Fiduciary Alternatives to Special Representative Actions in Civil Securities Disputes

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Abstract. As an institutional innovation, the special representative litigation arising from securities civil disputes is of great value for protecting the interests of small and medium investors, which improves the efficiency of class actions and promotes judicial justice. However, this seemingly perfect system has had difficulty in being widely used in China recently. Trusts are a widely applicable, flexible and efficient legal tool that is widely used in the international arena. This paper focuses on how to structure the introduction of litigation trusts into the dispute resolution mechanism of group litigation and how to use its development to update the dispute resolution mechanism of group litigation so as to activate the potential of trusts in China.

Keywords: Special Representative Litigation System for Securities Civil Disputes; Litigation Trust; Litigation Economy.

1. Overview of litigation trust system construction

1.1 Construction Purpose

Improving the efficiency of class action in securities civil disputes has always been an important purpose of China's representative system. According to the above, the efficiency problem is also one of the reasons for the extremely low application rate of the existing special representative system. For small and medium investors, special representative litigation has solved the deadlock that securities disputes cannot be sued, while its potential has not been activated. Currently, only Kangmei Pharmaceutical, which has great social influence and a wide radiation range, has started the special representative litigation.

Trust is a system with both applicability and efficiency, which has wide applicable scenarios. From the perspective of legislation and practice, trust for the purpose of litigation and debt collection is prohibited in China, which is also a common practice in civil law countries such as well as Japan and Taiwan in China. In contrast, Western developed countries have a high tolerance for trust, and the integration and development of a trust system also promote market prosperity. The legislative practice of trust in the world for many years fully demonstrates its stability and potential. The development of litigation trust in China is helpful to broaden the potential of the trust system in China market.

