

STAMP AMENDMENT BILL 1996

EXPLANATORY MEMORANDUM

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This Bill seeks to amend the Stamp Act to address a deficiency in the legislation which has arisen as a result of changes in business practice regarding the way company takeovers are effected.

By way of background, the Stamp Act imposes duty on off-market transfers of shares in companies incorporated in Western Australia.

Where the shares of a company are listed on the stock exchange, duty is calculated at the rate of thirty cents per one hundred dollars of the market value of the shares traded. If the company is not listed on the stock exchange, duty is calculated at the rate of sixty cents per one hundred dollars of the market value of the shares.

The Act does not, however, impose duty on an acquisition of a company undertaken off-market by other means. Notably, the issue and cancellation of shares are not generally subject to duty.

When a person seeks to take over a public company, the acquisition must be effected in accordance with Chapter 6 of the Corporations Law. This normally requires the direct acquisition by the acquirer of the issued shares in the company it is seeking to take over.

As this procedure necessitates a transfer of the shares, stamp duty is payable on the acquisition.

Notwithstanding that Chapter 6 of the Corporations Law requires a takeover to be effected by the direct acquisition of the other shareholders' shares, the Australian Securities Commission has special powers to permit a takeover to be effected by way of a selective reduction in the capital of a company. For example, under Chapter 5 of the Corporations Law, a capital reduction pursuant to a court approved scheme of arrangement can take place.

Such a capital reduction, if structured in an appropriate manner, can result in no stamp duty being required to be paid on the acquisition.

Accordingly, if an existing shareholder of a target company wishes to undertake a friendly takeover of the remaining shares in that company, it can do so via such a mechanism.

In such a case, rather than purchasing all other shares and receiving them by way of transfer, either under a special resolution of share holders or a court approved scheme of arrangement, those shares could be cancelled leaving the person or company wishing to effect the takeover as the sole shareholder of the target company.

Consideration for the cancellation of those shares could be provided either through the issue of shares in the new owner of the company or a straight cash payment of equal value to the shares cancelled.

As the Stamp Act currently only imposes duty on the transfer of shares, the acquisition of a company in this manner would not be subject to stamp duty.

It must be stressed that transactions undertaken in this manner are not necessarily driven by stamp duty considerations.

For example, a scheme of arrangement by way of a capital reduction may be attractive to enable a number of different classes of shares (eg. the ordinary shares, convertible notes and options of a company) to be acquired through the one mechanism rather than separate offers being made in respect to each type of security on issue as would be the case under a Chapter 6 takeover.

Furthermore, an acquisition in this manner provides greater certainty that the takeover succeeds. Were an acquisition to be pursued by way of a takeover offer, the acquiring company would be required to obtain 90% of the issued shares in the target before a compulsory acquisition could occur.

Under a scheme of arrangement, they need only 50% of share holders representing 75% of the issued shares to agree to the scheme to ensure that the takeover succeeds.

It is inequitable that a company takeover involving the transfer of shares is subject to stamp duty whereas a company takeover pursued by way of a capital reduction is not. Moreover, the Australian Securities Commission has advised that it is becoming increasingly common for the acquisition of a company to be pursued via a scheme of arrangement involving a capital reduction approved by the Commission.

The Commission's duty, however, is limited to ensuring that the shareholders of the takeover target are fully informed and dealt with in an even handed manner. The fact that stamp duty is minimised is immaterial.

It must be stressed that the amendments proposed in this Bill do not seek to prevent the acquisition of a company by means of a capital reduction.

Rather, they seeks to restore equity in the stamp duty treatment of interests in companies acquired by the direct purchase of shares with those acquired by way of capital reduction.

The proposed amendments will apply only in certain situations where a person gains 50% voting control of a company or increases their voting control above 50% by an incremental amount of 5%.

If such an increase in control results from either a cancellation of shares in that company or a voting rights alteration of the shares in the company followed by a share cancellation, the company is required to prepare and lodge a statement with the Commissioner.

Duty will then be charged on that statement at the appropriate marketable security rate of duty on the value of the cancelled shares. The party liable to pay the duty on the statement is the company and its directors at the time of the resolution to reduce the capital or alter the voting rights.

The legislation has been drafted to ensure that the provisions will not apply in all cases where shares are cancelled.

In particular, the provisions will not apply to share cancellations arising from: -

- share buy-backs;
- the ordinary forfeiture of shares;
- pro-rata capital reductions; or
- the cleaning up of "odd lots" of shares.

Stamp duty associated with transactions which have been undertaken since 20 November 1995 that are expected to fall within the operation of these amendments is expected to total around \$2 million.

Furthermore, the protection provided to the revenue in the future by these measures is likely to considerably exceed this amount, given the growing popularity of capital reductions as a means of company acquisition.

