



Inland Revenue Department
Hong Kong

STAMP OFFICE INTERPRETATION & PRACTICE NOTES

NO. 3

DEEMED CONSIDERATION UNDER SECTION 24 OF THE STAMP DUTY ORDINANCE, CAP. 117

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September 1998

Stamp Office Interpretation and Practice Notes No. 3

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INTRODUCTION

1. Section 24 of the Stamp Duty Ordinance (Cap 117) deems certain debts discharged, payments of money, transfers of stock and indebtedness incurred to be the whole or part of the consideration for the sale of property or the passing of a beneficial interest in Hong Kong stock. This Practice Note sets out the current practice of the Collector of Stamp Revenue in applying section 24 in relation to the assessment of stamp duty on conveyances on sale of immovable property, chargeable agreements for sale and purchase of residential property, and on any transaction whereby a beneficial interest in Hong Kong stock passes.

INSTRUMENTS / TRANSACTIONS AFFECTED

2. Section 24(1) applies to 3 types of instruments or transactions, namely, (i) a conveyance on sale of Hong Kong immovable property; (ii) a transaction whereby a beneficial interest in Hong Kong stock passes; and (iii) by virtue of section 29C(9), an agreement for sale and purchase of residential property. “Hong Kong stock” is defined in section 2 of the Ordinance to mean “stock the transfer of which is required to be registered in Hong Kong”. In general terms, it means stock of a company for which the register of members is maintained in Hong Kong, such as stock of companies incorporated under the Companies Ordinance (Cap. 32) and stock listed on the Stock Exchange of Hong Kong Ltd.

3. Section 24(3) extends the charge of section 24(1) to cover certain share transfers . This is discussed in more detail in paragraphs 15 to 20 below.

GENERAL PURPOSE

4. The section is, in essence, an anti-avoidance measure designed to tackle transactions with the following characteristics -

- “disguised consideration”, where part or all of the consideration paid by the purchaser of a property, or the transferee in respect of a transfer of stock, does not take the form of the usual consideration on sale, such as a payment of

money from the purchaser to the vendor. Examples of such disguised consideration cases include the discharge of a debt due to the purchaser or transferee, payment by the purchaser of a debt of the vendor to a third party, and a payment by the purchaser to a party specified by the vendor;

- “disguised equity” where a loan (typically a shareholder’s loan) is used to finance the operations of a company with a small amount of issued capital.

DEEMED CONSIDERATION UNDER SECTION 24(1)

5. Section 24(1) deals with two situations -

- (a) where the transfer of property or Hong Kong stock is in consideration, in whole or in part, of any debt due to the transferee (or to the purchaser in the case of a chargeable agreement for sale);
- (b) where the transfer of property or Hong Kong stock is subject either certainly or contingently to the payment or transfer of any money or stock

For the subsection to apply it is not necessary for the debt, or the payment or transfer of money or stock, as the case may be, to constitute a charge or incumbrance upon the property conveyed or transferred.

6. Under such a situation, the debt (subject to section 24(2)), money or stock is deemed to be the whole or part, as the case may be, of the consideration by reference to which the subject instrument (i.e. the conveyance, transfer or chargeable agreement) is chargeable with stamp duty.

7. Where a debt, or part of a debt, due to a transferee is discharged as consideration (wholly or in part) of a conveyance or transfer, the full amount discharged is deemed to be consideration under section 24(1), irrespective of whether the debt is doubtful or bad [*IRC v. North British Rly Co (1904) 4 F (Ct of Sess) 27*].

8. The second situation referred to in paragraph 5 above, is further expanded by section 24(3), as discussed in paragraphs 15 to 20 below.

SCOPE OF SECTION 24(1)

9. Section 24(1) is expressed in wide terms. In this regard, the following points should be noted -

(a) ***“whether or not ...constituting a charge or incumbrance”***

Provided that the other criteria are satisfied, the subsection applies whether or not the debt in question, or the payment or transfer of money or stock, constitutes a charge or incumbrance upon the property conveyed or the interest in the stock passing.

