



Is Stamp Duty Really a Tax on Instruments?

The recently enacted Stamp Duty (Amendment) (No 2) Ordinance contains several traps for the unwary

With the establishment of the Central Clearing and Settlement System (CCASS), large amounts of stock in Hong Kong listed companies have been placed in the central depository and registered in the name of a common nominee. Thus, a transfer of stock (or interest in stock) held in CCASS (otherwise than on sale and purchase) no longer requires executing an instrument of transfer.

It follows from this, that payment of stamp duty could be avoided by avoiding the execution of any 'transfer' document when dealing (by way of a voluntary disposition) with the beneficial interest in Hong Kong stock held in CCASS.

Section 19(1E) of the *Stamp Duty (Amendment) (No 2) Ordinance* was enacted with the specific aim of plugging this potential loophole. It is, however, important to appreciate that the Stamp Office apparently believes that the effect of s 19(1E) is much broader than this. Subject to para (c), an expansive view of s 19(1E) (if adopted by the Stamp Office) would deem there to be a sale and purchase of Hong Kong stock (listed or unlisted), whenever there has been a gift of Hong Kong stock (or a gift of an equitable interest in that stock) which was completed without creating a stampable instrument of transfer. A narrower yet, in my view, justifiable interpretation of s 19(1E) is that it only applies to stock transfers made under or through CCASS or other organisations performing clearing house functions.

Where s 19(1E) applies, contract notes will need to be prepared and stamped, in accordance with the provisions of s 19(1) and head 2(1) of the First Schedule, by those persons disposing of and acquiring the Hong Kong stock. Stamp duty will then be levied at the rate set out in head 2(1)

on the value of the stock, which for this purpose is deemed to be the amount or value of the consideration for the sale and purchase (see s 19(1E)(b)).

If the expansive interpretation noted above prevails, it would be fair to say that, in relation to transfers of Hong Kong stock, s 19(1E)(a) makes a mockery of the supposed rule that stamp duty is only levied on instruments and not on transactions. The only relaxation to the provisions of s 19(1E)(a) is that it does not apply to:

- mere changes of legal ownership of Hong Kong stock, eg upon the appointment of a new trustee to an existing trust, and
- transfers of Hong Kong stock which, if effectuated by way of a transfer falling within head 2(3) of the First Schedule, would qualify for exemption under s 27(5) (see s 19(1E)(c)).

An example of the latter would be where a trustee under a discretionary trust simply appoints Hong Kong stock in favour of a beneficiary under the trust without divesting itself of legal title. In this case, any note of appointment or other instrument passing beneficial interest in the Hong Kong stock (assuming that this does not operate as a 'transfer' which would normally be chargeable under head 2(3) were it not for the exempting effect of s 27(5)), would not be deemed to be a sale or purchase of Hong Kong stock.

Taking Advantage of the s 27(5) Exemption

An amendment to s 27(5), also taking effect on 1 May 1998, requires that the circumstances exempting an instrument from stamp duty under that provision, have to be set forth in the instrument itself. A similar requirement is contained in s 11(1), which states that the facts and circumstances affecting

the liability of any instrument to stamp duty, or the amount of duty chargeable on any instrument, have to be fully and truly set out in the instrument.

The combined effect of these provisions is that a casual disclosure of some facts and circumstances affecting stamp duty liability will amount to insufficient compliance. If there are other fundamental facts and circumstances, which are crucial for the Collector to determine whether an instrument qualifies for exemption under s 27(5) or in assessing the stamp duty liability of the instrument, such facts and circumstances have to be set forth in the instrument as well.

For instance, it will not be enough to simply note on an instrument that 'This is a conveyance/transfer under which no beneficial interest passes'. Such a statement simply sets out a deduced circumstance rendering the instrument exempt from duty under s 27(5). In such a case, the Collector would undoubtedly wish to ascertain the basic facts and circumstances giving rise to that statement, eg in cases where the instrument is made for the appointment of a new trustee or made for the transfer of assets from a trustee to a beneficiary under a trust (if those facts are not readily ascertainable by examining other parts of the instrument).

In short, primary facts affecting liability to stamp duty should be set out in the instrument itself, in order to satisfy the requirements of s 27(5) (and s 11(1)). Nonetheless, it should not be necessary to recite all background details (such as the particulars of the trust in the above example) in the instrument, to support the facts and circumstances already set forth.

That is not to say that the Stamp Office would not require evidence that the property being transferred was properly subject to the trust or that there was a valid deed of appointment and removal of trustees. The Collector could request such details under the information gathering powers provided to him by s 12.

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