of these)— with this company's bank account or companies that are in the parent-child relationship with this company.

Loan Trust (sequel)

Q9: In a loan trust, is it approved to invest the trust property in securities?

Loan Trust Law

Art. 13: ①A trustee shall manage a trust property of a loan trust solely in the method of loan or bill discounting.

②A trustee, in addition to the preceding clause, when the need for reserve requirements and such is acknowledged, may make effective use of a trust property of a loan trust by means of acquiring securities.

③The stipulations in the preceding two clauses shall not apply to a trust property pertaining to a trust contract during the period of handling subject trust contract related to a loan trust, and surplus money accrued through the management of a trust property of a loan trust.