(b) ***“either certainly or contingently”***

Likewise, where a conveyance of property or a transfer of stock is subject to “the payment or transfer of any money or stock”, the subsection will apply irrespective of whether the liability to pay or transfer is certain or contingent.

(c) ***“subject to the payment or transfer of”***

While the section does not expressly provide by whom and to whom the money or stock is paid or transferred, the Stamp Office accepts that the obligation to pay the money or transfer the stock would normally be that of the purchaser of the property or the stock, although this may be done in an indirect manner (e.g. the purchaser may instruct a related person to pay the money or transfer the stock on his behalf). However, it is not necessary for the purchaser to assume personal liability for making the payment or transfer. As for the recipient of such money or stock, this can be the vendor or indeed any other person. In *IRC v Liquidators of City of Glasgow Bank (1881) 8 R (Court of Session) 389*, it was held that an equivalent provision in the UK legislation had been correctly applied to include in the consideration in respect of which a conveyance of property was chargeable with stamp duty, not only the amount of a debt discharged

as a result of the transaction, but also the value of a bond, payable to a third-party, charged on the property.

10. Typical of the cases falling within the application of section 24(1) is one where shares in a target company are transferred at an agreed consideration and, at the same time, the company's indebtedness to the vendor of the shares (or an associate) is assigned to the purchaser of the shares (or an associate). In such a case, the transaction relating to the shares comes within the subsection as it is subject to the payment of a sum of money in respect of the assignment to the purchaser of the benefit of the company's debt. This sum of money (which may differ from the face value of the debt) would therefore be deemed to be part of the purchase consideration.

LIMITATIONS ON THE APPLICATION OF SECTION 24(1)

11. Despite the wide application of section 24(1), it is subject to the following limitations -

(a) ***“in consideration of”***

It is clear that for section 24(1) to apply, the payment of money or transfer of shares must form an integral part of the transaction effecting the transfer of property or Hong Kong stock. It follows that if a payment of money or transfer of shares is independent of the transaction for the sale of property or stock to which the subject instrument relates, the payment or the transfer, as the case may be, will not fall within the scope of section 24(1). It is pertinent in this regard that stamp duty is not chargeable in Hong Kong in relation to any independent dealings in debts (i.e. assignments of debts, etc.).

(b) ***Disregard liabilities inherent in the nature of the property or stock transferred***

One of the circumstances for invoking section 24(1) is that whenever a conveyance or transaction is subject to a condition that the purchaser assumes a liability of the vendor to a third party, the assumed liability is

deemed to be part or all of the consideration for the transaction. This provision, however, does not apply to liabilities inherent in the nature of the property transferred. As such, it has no application to rent payable under a lease in the case of a conveyance of a lease (*Swayne v IRC* [1899] 1 QB 335; *affd* [1900] 1 QB 172).

DEBT DUE TO TRANSFEREE - SECTION 24(2)

12. Section 24(1) provides that a conveyance of property or a transfer of stock in consideration of a debt due to the transferee shall be stamped by reference to the whole amount of the debt (or so much of the debt that is agreed to be discharged, as the case may be). If the subsection were to be read in isolation, it would follow that where a transferee agreed to discharge a debt due to him in return for a property or stock of a lesser value, stamp duty would nonetheless be payable on the amount of the debt agreed to be discharged.

13. However, section 24(2) provides, in effect, that in the above scenario the consideration for calculating stamp duty shall be treated as reduced to the value of the property conveyed or the beneficial interest in the stock passing. The end result is that the amount of the debt agreed to be discharged is disregarded and stamp duty is paid on the value of the property or of the stock transferred.

14. To obtain relief under section 24(2), the relevant instrument must be adjudicated by the Collector under section 13(3) in order to be duly stamped. The purpose of requiring adjudication is to afford an opportunity to the Collector to consider whether the instrument is properly stamped having regard to the provisions of sections 24(1) and (2).

