File Ref. : FIN R 43/5/136

LEGISLATIVE COUNCIL BRIEF

Stamp Duty Ordinance (Chapter 117)

STAMP DUTY (AMENDMENT) BILL 2000

INTRODUCTION

At its meeting held on 26 September 2000, the Executive Council **ADVISED** and the Chief Executive **ORDERED** that the Stamp Duty (Amendment) Bill 2000, at ***Annex***, should be introduced into the Legislative Council, to exempt the stamp duty chargeable on a transfer of units in investment funds under the mandatory provident fund (MPF) schemes when the units were issued or redeemed if a constituent fund of an MPF scheme was a party to the transfer.

BACKGROUND AND ARGUMENT

Mandatory Provident Fund Schemes

2. Under the Mandatory Provident Fund Schemes Ordinance, the entire working population of Hong Kong, except the exempted categories, are required to join MPF schemes registered with the Mandatory Provident Fund Schemes Authority (the MPF Schemes Authority).

3. An MPF Scheme is governed by a trust and provides for the

payment of pecuniary benefits to members of the scheme when they reach the retirement age of 65 or on the occurrence of early retirement, total incapacity, permanent departure from Hong Kong, or death in which case payment is made to the personal representatives. Contributions made into an MPF scheme will be invested to generate profits or income which will be accrued to the scheme members' beneficial interest. Most of the constituent funds (CFs) of the MPF schemes will be unitised to facilitate the accounting of investment profits and losses. The CFs of an MPF scheme may maintain an internal investment portfolio or invest in approved pooled investment funds (APIFs).

4. There will be a number of MPF schemes operated by trustees approved by the MPF Schemes Authority. It is the responsibility of an employer to enroll employees in an MPF scheme chosen by the employer. An MPF scheme may consist of one or more CFs, which may be unitised, each with its distinct investment policy to be offered as investment options. A scheme member may choose to switch funds from one CF to another CF. Upon the change of employment, an employee can choose to transfer his funds from the MPF scheme under his previous employer into the scheme of his new employer or a scheme chosen by the employee himself. If the scheme of his previous employer is a master trust scheme, the employee may also remain with the master trust scheme with accrued benefits switched from his employer account to his individual account. The Mandatory Provident Fund Schemes Ordinance requires that all MPF schemes, including the underlying unit trusts, be governed by the laws of Hong Kong.

Stamp Duty Requirements Applicable to MPF Schemes

5. Under the Ordinance, a “unit trust scheme” is defined as any arrangements made for the purpose of providing persons having funds available for investment with facilities to participate, as beneficiaries under a trust, in any profits or income arising from the acquisition, holding, management or disposal of any property relevant to the investments.

6. Under the Ordinance, contract notes in respect of sale and purchase of “units” in “unit trusts” are chargeable to the *ad valorem* stamp duty, currently at the rate of 0.1125% on each note, under head 2(1) in the First Schedule. An instrument of transfer of the units executed to complete the sale and purchase is chargeable with a fixed stamp duty, currently at $5 per instrument of transfer, under head 2(4) in the same Schedule. A redemption of a unit in a unit trust, in which a person authorizes or requires the trustees or managers of the unit trust to treat him as no longer interested in the unit and does not authorize them to treat another person as so entitled, is deemed to be a transfer of the unit to the managers by way of sale under section 30(4). The instrument giving such authorization or making such request or its substitution instrument is deemed to be an instrument of transfer chargeable with a fixed stamp duty of $5 under head 2(4) of the First Schedule. However, section 19(1A)(a) exempts the sale of units back to the unit trust or the fund manager by the unit holders on redemption from the requirements of making and stamping contract notes where such sales and purchases are effected by extinguishing the units affected. Despite this, the instrument effecting such transfer back is still chargeable with the fixed stamp duty of $5.

7. Direct allotment of units by a unit trust to unit holders is neither a sale and purchase nor a transfer of units. It is thus not subject to both the *ad valorem* or the fixed stamp duty. Nevertheless, there are practices in the market that the units are allotted by a unit trust to the fund managers who will keep the units in a “manager box” for a while before issuing the units to investors. Strictly speaking, the issuing of units from the “manager box” to investors is a transfer of existing units on sale by the manager and is subject to both the fixed stamp duty (on the instrument of transfer) and *ad valorem* stamp duty (on the contract notes). Section 19(1A)(b)(ii), however, exempts the requirement to make contract notes and thus the charge of *ad valorem* stamp duty on such indirect allotment of units. The fixed stamp duty though is still payable on the transfer instrument.

8. All the transfer instruments referred to in paragraphs 6 and 7 above are required under section 19(8)(b)(ii) of the Ordinance to be endorsed as not chargeable with *ad valorem* stamp duty in order to become a duly stamped instrument which can be received in evidence in civil proceedings and can be acted upon, filed or registered by public officers and body corporates. In other words, a unit cannot be transferred legally unless the transfer instrument has been so endorsed.

