

MODERN USE OF TRUSTS IN COMMERCIAL TRANSACTIONS: POSSIBLE REFORMS IN THE SRI LANKAN TRUSTS LAW

M.P.S. KAUSHANI PATHIRANA

BACKGROUND

A trust involves a relationship wherein a person (the settlor) transfers property (movable or immovable) to another (the trustee) for its management and control for the benefit of someone else (the beneficiary). Most rules regarding trusts have been created based on aged old principles of equity and English cases. Trusts Law of Sri Lanka is contained in both statute and case law. The main legislation is the Trusts Ordinance, No.09 of 1917.

The concept of trust has spread into the commercial law and company law in commercial transactions. This paper identifies these recent developments in the trusts law in commercial transactions and suggests reforms for Sri Lankan trusts regime.

The Unit trust is the popular mode of trusts used in commercial transactions in many countries. A Unit trust is a trust where the unit holders can possess certain shares (units) and can direct the trustee to pay money to them according to the number of units. It makes a path for the general public to invest their money without all the typical risks. In Singapore, Business trusts have been used as innovative investment structures in international trade market. The business trust is designed to give investors direct exposure through the purchase of units which are tradable in the Singapore Stock Exchange. Especially it should be mentioned that business trusts have various advantages in capital intensive sectors such as shipping and infrastructure in Singapore. This is governed under the Singapore Business Trusts Act 2004.

Thailand has introduced ‘The Trust for Transactions in Capital Market Act 2007’ as one of their modern developments in trusts law. The Securities and Exchange Commission of Thailand has the power and duty to formulate policies to promote, develop and supervise trusts for transactions in the capital market. The Act specifically identifies the transactions which can be use the trusts relationships.⁴⁷

The trust can be used by an employer to arrange a pension scheme for his employees. The benefit of using the trust structure for a pension fund is that if the employer comes in to financial difficulty there is a separation of money of pension fund. In a recent case⁴⁸ of United Kingdom demonstrates that an employer who has arranged a pension scheme by using the trust was obliged to work in good faith for his employees.

The trust also can be used to taking security in relation to ordinary loan contracts. When the borrower receives the loan money, he can use it as his own money to any purpose. Only a well drafted loan contract will look after the lender against such risks. Therefore the lender can use the trust for the loan contract to direct the loan money for a specific purpose. If the money is used to another purpose, the lender has a right to reverse the money. This type of trusts has been introduced in United Kingdom named Quistclose trusts⁴⁹.

The trust also can be used as a tax planning method. Some scholars state that where a settlor is in a high tax jurisdiction transfers properties to a trustee in a low tax jurisdiction, the settlor can earn some substantial tax advantages⁵⁰. Therefore this is an apparently easy way of avoiding taxation. But it should not be a selfish tax planning. However the anti-tax avoidance measures are enforced by tax authorities in most countries as a preventing method.

The application of Constructive trusts for the liability of directors of a company is another emerging trend of trusts law. If a director has made a personal profit or gain from the company's assets, constructive trust would be the better remedy on behalf of the company.⁵¹ Also the trust can use as a method to protect a company from a hostile takeover. If the original owner of the company does not want any single person to acquire a controlling shareholding of the company, can put some sufficient number of shares in the trust.

Trusts have been developed as the 'International Trusts'. This means the trusts law can apply when the parties or the assets of the trust are situated in different jurisdictions. Hague Convention on the Law Applicable to Trusts and on Their Recognition came into force in 1992 and seeks to harmonize the private international laws relating to trusts. This convention aims to resolve many of the difficulties which have been arisen from trusts law conflicts and establish common provisions on the trusts law. But unfortunately many countries have not joined and ratified yet.

Methodology

The purpose of this paper is to identify the modern use of trusts in commercial transactions and suggest reforms for Sri Lankan Trusts Law in comparison with Laws relating to Trusts of United Kingdom, United States, Singapore, Thailand, New Zealand, Scotland and Ireland. This is based on library and Internet research of statutes, cases, commission reports, journals and articles.

CONCLUSION

It should be mentioned that the trusts laws of most countries have been reformed in the light of commercial transactions and other current developments. The primary trusts legislation in United Kingdom has been reformed by many of the recent legislation. The Irish Law Reform Commission is reviewing trusts legislation and made recommendations and presented a draft bill for a modern trusts code in 2008.⁵² The Scottish Law Commission made proposals for their traditional Trusts Acts 1921 and 1961.⁵³ In United States, the National Conference of Commissioners on Uniform State Laws produced a Uniform Trust Code in 2000. It was last amended in 2005.⁵⁴ New Zealand also has traditional Trustee Act in 1956 and made proposals to reform the trust law.⁵⁵

Today the trusts law is approached into many emerging criteria such as commercial transactions and company issues. In this context this is the most suitable time to amend the Trusts Ordinance 1917 of Sri Lanka as well. The extent and the language of the ordinance appear irrelevant to modern day legal practice. It should be formulated in a contemporary and understandable structure in favour of law students and legal practitioners.

** LL.B (Hons), Attorney-at-Law, Temporary Tutor, Department of Private and Comparative Law, Faculty of Law, University of Colombo.*

- 47 Section No.04 of The Trusts for Transactions in Capital Market Act 2007 of Thailand.
- 48 *Imperial Group Pension Trust v. Imperial Tobacco Ltd* (1991) 1 WLR 589
- 49 Hudson A., *Commercial trusts law, study guide*, University of London Press 2005, pg.09
- 50 www.trust-world.net/index.php?option=com_content&view=article&id=94:intrototrusts&catid=11:generalconsumer&itemid=20
- 51 *Sinclair Investments (UK) Ltd v Versailles Trade Finance Ltd* 2010 EWHC 1614] (Ch)
- 52 *Irish Law Reform Commission Trust law: General Proposals* (Dublin, 2008) at 1.
- 53 *Scottish Law Commission, Discussion Paper on the Nature and Constitution of Trusts* (Edinburgh 2006)
- 54 STEP Journal website —Jurisdiction Summaries – United States||<www.stepjournal.org>.
- 55 *Review of Trust Law in New Zealand: Introductory Issues Paper*, November 2010