APPLICATION OF SECTION 24(3)

15. Section 24(3) extends the application of section 24(1) under certain circumstances. Section 24(3) provides that where, in relation to a transaction which falls within section 24(1), any liability is incurred by the transferee of shares in respect of any indebtedness of the target company, the transaction shall (in addition to any other

payment of money or transfer of shares to which it is subject) be deemed to be subject to the payment of an amount of money equal to the amount of the indebtedness. By virtue of section 24(1), the “payment of money” is deemed to be part of the chargeable consideration.

16. The intention behind the introduction of section 24(3) was to extend the ambit of the anti-avoidance provisions of section 24(1) to cover transactions where shares in a company change hands and an arrangement is made between the parties so that the purchaser of the shares is required to “re-finance, or guarantee, or otherwise assume liability for the company’s debt” (Hong Kong Hansard, 11 March 1981). Typically, the situation would arise where the company had only a small amount of capital and the value of the shares was insignificant in relation to the debt-financed underlying assets of the company.

17. Section 24(3) operates to treat as consideration the indebtedness of a company which is assumed, undertaken or guaranteed by the transferee of the beneficial interest in the shares of a company. This may occur where a transferee of shares in a company, as an integral part of the arrangement to purchase the shares, agrees to procure or guarantee that a loan due by the company to the outgoing shareholder or some other party will be paid. In such a case, it is common practice to have a provision in the agreement covering the transfer of the shares which requires the transferee himself to provide the relevant funds in the case of default. Such a provision is prima facie evidence that some form of liability within the terms of section 24(3) has been incurred by the transferee of the shares.

18. The amount taken into account for the purposes of section 24(3) is the *amount* of the indebtedness incurred by the transferee. No account will be taken of the *value* of the indebtedness, i.e. whether the debt is likely to be fully repaid or to be a bad debt.

19. It should be noted that in a case where section 24(3) does not apply, for example because the transferee does not personally incur liability in respect of any indebtedness of the company, section 24(1) may still be applicable if the transfer of the shares is in consideration of any money payable by any other person.

20. Section 24(3) cannot apply to a conveyance on sale of immovable property nor to a chargeable agreement for sale and purchase of residential property; it can only apply in respect of a transfer of shares.

EXAMPLES

21. The following examples illustrate the Stamp Office's practice in relation to the application of section 24 -

- (a) **A sells shares in target company to B. As part of an integral transaction of such sale, A assigns to B the shareholder's loan due by the company.**

By virtue of section 24(1), the money paid by B as consideration for the assignment of the shareholder's loan would be deemed to be part of the consideration for the sale and purchase of the shares. This is because the sale of shares is subject to a payment of money, and B can only obtain the unencumbered corpus of the subject matter (the shares) upon payment of the relevant sum.

If in the above case, instead of accepting an assignment of debt, B incurs a liability in respect of the shareholder's loan such as undertaking or guaranteeing its repayment, the full amount of the debt (rather than the amount paid for the assignment of the debt) will be chargeable to duty pursuant to section 24(3) .

- (b) **Same facts as (a), but (instead of B) C, an associate or a nominee of B, takes up the assignment of the shareholder's loan.**

The money paid by C to A for the assignment of loan would be deemed under section 24(1) to be part of the consideration paid for the share (see also paragraph 9(c) above).

- (c) **A sells shares in target company to B. As part of an integral transaction of such sale, B undertakes to make a loan to the target company to enable it to repay the shareholder's loan to A.**

The injection of funds into the target company is a “payment of money” for the purposes of section 24(1). Therefore, the basic charge under section 24(1) applies to deem the amount of the agreed loan to be part of the consideration for the transfer. The use of the loaned money is in fact irrelevant.

- (d) **A sells shares in target company to B. A assigns his shareholder's loan to the target company to C. The two transactions are independent and separate transactions in the sense that the performance or otherwise of either one is unaffected by the performance or otherwise of the other.**

Section 24 would have no application. The selling of shares is not subject to the payment of the consideration for the purchase of the rights to the shareholder's loan and hence section 24(1) would not be relevant. Furthermore, as B has not *incurred* any liability in respect of the target company's debt (see paragraph 17 above), section 24(3) would also not be applicable. It would, of course, be a question of fact as to whether C had agreed to buy the shareholder's loan independently of A agreeing to sell the shares to B.