9. Both the CFs under an MPF scheme and the APIF in which the CFs are invested fall within the definition of a unit trust scheme under the Ordinance. There are six types of unit transfers which will take place amongst the CFs, the APIF, the MPF scheme participants and fund managers under an MPF scheme. Of these six types of unit transfers, four

_ (B, C, E and F in the table below) are subject to specific stamping requirements under the Ordinance. The purposes underlying these transfers and the relevant stamping requirements are set out below:

Transfer	Events/Instruments	Major underlying objectives	Stamp duty requirements
A	Direct allotment of units by CFs to the scheme members	Investment in the CFs	Not a transfer, nor a sale or purchase, hence not chargeable with stamp duty at all
B*	Indirect allotment of units by the CFs through the fund managers	Common investment practice of unit trusts in the market whereby units are alloted by CFs to the fund managers who will keep the units for a while before issuing them to investors, i.e. the employees or self-employed MPF scheme members	• Transfer of units by the fund managers to the scheme member on an indirect allotment is chargeable with the fixed stamp duty of $5 under head 2(4) of the First Schedule • *Ad valorem* stamp duty exempted under section 19(1A)(b)(ii) • Transfer instrument to be endorsed by the Collector of Stamp Revenue as not chargeable with *ad valorem* stamp duty, under section 19(8)(b)(ii)
C*	Redemption of units in CFs by scheme members	• Retirement of employees or self-employed scheme members • Switching of scheme	• Deemed to be a transfer by way of sale, hence liable to the fixed stamp duty of $5 under head 2(4) of the First

		member's interest from one MPF scheme to another MPF scheme upon changes of employment or changes of investment preference	Schedule • *Ad valorem* stamp duty exempted under section 19(1A)(a) • Transfer instrument to be endorsed by the Collector of Stamp Revenue as not chargeable with *ad valorem* stamp duty, under section 19(8)(b)(ii)
D	Direct allotment of units by the APIFs to the CFs	• Investment of the CF in the APIF	Not a transfer, nor a sale or purchase, hence not chargeable with stamp duty at all
E*	Indirect allotment of units by the APIFs to the CFs through the fund managers	Common investment practice of unit trusts in the market whereby units are alloted by APIF to the fund managers who will keep the units for a while before issuing them to investors, i.e. the CF	• Indirect allotment of units by the APIFs to CFs through fund managers will be chargeable as a transfer and liable to the fixed stamp duty of $5 under head 2(4) of the First Schedule • *Ad valorem* stamp duty exempted under section 19(1A)(b)(ii)

			• Transfer instrument to be endorsed by the Collector of Stamp Revenue as not chargeable with *ad valorem* stamp duty, under

			section 19(8)(b)(ii)
F*	Redemption of units in APIFs by the CFs	• Redemption of underlying units held by a CF in the APIF to generate cash for payment to its beneficiaries (MPF scheme members) upon the latter's retirement or change of MPF schemes • To give effect to changes in the investment portfolio of a CF	• Deemed to be a transfer by way of sale, hence liable to the fixed stamp duty of $5 under head 2(4) of the First Schedule • *Ad valorem* stamp duty exempted under section 19(1A)(a) • Transfer instrument to be endorsed by the Collector of Stamp Revenue as not chargeable with *ad valorem* stamp duty, under section 19(8)(b)(ii)

*Note Unit transfers subject to specific stamping requirements under the Stamp Duty Ordinance.

Proposal and justifications

10. Given that around three million employees and self-employed persons will participate in the MPF schemes, we expect that the number of transfers arising from indirect allotment of units through fund managers, and redemption of units (i.e. transaction types B, C, E and F explained in paragraph 9 above) which may be executed in a year, will be huge.

11. Our preliminary estimate is that the total number of such MPF-

related transfers may involve 400 000 additional instruments a year (or some 1 500 documents a day), which amounts to 160% increase in the volume of transfers (both for charging the fixed stamp duty of $5 and endorsing the transfer instrument to be not chargeable with *ad valorem* duty) handled by the Stamp Duty Office in 1999-2000. The processing of these transfer documents involves cash or cheque collection, vetting, stamping and despatching documents. To enable the Stamp Duty Office to cope with this additional workload while continuing to deliver its stamping service according to its performance pledge (stamping to be performed within the same day), the Office will require at least two additional clerical staff and a new franking machine, while the estimated revenue gain will only be $2 million a year.

12. Separately, the stamping requirements in respect of the various unit transfer transactions will complicate the procedures involved in investment transactions under the MPF schemes, and add to the administrative burden of both the trustees and fund managers. Such extra administrative costs may be passed on to the MPF scheme members (i.e. the employees and self-employed persons), and hence reduce the amount of retirement benefits eventually available to them.

13. In view of the above, we propose to exempt the following types of unit transfers from the requirement to pay the fixed stamp duty of $5 per transfer instrument and the requirement to submit the instrument of transfer to the Collector of Stamp Revenue for endorsement to the effect that it is not chargeable with *ad valorem* stamp duty:

a) indirect allotment of units by the CFs under the MPF schemes to the

MPF scheme members through the fund managers (transaction type B in para 9);

b) redemption of units in CFs by MPF scheme members (transaction type C in para 9);

c) indirect allotment of units by the APIFs to the CFs under the MPF schemes through the fund managers (transaction type E in para 9); and

d) redemption of units in APIFs by the CFs under the MPF schemes (transaction type F in para 9).

