

Trust Business and Regulations on Trust Business (Part 2)

Makoto Orihara
Trust Companies Association of Japan

Introduction

I Trust Business

1. Trust business

The term "trust business" shall mean "business" to conduct "acceptance" of "trust." (Trust Business Act § 1-1)

① "Trust"

A trust is a trust based on Trust Law, i.e., contract trust, testamentary trust, self-trust, except that a self-trust, though practiced as a trade, does not constitute the subject of the trust business, which is valid only when a large number of persons are able to obtain the beneficiary right.

② "Acceptance of trust"

Viewed from the standpoint of a trustee, in the face of a settlor's manifestation of intent to set up a trust, to indicate the trustee's intention to accept this, and to ingenerate a trust relationship.

In a contract trust, while a trust is set up between a settlor and a trustee, because a trustee, not a settlor, needs to be controlled, the subject is one who conducts an "acceptance of a trust" (trustee).

③ "Business"

- To "repeatedly continue" with the "objective of the pursuit of mercenary profit"
- "The objective of the pursuit of mercenary profit": an equilibrium between income and expenditure at minimum
- "Repeatedly continue": the number of deeds and subjectivity of a transactor to be considered additionally

④ Exclusion of application (Cabinet Order § 1-2)

When a depositing of money gets conducted accompanying the conclusion of other contracts, there are cases in which a trust comes to be approved in an unanticipated form. The application of the control over these is excluded as it is deemed inappropriate.

- (a) An act to receive a monetary deposit from a client with the purpose to appropriate for expenditures of services by lawyers or law offices; an act for an appointee to receive a monetary deposit from a mandatory with the purpose to appropriate for expenditures required for trust affairs in other commission contracts
- (b) An act for a contractor in a contract agreement to receive a monetary deposit from the orderer with the purpose to appropriate for expenditures required for work done by contract
- (c) The deed provided for as corresponding to the deeds listed in (a) and (b) by the Cabinet Office Ordinance

2. Administration-type trust business (§ 2-3) —Registration

The administration-type trust business means (1) the settlor-directed-type administration trust, or (2) the preservation-act-type administrative trust, as listed below. While trust business is controlled by a licensing system in principle, a registration system is applied to the administration-type trust business since in the type (1) discretionary power is small and a high degree of capability is not required, and there is little danger of causing damage in the type (2) limited to an act of preservation.

(1) Settlor-directed-type administration trust

A trust in which the management or disposition of trust property (including acts required for achieving the purpose of the relevant disposition) is practiced only under the instruction of a settlor or party who has been entrusted with the authority of the direction by a settlor

(2) Preservation-act-type administrative trust

A trust in which only the following acts are practiced; an act of preservation, or a usage act or improvement act within the realm of not changing the characteristic of the trust property

3. Scope of business services of trust company (regulations on sideline)

(1) Trust business and other legal lines of business (§ 21-1)

A trust company may operate, in addition to trust business, trust contract agency business, trust-beneficiary-right selling business, and property management business (other legal lines of business).

The other legal lines of business are not under the regulation on the sideline since they are approved to be relevant to trust business practiced by a trust company, and are considered to have little effect on the operation of a trust company.

①Trust contract agency business

A business to practice representation (limited to the situation representing a trust company or a foreign trust company) or intermediation of the conclusion of a trust contract (except for a case in which a trustee of the trust based on the relevant contract is deemed to be an issuer (issuer as in Article 2, paragraph (5) of Financial Instruments and Exchange Law) of the relevant beneficiary right (including a bill or document indicating the relevant beneficiary right)

②Trust-beneficiary-right selling business

A business to practice selling of beneficiary rights of trust (beneficiary certificate and imputed securities) or its representation or intermediation

③Property management business

Management business of property is restricted to the same kind of property as stated in business and service documents of a trust company, and to the same method as the management method a trust company practices for trust property.