1.2 Construction Ideas

1.2.1 Schematic Diagram of Litigation Trust

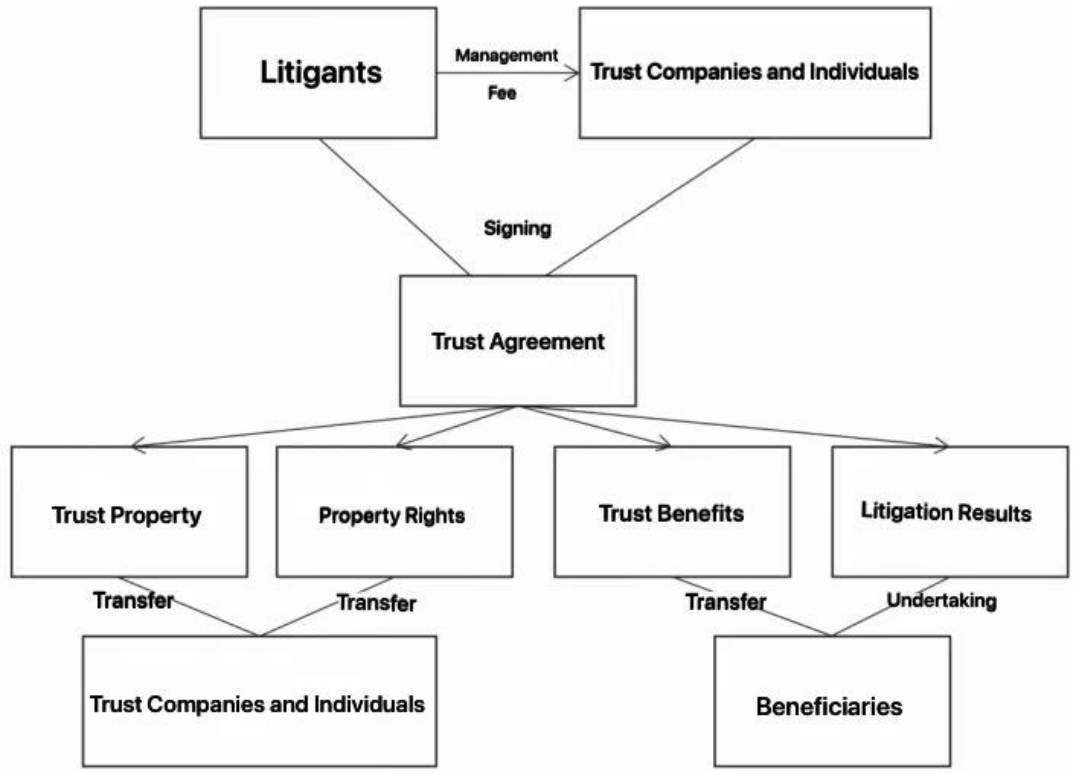


Figure 1. Schematic Diagram of Litigation Trust

1.2.2 Model Building

The construction idea of a litigation trust system is very clear, so we take securities civil disputes as an example to make a simple framework.

a. Content and Signing of Litigation Trust Contract

When faced with civil disputes over securities, the parties' strength is not enough to compete with capital. Considering the problem of litigation, they will choose to sign trust contracts with trust companies or individuals, and hand over the property rights of investments such as securities or stocks to the trustee. Besides, these investments such as securities or stocks will become trust property. The trustee has the obligation to manage the property according to the principal, including litigation for his property when necessary. At the same time, the party as the principal automatically withdraws from the litigants. Being a party with subject qualification and the obligation to participate in the management, the trustee bears the responsibility and will strive for the greatest trust benefits for the beneficiary according to the principal. Because the client has to pay the property management fee based on the trust contract, the disputes between the parties arising from the above-mentioned "free rider" and other behaviors will cease to exist.

b. Rules and Mechanisms of Trustee's Participation In Litigation

At this time, the trust company or the entrusted individual will become the holder of the property rights from stocks or securities, which will exert its professional knowledge to fight for the interests of the trust property according to the entrusting party in the litigation. During this period, they do not need to discuss with the entrusting party, after the transfer of property rights, they have become eligible parties to civil litigation of securities disputes.

The efficiency of this process is higher than that of the original special representative litigation. As for courts, it is often more efficient to connect with professionals, from which they simplify the original rights registration system, equivalent to many rights registrants condensed into one or more trust companies and entrusted individuals, greatly reducing the tedious degree and time cost of

procedures. The original procedure of parties' participation has also been replaced by a flexible and simple trust contract, which reduces the complexity of group litigation.

c. Acceptance and Distribution of Litigation Results

It is a part of the trust's responsibility to bear the risk of managing trust property. Generally, the shrinkage and risk of trust property in the management are borne by the principal and beneficiary, because the trust property is relatively independent and will not be entangled with the inherent assets of the trustee. Similarly, the trust behavior of litigation trust is "litigation", and the trustee is not liable for compensation for the impact on the income of trust property caused by litigation results. No matter whether the entrusted property is reduced or increased due to litigation, the trustee must transfer all of it to the beneficiary according to the contract.

Regarding the issue of winning the case. In this process, the trustees are a group of people with expertise who also have property rights over the trust property during the litigation process, and if they also lose the case, it is difficult for small and medium-sized investors to have a greater chance of winning as individuals who do not have the expertise and professional capacity to do so.

As for the confusion between the trustee's personal property and trust property, beneficiaries, and principals need not worry about the dispute's confusion between trustee's inherent property and trust property. The trust property in litigation trust also includes the trust interests increased by the trustee due to management, application, and disposal. The trustee must manage and keep accounts of the trust property and the inherent property separately, which may not classify them as his own inherent property. The increased interests of the trust property also belong to the trust property.

2. Feasibility Analysis of Litigation Trust

2.1 Analysis and development of overseas practice

Unlike civil law countries, which generally restrict litigation trusts, the trust system in the United States is very developed, and trusts are used in all areas of life, and it generally adopts a policy of encouraging the use of trusts and trust product development, just like China in the field of contract "to encourage the validity of contracts". Under this law policy, since the law does not explicitly provide that litigation trust is invalid, the parties to set up such a trust is naturally valid.