Outlined below for further information is a more detailed discussion of each clause of the Bill.

Clause 1: Short title and citation.

Clause 2: Provides that the amendments come into operation on 20 November 1995. This date is consistent with the date the Government announced its intention to legislate these changes in a media statement issued by the Hon Minister for Finance.

Clause 3: This clause identifies the principal Act as the Stamp Act 1921.

Clause 4: Amends section 4(1) of the principal Act to insert in the general definitions a definition of "director".

Director has been defined to have the same meaning as that term is defined in section 9 of the Corporations Law.

Clause 5: Subclause (1) amends section 20(1) of the principal Act which deals with the timing requirements for the lodgement of instruments and statements without the imposition of fines for late lodgement.

Paragraphs (a) and (b) are changes necessary to accommodate the insertion of a new paragraph (d) in that section.

Paragraph (c) inserts a new paragraph (d) in section 20(1) to provide that the statement required under section 112HA in respect of share cancellations of Western Australian incorporated companies will not be subject to a fine if it is lodged within the period specified in that section.

Subclause (2) amends section 20(5a) to ensure that a statement required to be lodged under section 112HA is excluded from the fining provisions applicable to the lodgement of returns outside the requisite times.

These statements are subject to the fining provisions in section 20(2) of the principal Act.

Clause 6: This clause amends section 75D(1) of the principal Act relating to transfers of farming property between family members by deleting the definition of "director" as it currently applies in that Part of the Act.

As the definition of director has application to several Parts of the principal Act, it has instead been inserted by clause 4 in the general interpretation provisions of the Act.

Clause 7: This clause amends section 76(1) of the principal Act which provides the definitions applicable to Part IIIIBA of the Act.

Part IIIIBA provides that certain acquisitions in unlisted companies which own land of a substantial value (\$1,000,000 or more) in

Western Australia, shall be treated as if they were an acquisition of that land.

Paragraph (a) deletes the definition of "director" for the same reason described for clause 6 above.

Paragraph (b) amends the definition of "acquire" by providing that the exclusion in paragraph (e)(iii) of the definition for an acquisition made under a scheme of arrangement does not apply to a share cancellation or an alteration of rights to shares to which section 112HA applies.

Without the amendment, the takeover of a land rich company could be effected without the payment of land rich duty by cancelling or varying the rights of the shares of the outgoing shareholders under a scheme of arrangement.

Clause 8: This clause inserts a new Part IVAC into the principal Act to ensure that marketable security duty is paid on the acquisition of a Western Australian incorporated company that is effected by a selective reduction of the capital of the company.

Traditionally, the acquisition or takeover of a company has been effected under Chapter 6 of the Corporations Law. As the acquisition in these circumstances requires a transfer of the shares to be made from the seller to the purchaser, duty has been payable on the acquisition.

It is becoming common for an existing shareholder of a company wishing to take over the company to by-pass the takeover provisions of the Corporations Law and effect the acquisition by arrangement with the other shareholders to cancel their shares under a capital reduction scheme.

Because duty is only payable on a "transfer" of shares, the acquisition of the company is not currently subject to duty

These amendments will provide that duty will be payable on the acquisition of Western Australian company in these circumstances.

Section 112H - Interpretation

This section defines the terms applicable to the operation of Part IVAC.

Subsection (1) defines "voting share" to have the same meaning as that term is defined in section 9 of the Corporations Law.

The scheme is based on the concept of "control" in the same way as Chapter 6 of the Corporations Law applies to company takeovers.

Control is measured by a person's entitlement to the voting shares of a company.

In conjunction with the definition in subsection (2), this definition is important in determining whether a share cancellation under a capital reduction scheme is subject to duty.

Subsection (2) provides that a person is entitled to a voting share if that person is regarded as being entitled to that share under section 609 of the Corporations Law.

The concept of "entitlement" in the Corporations Law focuses on the power to -

- exercise, or to control the exercise of, the right to the vote attached to the share, or
- dispose of, or to exercise control over the disposal of, that share.

It does not necessarily mean that the person is the owner of the shares.

The entitlement of a person is also measured by taking into account the entitlement to voting shares of associates of that person.

For example, a corporation's entitlement is measured by its direct entitlement and those of its associates including its directors, secretaries, related companies and the directors and secretaries of the related companies.

Section 112HA - Certain capital reductions dutiable

This section provides the mechanics for the operation of the scheme.

Subsection (1) provides that the section applies if a Western Australian incorporated company reduces its capital under section 195 of the Corporations Law by cancelling any of its shares and a taxable event occurs as a result of that cancellation.

A taxable event is defined in subsection (3).

Importantly, the section is not limited to voting shares. As a result, if a taxable event occurs, duty is applied under subsections (8) and (9) on the dutiable value of all classes of shares cancelled under the capital reduction scheme.