(2) Sideline business (§21-2 of Trust Business Act)

A trust company may, with the approval of the Prime Minister, operate a business which is related to trust business and in no danger of posing a problem for running trust business appropriately and surely.

①Sideline business's incidental nature of

②Sideline business's relevancy

II Control over activities

1. Commission of trust business

While the matters on the consignment of trust business (making it a discretionary provision, deleting the identical responsibility with that of a consignee's trustee) have been largely relaxed in Trust Law, when viewed from a client standpoint, a consignee and a trustee appear to be the same, and there is a gap in amount of information and bargaining power between a client and a consignee/trustee, and the Law alone might be inadequate to protect the beneficiary. Thus the regulation pertaining to the trust business commission has been established.

(1) Situation the commission of trust business is possible (§ 22-1 · 3)

①Requisites for commission

② Not applicable in case of preservation/ improvement acts

③ Assistance act

(2) Responsibility of the consignee when commissioned (§ 22-2 · 3)

- ① Consignee's responsibility
- ② Consignee's responsibility not applicable

(3) Responsibility of the trust company when commissioned (§ 23)

- ① Trust company's responsibility
- ② Trust company's responsibility not applicable

2. Rules to activities pertaining to the acceptance of trust (§ 24)

As to the acceptance of trust by a trust company, the rules to the acts are stipulated so as to provide a settlor with proper information, to prevent a conclusion of a trust contract involving excessive risks, and to secure appropriate operation of a trust company's business.

(1) Prohibited acts (Trust Business Act § 24-1)

- ① False notice
- ② Provision of an assertive judgment
- ③ Provision of a special profit
- ④ Replacement of losses and such
- ⑤ Other acts that fall short of the protection of a settlor as prescribed by the Cabinet Office Ordinance
 - (a) Ban on the provision of mistaken matters regarding important matters
 - (b) Ban on back finance
 - (c) Ban on acts violating the law

(2) Principle of compatibility(§ 24-2)

Balance between a settlor's attribute (knowledge or the like) and the content of trust

(3) Corresponding application of Financial Instruments and Exchange Law pertaining to the specified trust contract (§ 24-2)

As to a trust with strong investment disposition, in view of the spirit of regulatory crosscutting as intended by Financial Instruments and Exchange Law, the regulatory equivalence is secured by the corresponding application of Financial Instruments and Exchange Law in Trust Business Act by means of naming a particular trust contract—having possibility of falling below par value because of market risks— a "specified trust contract."

- ① Specified trust contract (Rule on Business § Act 30-2)

- ②Corresponding application of control over activities pertaining to sales/inducement
 - (a)Control over public notices (§ 37)
 - (b)Duty to deliver the document prior to the conclusion of an agreement (3-1 · 2 of § 37)
 - (c)Cancellation by the document: cooling off (§ 37-6)
 - (d)Prohibited acts: ban on an uninvited inducement, duty to confirm an intention pertaining to a solicited trust, ban on re-inducement, commission matters in the Cabinet Office Ordinance (§ 38)
 - (e)Ban on compensation for loss (39)
 - (f)Proper treatment of information client (§ 40—2)
- ③Duty of disclosure and representation to specified investors (§ 34, 34-2)
- ④No corresponding application
 - (a)Matters that overlap with the control over activities regulated in Trust Business Act (ban on false disclosure; § 38—1), principle on compatibility (§ 40—1)
 - (b)Matters that do not fall under the control over activities pertaining to investment disposition (duty of loyalty to clients; § 36), the duty to specify dealing terms in advance (§ 37-2)
 - (c) Matters inherent to the business of financial instruments and exchange (ban on the management of bonds; § 36-4)

(4) Explanation about contents of a trust contract (§ 25)

(5) Issuance of the document at the time of concluding a trust contract (Business Act § 26)

①Issuance/delivery of the document

②Desuetude of the document issuance

(6) Issuance of a status report on property in trust (Business Act § 27)