As for judicial practice. Litigation trust has penetrated into the judicial system of the United States, Germany and other countries, especially after the ratification of the Hague Trust Convention, the trust transcends the traditional national boundaries. Common law countries have entered the research stage of trust litigation specific problem solving, facing such issues as bankruptcy trust litigation, Z-trust litigation, etc. Insolvency trusts, whether trusts are suitable to be incorporated into the arbitration system by the litigation system are also hot issues at this stage. In terms of type update, Oliver Passmore (2020) in his article "Insolvent trusts-the Z Trusts litigation" mentions that the Z Trust litigation in Jersey represents the first time that the court considered what happens when a trust becomes "insolvent What happens when a trust becomes "insolvent". At this point, dealing with this situation should address everything from the duties of the trustee, to the procedures for creditor claims, to the issue of priority among creditors. In terms of procedural construction, some US scholars such as Tina Wusteman (2018) also argue that the development of litigation trusts has matured and the privacy and confidentiality of arbitration has made trust arbitration possible.

As for institutional renewal. First, the scope of application of litigation trusts is being expanded. From the earliest private interest litigation trusts gradually expanded to public interest litigation trusts, such as Juliana v. United States, which sparked a discussion of atmospheric public interest litigation trusts, a global movement called Atmospheric Trust Litigation (ATL) launched as early as 2012.ATL proposes a macro litigation approach to the climate crisis, focusing on treating the atmosphere as a whole asset. As trustees, all states have a primary fiduciary obligation to their citizen beneficiaries to restore the health of the atmosphere. Second, the areas of application of litigation trusts are constantly being updated. One of the more interesting areas is the probate litigation trust, where some scholars such as Professor Molly from Oxford University argue that humanitarian concerns should be added

to the probate litigation trust, meaning that we cannot require the trustee to simply mechanically comply with the requirements of the deceased principal to preserve the actual value of the capital, and that we should give the judge discretion in this regard in the design of the system. Finally, there is a more in-depth institutional exploration of the interests of the principal trustee, for example, Kate Davenport, QC's article "In depth Recoverability of Trustee Litigation Costs" published in Trusts & Trustees explores the trustee's interest in the right of trustees to reasonable compensation for costs "properly incurred" and "within reason" and how to provide for such a system of compensation to balance the interests of trustees and beneficiaries.

As for Court proceedings. Because a litigation trust is essentially a fiduciary model, the same rules that apply to court proceedings apply to litigation trusts. First, the trustee's discretion is not absolutely unlimited, although, as the language of the U.S. Uniform Trust Code claims to grant broad discretion, the trustee must act fairly in equity in making decisions that affect different classes of beneficiaries differently. Second, trustees are subject to non-fiduciary duties in addition to their fiduciary duties, what we commonly refer to as the duty of care, but the duty of care here should be distinguished from the duty of loyalty, such as that referred to by Lord Walker of England in the House of Lords case of Hilton v. Barker Booth & Eastwood (2015), where "if a solicitor is investigating a title or drafting a lease carelessly, he may be liable to pay damages for breach of his professional duties, but this is not a breach of the fiduciary duty of loyalty; it is only a breach of the duty of care". The judge should make a decision appropriate to the different duties when hearing the case.

2.2 China Practice Feasibility Analysis

Although Article 11(4) of the Trust Law of the People's Republic of China denies the legality of litigation trusts in China by stating that "a trust established exclusively for the purpose of litigation or debt collection is invalid. [1] However, this article is a copy of the Japanese Trust Law at the time of its establishment, and the risk of abusive litigation and the risk of investors' interests, which was the concern behind this article, no longer exists, because litigation trusts transfer not litigation rights but trust property, so this article is no longer suitable for this restriction.