- (e) **Same facts as (a) above, but the shareholder's loan is assigned for less than its face value.**

Same treatment as for (a) above. The amount to be taken into account as consideration would be the actual amount paid for the assignment and not the face value of the loan (see paragraph 10 above).

- (f) **A sells vacant land to B. As part of the sale agreement, A agrees to erect on the site a house or flat and to spend \$x for this purpose.**

What A undertakes to do is to provide the service of erecting a house or flat. The sale of land is not subject to any payment of money (\$x for the

erection of the house or flat is not such a payment) or transfer of shares and thus does not fall within the scope of section 24(1). Furthermore, as a sale of shares is not involved, section 24(3) is inapplicable.

- (g) A liquidator of a company assigns immovable property to shareholders by way of a distribution in specie. The assignment is subject to a mortgage in favour of a third party.**

As an assignment effecting a distribution in specie by a liquidator in relation to a voluntary liquidation is not a conveyance on sale, the assignment in question would not come within the scope of section 24.

- (h) An executor of a will transfers Hong Kong stock or immovable property to a pecuniary legatee in satisfaction of a pecuniary legacy.**

A transfer of Hong Kong stock or conveyance of immovable property by an executor of a will to a pecuniary legatee in satisfaction of a pecuniary legacy is taken as a sale and purchase of the stock or property, with the pecuniary entitlement of the legatee as the consideration. Where the value of the property or stock differs from the pecuniary entitlement (whether more or less), through the operation of section 27(4) and section 24(2), the amount of the stamp duty payable will be calculated by reference to the value of the property or stock transferred rather than to the amount of the pecuniary legacy.

Where the beneficiaries under a will agree upon and execute a deed of family arrangement (with bequests under the will re-arranged by mutual agreement), the deed is stamped with the applicable stamp duty. A transfer of Hong Kong stock or immovable property in pursuance of such a stamped deed does not attract any further stamp duty.

- (i) Upon transfer of Hong Kong stock, the purchaser agrees upon registration of the share transfer to cause the company to convert the vendor shareholder's loan to the company into equity.**

For a liability to fall within the scope of the words “any liability is incurred in respect of any indebtedness” in section 24(3), it should directly relate to an arrangement under which the purchaser of shares re-finances, guarantees, or otherwise assumes liability in respect of a debt of the company. The arrangement should be such that it will allow the debt to be actually repaid. Accordingly, in the scenario outlined, the agreement to cause the company to convert the loan of the vendor shareholder into equity would not come within the scope of the subsection.

SECTION 27

22. It should be noted that section 24 merely provides a formula for the determination of the consideration, for stamp duty purposes, in respect of a conveyance on sale, a chargeable agreement or a transfer of stock under the circumstances specified in the section. This does not prevent the application of section 27(4) and (1) of the Ordinance to a case where the “deemed consideration” would still be below the value of the property or stocks transferred. Where section 27 applies, stamp duty is based on the value of the property or of the stock concerned.

DISCLOSURE REQUIREMENT

23. Section 11 of the Stamp Duty Ordinance requires that all the facts and circumstances affecting the liability of any instrument to stamp duty, or the amount of the stamp duty chargeable on an instrument, be fully and truly set forth in the instrument. Therefore, in presenting any conveyance on sale of immovable property, chargeable agreement for sale and purchase of residential property or transfer of Hong Kong stocks to the Stamp Office for stamping, in circumstances where section 24 may be applicable, it is the duty of the purchaser and seller, or transferor and transferee as the case may be, of the property or stock to provide full details of the facts and circumstances of the transaction *in the relevant instrument*. The Stamp Office may, if it is considered necessary, make enquiries in relation to the facts and circumstances of a transaction before stamping the instruments concerned.