① Issuance of the report

② Desuetude of the document issuance

3. Obligations of the trust company

- Nature of duties
- Scope of duties

(1) Care duty of good administration (§ 28-2)

- ① Scope to duty
- ② Degree of duty

(2) Duty of impartiality

(3) Duty of loyalty (§ 28-1)

(4) Duty of system preparation such as the separate management system (§ 28-3)

① Preparation of the system such as the separate management system(Rule § 39)

(a) To manage in a state allowing to identify each beneficiary by means of separating places to manage trust property and inherent property

(b) To prepare a system for a consignee of the management of trust property to secure the management by means of separating trust property and property belonging to the said consignee

(c) To draw up and preserve for a prescribed period the trust account ledger and general ledger in order to clarify the processing and calculation of trust business

②Preparation of other systems (Rule § 40)

Development of systems to prevent causation of losses on trust property, and impair of credibility of trust business

(a) To secure human constitution capable to appropriately carry out internal control activities

(b) To improve inter-company rules

(c) To conduct a system preparation like making those responsible for internal control activities independent of a section that operates trust property

4. Rules to activities pertaining to the property in trust

(1) Prohibited acts

①Transaction under the condition to cause damage to the property in trust

② Unnecessary transaction

③ Information-use transaction

To exclude the following acts:

i) An act that cannot be approved as solely aiming at gaining profits for oneself or the third party by newly conducting a transaction with the other party in dealing

- ii) Usage of the information that can be known to the third party
- iii) To act by presenting the important information to a beneficiary and obtaining the consent of said beneficiary
- iv) A transaction that is approved not to cause damage to the property in trust
- ④ Other acts which might cause damage to the property in trust, or to lose credibility of trust business
- (2) Ban on the act in conflict of interest (§ 29-2)
 - ① Prohibited acts
 - (a) Self transaction
 - (b) Transaction between the trust properties
 - (c) Transaction as proxy for both sides
 - ② Exceptions for the prohibited acts
 - (a) Transactions by the direction of a settlor and a beneficiary alone
 - (b) Transactions under a fair terms of business
 - (i) Transactions in the market for listed securities and bonds, and ones of bonds and securities based on published prices
 - (ii) Derivatives trading in market , transactions in financial market
 - (iii) Transactions of realties grounded in appraisals
 - (iv) Transactions that are not disadvantageous to a beneficiary as compared to ordinary business terms which come to be materialize under the same kind same quantity, and same condition
 - ③ Transactions to be conducted with the consent of a beneficiary by disclosing important facts for an individual transaction
 - ④ Transactions under an approval of the Director of Financial Service Agency
- (3) Obligation to issue a document in case the act in conflict of interest was conducted (§ 29-3)

III Special Cases of Self-Trust

Self-trust newly came to be approved in the full-fledged revision of Trust Law in December, 2006, and in response to this, "Special Cases as to Self-Trust" (§ 52-2) was added as a part of "Section 6: Special Cases as to Special Trust in Chapter 2's Trust Company" in Trust Business Act.

1. Significance of self-trust

(1) Features of self-trust

- A settlor and a trustee are one and the same.
- A sideline business is assumed.

(2) Introduction of the concept of a “plurality of parties” =50-person regulation

2. Regulation on entry

(1) Registration=50-person regulation (Business Act § 50-2-1 the text, Cabinet Order on Business Act § 15-2)

- ① When the number of beneficiaries becomes 50 or more for one time of self-trust (Cabinet Order on Business Act § 15-2-2-1)
- ② When the number of virtual beneficiaries becomes 50 or more by letting the so-called structured investment vehicle involved (Cabinet Order on Business Act § 15-2-2-2)
- ③ When the total number of beneficiaries exceeds 50 by repeating self-trust (Cabinet Order on Business Act § 15-2-2-3)
- ④ When, by issuing numerous units of beneficiary right, the total number of units becomes 50 or more (Cabinet Order on Business Act § 15-2-2-4)