The litigation trust has the feasibility of solving realistic problems, from the subject: the litigation trust makes the parties out of the original state, the full use of the trustee's professionalism and scale, to maximize the success of litigation; from the procedural point of view: the scope of the selection of cases is more clearly defined, and the overall procedure is more flexible and effective.

From the perspective of legal economic analysis, litigation trust has great practical economic rationality and feasibility, litigation trust as an efficient dispute resolution mechanism, to make up for the long time span in the special representative litigation, the trustee's lack of efficiency and other disadvantages, in addition to ordinary representative litigation and special representative litigation, the principal can choose trust litigation according to their own circumstances, increasing the parties' remedy channels, in judicial practice makes the parties fit to expand. In addition, for the court, it is often more efficient to communicate with professionally qualified people such as a delegated company or individual, and also reduces the process flow within the parties because of publishing opinions and voting.

2.3 Analysis of drawbacks and construction of supporting system

2.3.1 Entrusted Company or Individual Seeks Improper Benefits

A litigation trust is in a restricted state in Chinese law without a clear regulation path and definite proportion limit for the property management fees that the trustee can obtain. The entrusted trust company or individual may infringe on the interests of the principal through the status of qualified parties alone or together with securities-infringing companies to obtain illegal interests. Moreover, the trust company may extort money from both sides, thus raising the entrusted fees.

Firstly, entrusted companies or individuals collaborate with securities companies to infringe upon the interests of clients. As mentioned earlier, because the shrinkage and reduction of trust property caused by litigation is generally borne by the principal and beneficiary, if there are loopholes in the

supervision, the trustee may accept bribes from securities companies for greater benefit and realize charges on both sides.

Secondly, extortion from both sides of the trust company. In case of loopholes in supervision, apart from collecting the principal and informing the corresponding securities company of the entrusted facts, the trust company extorts money from the securities company at the critical stage of litigation from both sides or extorts money from the principal based on the facts and evidence it has mastered.

2.3.2 Prohibition Provision of the Trust Law

The fourth provision of Article 11 of the Trust Law stipulates that trust cannot be used for litigation and debt collection. Compared with other countries that restrict trust, China's Trust Law also includes the extension of "litigation" and "debt collection", making the trust market subject to many restrictions in China, which is also an important reason why litigation trust is difficult to realize in China at present. Although litigation trust is essentially based on trust property and the provisions of Article 11, the trust for the purpose of "litigation" is still illegal in China, which also creates a fundamental dilemma for the realization of litigation trust in China. However, concerning the development of the rule of law in China, the author thinks that the existence of this provision will do more harm than good after 20 years.

Firstly, litigation trust is an international legislative trend. Although civil law countries generally adopt conservative legislative measures for trust, and judges also adopt conservative restrictive attitudes in judicial practice, we can't deny that litigation trust plays a great role in revitalizing non-performing assets and improving practical efficiency.

Secondly, the reasons for prohibiting litigation trust in civil law countries are no longer valid at this stage. The main reason is that restricting people who are not lawyers from obtaining illegitimate interests through litigation and debt collection will cause social abuse of litigation. Litigation trust does not necessarily lead to litigation abuse. Commercial trust is the main one in China, and litigation trust is also a system that needs to pay trust remuneration. Formulating reasonable remuneration standards can greatly reduce the risk of abuse of litigation. [2]

2.3.3 Weaknesses of China's Trust Market

a. Limitations brought by Professionalism

Trust mechanism is still a highly professional term for the market with certain barriers to its popularization. Small and medium investors have different educational levels and professional fields. Under this situation, trusts often involve their knowledge blind spots, not to mention looking for professional trust companies to entrust litigation trust business.

b. Overcautious Status Quo

From the public perspective, trust is a system of temporarily delivering one's own property to others, with substantive rights involved in this process, because some related professionals use the blindness of public knowledge to seek illegal interests by illegal extortion and other means, which leads to the trust market taking an extremely cautious attitude towards transferring substantive rights. From the legislative perspective, the current legislation on trust is only the Trust Law promulgated in 2001, and some provisions have been outdated after more than 20 years. The over-conservative attitude of trust legislation is no longer applicable to the present.

