

What your Chinese private clients want to know and why

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China is a huge potential market but winning Chinese clients' trust is not easy. All private clients are different and all families are different, with varying circumstances, backgrounds and motivations. Chinese culture is not monolithic and your clients will have differing expectations from province to province and city to city.

Nevertheless, from our experience there are a number of questions that are frequently asked by Chinese clients which are often the product of specific cultural and social factors. Private wealth advisors should be aware of these questions, not only to ensure they have answers prepared, but also as a key to understanding the culture and background of their client. We advise the ACE approach:

- Action – have a plan to guide the family through the whole process, step by step
- Communication – pay attention to the family's verbal and, importantly, non-verbal communication
- Empathy – understand the family's thoughts and concerns

The questions we have chosen below are simply the ones that come up most frequently and our comments are a high level overview with general principles, and not tailored to a particular case or situation.

What is a trust and how can it help me?

Chinese law does not have an equivalent of the offshore trust concept, so not all clients will be familiar with the central idea of a trust, namely that it entails handing over the legal ownership of their assets (which are often of significant value) to a third party. It's important that advisors ensure that their client is truly comfortable with the trust concept, both in theory and in practice. If they are not, then this is an opportunity to explore a different form of structure with the client.

In other instances where the client does have familiarity with the offshore trust concept, they will likely have been told lots of different things by lots of different parties. It's important for advisors to provide reassurance and clarity, and also to ensure they fully understand what their client's objectives are so advice can be best tailored to the client's needs.

Which jurisdiction should I settle the trust in?

Your client may well have been approached by a number of advisors proposing various jurisdictions and structures and propagating various - at times conflicting - messages. Trust advisory is not regulated in China or Hong Kong, meaning anyone can advise on setting up a trust, even if they are not competent.

It's important to bear this context in mind and your client's understandable desire for clarity in the face of it, while at the same time explaining that there is no such thing as "the best jurisdiction". The trust law in each jurisdiction is largely similar but subtly different. Those subtle differences may or may not be material. Again what's key for advisors is to really get to the heart of what the family wants to achieve and their particular circumstances, and then overlay this on the trust law of the various jurisdictions to find the best fit, bearing in mind that this may mean selecting a combination of jurisdictions and structures.

How do I choose a trustee?

Chinese families ask this question for similar reasons as those highlighted above – it is likely that they have been approached by a number of trustees, and the client may be unsure of how to choose between the large number of options available.

It's important for advisors to help their client define the criteria by which they judge the suitability of different trustees. Cost is clearly a factor, but it shouldn't be the overarching one. It's often an important role on the part of the advisor to try and disabuse clients from thinking that price overrides all other considerations, and get them to think more in terms of the value the trustee provides.

Much like you would first choose what you would like to eat and then choose the restaurant, choice of trustee should come after a decision has been made on which jurisdiction to settle the trust in. It's important to highlight to clients that the location of the trustee may not be the same as the jurisdiction of the trust, and to reassure them that this is perfectly acceptable so long as the trustee is competent to manage a trust not governed by their local law. Notable exceptions to this are BVI VISTA trusts and Cayman STAR trusts, which require locally licensed trustees.

It is equally important to speak with your client about the human side too. A trust is fundamentally about human relationships - virtual meetings are acceptable, but to build rapport with and confidence in the trustee, your client needs real-life meetings with them too.

Questions for advisors and their clients to consider in this respect include which time-zone the trustee is based in, whether the trustee is knowledgeable about Chinese culture, and whether the trustee can speak with the client in their own language. Miscommunication and misunderstandings can easily happen if this isn't the case.

Deep background research on the trustee is key, including meeting trust officers who will be managing the trust on a day-to-day basis. Are they experienced in managing trusts of Chinese families? Are they rated by their peers and clients?

What are the rights and duties of a settlor, trustee, beneficiaries and protector in a trust structure?

This question again is about the fundamental nature of what a trust is. The client needs to be aware of the two fundamental duties of a settlor: to transfer ownership of their assets to the trustee, and to have a genuine intention to create a trust on the terms of the trust document. Intention is absolutely crucial – without it, there is no trust.

With regards to the rights and responsibilities of the trustee, it is important to emphasise to the client that the trustee will be the legal owner of the trust assets and is entitled to deal with those assets in line with the terms of the trust document and their fiduciary duty to the beneficiaries of the trust.

Beneficiaries have limited obligations but an extensive list of rights, one of the more vexed ones being their right to information about the trust, which is established by a mixture of common law, statute and the terms of the trust deed. Statutory limitations on beneficiaries' right to information vary across jurisdictions and there is a plethora of case law in this area.

The role of the protector is the least well defined, with relatively limited statutory recognition and case law. The fundamental role which case law has endorsed is that the role of a protector is to protect the interests of beneficiaries and, absent of different provisions in the trust deed, their role is of a fiduciary. Many settlors view protectors as having the role of protecting the settlor's interests and not the beneficiaries', so if this is the case for your client, ensure that you impress on them that the protector is there to protect the beneficiaries, not any other parties.