(2) Registration requisites (Business Act 50-2-6)

① Control on organizational (Business Act 50-2-6-1, -4 to 6, -8))

② Control on property (Business Act 50-2-6-2, -3))

Capital, net worth (¥30 million each), trade deposit money (¥10 million)

③ Control on sideline (Business Act 50-2-6-7)

Soundness of sideline business

(3) Exemption from application of registration (proviso of Business Act 50-2-1, Cabinet Order on Business Act §15-3)

- ① When Japan Finance Corporation for Small Business practices self-trust by obtaining the authorization for each scheme (Cabinet Order on Business Act §15-3—from 1 to 3))
- ② When a party engaged in collecting specified pecuniary claim puts subject money in self-trust (Cabinet Order on Business Act §15-3—4)
- ③ When an appointee of a delegation contract and a contractor of a contract agreement put the money which they manage in self-trust (Cabinet Order on Business Act §15-3—5 and 6)
- ④ When a party who receives money on someone’s behalf puts the money in self-trust (Cabinet Order on Business Act §15-3—7)
- ⑤ When a leaseholder under a lease contract puts the money managed by the said party in self-trust (Cabinet Order on Business Act §15-3—8, Rule on Business Act §51-10)

3. Control over acts

(1) Duty of the trustee of self-trust (Business Act 50-2-12)

A party who has accepted the registration of self-trust is regarded as a trust company (or an administration-type trust company), to whom the regulations pertaining to the trust company shall be applied.

① Nonapplication of the regulation pertaining to the settlor protection

Rules to activity of the acceptance of trust (Business Act §24), the duty to explain contents of a trust contract (Business Act §25), the duty to issue documents at the time of concluding a trust contract (Business Act §26)

② Nonapplication of the regulations that are to become excessive rules

Trade name regulation (Business Act §14), the restriction on holding more than one office by directors (Business Act §16), the restriction on main shareholders (Business Act §17), an accounting period (Business Act §32)

(2) Third party's checkup on trust property (Business Act §50-2-10)

① Duty of checkup by the third party

When the number of beneficiaries is 50 or more

③ Checkup party (Cabinet Order on Business Act §15-5)

Attorney, chartered accountant, licensed tax accountant, real estate appraiser, etc.

③ Matters for checkup and report (Rule on Business Act §51-7)

(a) State of affairs as to properties that belong to trust properties in accord with such kinds as securities and bonds, immovable] properties, movable properties, pecuniary claims, and intellectual property rights

(b) The amount of money equivalent to the value of properties that belong to trust property at the time of setting up self-trust

IV Financial Instruments and Exchange Law and Trust

1. Regulations on securities and bonds under Financial Instruments and Exchange Law

(1) Control on business and one on act

① Control on business

② Control on act

(2) Control on disclosure

① Control on issuance disclosure

② Control on continuous disclosure

(3) Control on transaction

2. Trust beneficiary right and Financial Instruments and Exchange Law

(1) To add the beneficiary certificate of beneficiary-certificate issuance trust to “securities and bonds” under Financial Instruments and Exchange Law

(2) To convert trust beneficiary rights into imputed securities under Financial Instruments and Exchange Law

3. Effect on trust business accompanying securitization of trust beneficiary rights

(1) Trust company’s acceptance of trust

① Acceptance of general trusts = Self-subscription for trust beneficiary right
→ Exemption from application

② Acceptance of specified trust = Corresponding application of Financial Instruments and Exchange Law under Trust Business Act

(2) Trust agency’s representation or intermediation of the conclusion of a trust contract = Handling of the subscription for securities and bonds, and a private placement

(3) Trust-beneficiary-right selling business = Buying and selling, or representation, or intermediation, of securities and bonds

Data: Trust Business Act (Excerpts) — [*English translation omitted*]

【Bibliography】

Takuya Koide, *Trust Business Act: Article-By-Article Commentary*, Seibunsha, Jun. 2008