2.4 How to Solve the Problems in and Improve This Design

Litigation trust is a kind of trust in essence, so the current legislative measures for the trust should also be applied to a litigation trust. However, litigation trust itself has characteristics that general trust does not have, so the improvement of litigation trust mainly starts from its characteristics.

2.4.1 Stipulate The Faithful Duty of The Litigation Trust's Trustee

In the final analysis, trust is a legal relationship based on trust, and litigation trust is a system that endows the trustee with the status of a party. In order to avoid infringing on the property interests of the trustee for greater illegal interests, the trustee must have a certain loyalty obligation. Although the

loyalty obligation is difficult to enumerate in the law, its significance is great, which can produce deterrence for trust companies and entrusted individuals.

a. Set a Reasonable Range of Property Management Fees

For the property management fee of a litigation trust, a reasonable maximum charging ratio should be set according to the general market standard, which can avoid the trust company from extorting clients who lack professional knowledge. Besides, friction and disputes between the two parties should be avoided due to the charging standards setting.

b. Stipulate Responsibility of the Trustee for Abnormal Shrinkage of Trust Property

This provision is mainly aimed at the trustee colluding with securities infringing on the property interests of clients and beneficiaries to seek illegal interests. A reasonable proportion of litigation trust property preservation standards can be formulated, which will also alleviate the client's concerns about choosing litigation trust, leaving a regulatory effect on the trustee with expanded authority.

2.4.2 Learn From Relevant Foreign Systems

Trust originated and developed in common law countries, which is different from civil law countries. Besides, common law countries generally do not prohibit litigation trust with many applications in judicial practice. For example, the American Trust Law stipulates that "trusts can be established for any legitimate purpose".

a. Identification of Trust Systems with Litigation Functions

Litigation trust cannot be purely for the purpose of "litigation" in practice, because when the parties find the trust company, they essentially hold the purpose of revitalizing investment interests. Litigation may only be a means that has to be taken to manage and protect property interests in this process, so it is essentially different from the trust with the purpose of litigation and debt collection. According to this system design, litigation trust cannot be interfered with by Article 11 of Trust Law. In addition, it is a legal system and can be realized in judicial practice by making great efforts in "identification".

b. Correct view of revitalizing non-performing assets by means of trust

As mentioned above, because of the inherent advantages of trust companies, the use of trusts to revitalize non-performing assets has become an internationally accepted method, and is an effective way to take advantage of the flexibility and efficiency of the trust system.

c. Formulating Standards for Judicial Review of Litigation Trusts

This step can help identify the trust system with litigation function and avoid illegal litigation trust and debt collection trust in practice. First of all, whether litigation or debt collection is the only way to manage a property can be judged from the content of the trust contract and the trust management behavior of the trustee. Secondly, it can be used as a reference to see whether the time interval between taking over the trust property and suing is too short. If so, it is likely to be "for the purpose of litigation".

2.4.3 Introduce Trust Compliance System

a. Introduction of a Third-Party Review Process

A third-party review institution or supervision system between the principal and the trustee should be established to control the safety of trust property and reduce the risks of trust property. Meanwhile, the trust business qualifications of trustees and individuals should be strictly checked, so as to set a model of entrustment contract and protect the interests of both parties.

b. Taking Law Firms as The Main Body of Legal Services and Introducing

Lawyers' Risk Agency

Law firms, especially high-level law firms, often have strong economic strength and professional level, which can give full play to the great promotion of the market economy compared with investor protection institutions. Therefore, high-level law firms should be encouraged to participate in class actions, advance litigation-related expenses [3], and collect an appropriate proportion of risk agency fees after winning the case. The risk agency fees can be drawn from the trust property, which is decided by the trustee according to the situation and the agreed risk ratio.

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