Subsection (2) provides that the section also applies if -

- a taxable event occurs because a Western Australian incorporated company varies or extinguishes the voting rights attached to voting shares; and
- within six months after the variation or extinguishment, the shares are cancelled under a capital reduction scheme.

The subsection is an anti-avoidance provision to ensure that subsection (1) cannot be defeated.

That is, the scheme is based on the concept of a change in control of a company through the cancellation of voting shares.

But for subsection (2), the scheme could be defeated by varying or extinguishing the voting rights of the outgoing shareholders before their shares are cancelled.

Subsection (3) defines the circumstances when a taxable event occurs.

Paragraph (a) provides that a taxable event occurs if a person who prior to the capital reduction or rights alteration was -

- not entitled to any voting shares in the company; or
- entitled to less than 50% of the voting shares,

becomes entitled after the cancellation or variation of rights to at least 50% of the voting shares.

Paragraph (b) provides that a taxable event also occurs if a person who was previously entitled to at least 50% of the voting shares becomes entitled after the cancellation or variation of rights to at least an additional 5% of the voting shares.

Subsection (4) requires the Western Australian incorporated company to lodge a statement if subsection (1) or (2) applies unless the capital reduction, alteration of rights or share cancellation also results in a requirement to lodge a statement under Part IIIA of the principal Act.

The exclusion for the requirement to lodge the statement where Part IIIA applies eliminates the need for the preparation of two statements on the one transaction. Moreover, full duty will apply on the Part IIIA statement.

Subsection (5) requires the statement to be lodged within 3 months after the later of -

- the date the capital reduction or share cancellation has effect; or
- if the capital reduction requires the approval of the Court, the date the copy of the Court order is required to be lodged with the Australian Securities Commission.

The alternative timing requirement is to cater for circumstances where, subject to the Court's approval of the scheme, the capital reduction applies from a retrospective date (the date cannot be before the date the company resolved to reduce its capital).

In these circumstances, without the alternative, the company could be in breach of subsection (12) and the statement could be subject to late lodgement fines under section 20(2) of the principal Act.

Subsection (6) deems the statement to be an instrument executed on the date the capital reduction or share cancellation has effect.

The purpose of the subsection is ensure the mechanics of the principal Act relating to imposition of fines on instruments, recovery of duty and fines on instruments etc. apply to the statement as if it were an instrument.

Subsection (7) provides that the statement is to be charged with duty on the dutiable value of the cancelled shares at the rate provided for in -

- item 4A(1)(f) of the Second Schedule to the principal Act if the shares were prior to their cancellation listed on the stock exchange; or
- item 4A(1)(fa) of the Second Schedule to the principal Act if the shares were not listed on the stock exchange.

The rate of duty applicable to shares listed on the stock exchange is 0.03% and for unlisted shares, 0.06%.

Subsection (8) specifies the dutiable value of the cancelled shares as the greater of-

- the market value of the shares immediately prior to the date the company resolved to reduce its capital or to alter the rights of the voting shares; or
- the amount or value of the consideration payable to the holders of the cancelled shares at the date the company resolved to cancel the shares or vary the rights of the voting shares.

Subsection (9) provides that where a capital reduction results in property of the Western Australian incorporated company being transferred to the outgoing shareholders and duty is payable on that transfer under section 75(2a) of the principal Act, the value upon which duty is to be assessed on the statement is to be reduced by the value of that property.

Subsection (10) provides that the Commissioner may request the Western Australian incorporated company to furnish a valuation of the market value of the shares cancelled or of the consideration payable to holders of the cancelled shares.

The subsection also provides that the Commissioner may assess duty on that valuation or on a valuation separately obtained by the Commissioner.

Subsection (11) provides that the Western Australian company that is required to lodge the statement and its directors at the time the relevant resolution for the capital reduction or rights alteration was made, are jointly and severally liable for the payment of the duty.

Subsection (12) provides that if the Western Australian company fails to prepare and lodge a statement or lodges a statement that is false in any material particular, it commits an offence against the Act.

Subsection (13) provides that a Western Australian incorporated company that fails to furnish a valuation of the shares or consideration as required by the Commissioner commits an offence against the Act.

Clause 9: This clause provides for transitional arrangements to apply due to the retrospective commencement date of the amendments.

Subsections (1) and (2) provide that if the amendments result in a requirement to lodge a statement under Division 2 of Part IIIBA or section 112HA in respect of a taxable event which occurred between 20 November 1995 and the date of Royal Assent, the statement shall be lodged within three months after the date of Assent.

Without these provisions, the parties may otherwise be in breach of the lodgment requirements for the statements and potentially be subject to substantial penalties.