Who should play the above roles and how do they interact with each other?

The key thing here is to ensure the client understands the essential requirement of avoiding conflicts of interest. The parties should be genuinely independent – that doesn't necessarily mean that they need to be unrelated, but they should take their roles seriously and discharge them in accordance with the law and not just act as a cipher of one of the other parties.

The question of interaction between the parties is key. In our experience, clients spend a huge

amount of time thinking about who should take these roles and less time on the equally important question of how these individuals will interact with each other.

While there is not a great deal of choice on who the settlor is, one thing we do come across fairly frequently is the desire for clients not to appear to be the settlor, by having a third party be named as settlor in the trust document or by having a corporate settlor. Great care should be taken in these circumstances to ensure that the settlor is the party providing the assets of the trust.

Trust between the settlor and the trustee, and indeed the beneficiaries and the trustee, is absolutely fundamental in order for a trust structure to succeed. Do not presume your client's confidence. Discuss with them whether the trustee will need particular expertise, for example in investing high risk assets or in dealing with difficult interpersonal relationships between beneficiaries.

In terms of who the beneficiaries should be, it's important to encourage the client to think of this both positively and negatively i.e. who do I want and who do I not want as beneficiary, and to be expansive in their considerations, including for example the position of adopted children, surrogate children, children born outside of marriage, second, third and legally unrecognised families, same sex partners, civil partners and cohabitees.

Perhaps in some ways the most difficult role to fill successfully is the protector, as they need to have the confidence of the settlor, trustee and beneficiaries.

What are the pros and cons of allowing the settlor of a trust to reserve powers to themselves?

As an advisor, you need to be aware of why your client wants to reserve powers - most of the time it's because they simply don't trust the trustee. In the context of Chinese settlors, this mistrust can stem from myriad issues, perhaps it's a reservation around not speaking the same language or perhaps the settlor isn't sufficiently familiar with the offshore trust concept.

Reserved powers can provide a degree of comfort to the settlor, especially if they have no idea how an offshore trust operates, but they aren't a panacea and may end up jeopardising the robustness of the trust.

Advisors need to drill down to the reason why their client wishes to reserve particular powers and ensure their client is made aware of the legal consequences of doing so. Always have a person play the role of "devil's advocate" to challenge the validity and robustness of a trust where the powers are reserved as the client wishes – and then only reserve the powers where you "win" in the face of these challenges.

How can the powers of the trustee be restricted?

Your client may not be aware that a trustee's powers are already restricted under law, so make sure that you have advised them of this. If they are aware of the limitations on the powers of the trustee and wish to restrict them further, then this may be because they don't trust the trustee. In which case there is more fundamental ground work that you need to do to as an advisor.

If they do trust the trustee, the client may only wish to restrict the trustee's powers in specific areas, where they feel the trustee doesn't have the requisite specialised knowledge or the right background.

The question of scale and concentration is key here. Are all those restricted powers intended to be reserved to one particular party? This question can sometimes show that the settlor is intending to hold too many powers, in a way that impedes the trustee discharging their duty, and threatens the robustness of the trust.

How do I terminate a trust?

Chinese people are smart investors, and often want to know how they can exit an arrangement long before they would think about investing in it. Your client will often want assurance that, should the trust not turn out how they wish, they can exit with the trust assets still intact.

There are various ways to terminate a trust. For example, a revocable trust can be set up, where the settlor has the power to revoke the trust at any time with all the trust assets returning to the settlor. It's also possible to shorten the trust period by appointing a fixed date so the trust only runs to a particular date. The trustee may also distribute the whole trust assets to beneficiaries. These are ways that you can reassure your client that settling assets into a trust is not a one way road.

What is a PTC and what are the pros and cons of having one as trustee?

Again it's important to understand why your client is asking this question. Generally speaking, Private Trust Companies are not best suited to small or simple structures, or where families have no real experience of trust structures. A PTC, generally speaking, is most suitable for holding specific assets/high risk assets or investments which require very specific knowledge, for example a family company in a niche area of business.

Ensure that your client doesn't just want a PTC because they think it will be much cheaper than engaging a professional trustee, as this indicates that they do not appreciate what it is. Likewise, ensure your client doesn't want a PTC to avoid scrutiny or outsiders in the trust arrangement, as outsiders will need to be involved in a PTC.

How do a trust deed, settlor's letter of wishes and a family constitution work together as part of family governance and

succession?

Family is important in Chinese culture, and succession is about more than just passing on assets - it's also about passing on family values, the family legacy, and keeping the family together. Wealthy Chinese families often face similar challenges in this regard, for example the next generation may have been largely or exclusively educated overseas, which could lead to an intergenerational value and culture clash.

Some family values could be reflected in a letter of wishes or in the trust deed, but the main function of a trust is pass on assets. A family constitution is better suited to pass on and inform more intangible things like legacy, wellbeing and family unity. It's important that a family constitution is flexible enough to allow the family to adapt while providing sufficient certainty to the family knowing what has been agreed on.

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