THE BILL

14. **Clause 1** specifies the title and commencement of the Bill. **Clause 2** adds a new section 47A to exempt the stamp duty chargeable on a transfer or redemption of units at the CF and APIF levels. **New section 47A(1)** deals with **transaction type B** in paragraph 9 above. **New section 47A(2)** deals with **transaction type E** in paragraph 9. **New section 47A(3)** deals with **transaction type C** in paragraph 9. **New section 47A(4)** deals with **transaction type F** in paragraph 9. **Clause 3** updates the First Schedule to the Ordinance in the light of the proposed amendments.

LEGISLATIVE TIMETABLE

15. The legislative timetable for the Bill is -

Publication in the Gazette	5 October 2000
First Reading and commencement of Second Reading debate	18 October 2000
Resumption of Second Reading debate, committee stage and Third Reading	to be notified

BASIC LAW IMPLICATIONS

16. The Department of Justice advises that the proposed legislation is consistent with the Basic Law.

HUMAN RIGHTS IMPLICATIONS

17. The Department of Justice advises that the proposed legislation has no human rights implications.

BINDING EFFECT OF THE LEGISLATION

18. The Bill will not affect the current binding effect of the Ordinance.

FINANCIAL AND STAFFING IMPLICATIONS

19. Assuming that the implementation of the MPF schemes will generate an additional 400 000 transfers in respect of indirect allotment and redemption of units each year, the revenue forgone as a result of the proposal to exempt the fixed stamp duty of $5 per transfer would be about $2 million a year. On the other hand, the proposal would give rise to a notional savings of $552,000 in recurrent expenditure, being the additional staff cost, which may otherwise have to be incurred by the Stamp Duty Office of Inland Revenue Department to cope with the additional workload. The proposed lifting of the stamping requirement will not have any staffing implications.

ECONOMIC IMPLICATIONS

20. Smooth transfer of units in investment funds in relation to MPF schemes, involving the minimum administrative handling, is a pre-requisite for the effective operation of the MPF system. The proposed measures will contribute substantively to this end, to the benefit of the MPF scheme contributors and hence a very broad spectrum of the local community.

PUBLIC CONSULTATION

21. The proposals to exempt the fixed stamp duty and lift the stamping requirement in respect of transfers of units of CFs relating to the MPF schemes have the support of the Hong Kong Investment Funds Association, whose members will play an active role in MPF scheme fund management. Since the proposal will benefit MPF scheme members, fund managers and their trustees, we do not consider it necessary to consult them.

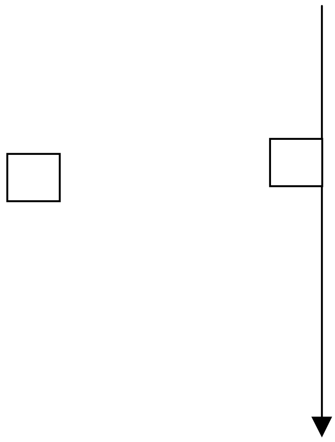
PUBLICITY

22. We will issue a press release on 4 October 2000.

ENQUIRIES

23. In case of enquiries about this Brief, please contact Ms Esther Leung, Principal Assistant Secretary for the Treasury (Revenue), at 2810 2370.

Finance Bureau
FIN R 43/5/136
29 September 2000



Annex

A BILL

To

Amend the Stamp Duty Ordinance.

Enacted by the Legislative Council.

1. Short title and commencement

(1) This Ordinance may be cited as the Stamp Duty (Amendment) Ordinance 2000.

(2) This Ordinance shall come into operation on 1 December 2000.

2. Section added

The Stamp Duty Ordinance (Cap. 117) is amended by adding in Part V -

"47A. Instruments of transfer of units under mandatory provident fund schemes to be exempt

(1) An instrument of transfer of a unit under a unit trust scheme is not chargeable with stamp duty if -

(a) the scheme is a constituent fund of a registered scheme;

(b) the unit is transferred by the manager of the fund to a person who is, or intends to be, a scheme member of the registered scheme; and

(c) the power of the manager to effect the transfer arises otherwise than from a previous transfer to him of that or some other unit.

(2) An instrument of transfer of a unit under a unit trust scheme is not chargeable with stamp duty if -

(a) the scheme is an approved pooled investment fund;

(b) the unit is transferred by the manager of the fund ("fund manager") to the trustee or manager of a constituent fund of a registered scheme; and

(c) the power of the fund manager to effect the transfer arises otherwise than from a previous transfer to him of that or some other unit.

(3) Where a person is deemed under section 30(4) to transfer a unit under a unit trust scheme, then if -

(a) the scheme is a constituent fund of a registered scheme; and

(b) such deemed transfer is effected by extinguishing the unit,

the instrument that is deemed under that section to be a transfer of the unit is not chargeable with stamp duty.

(4) Where the trustee or manager of a constituent fund of a registered scheme is deemed under section 30(4) to transfer a unit under a unit trust scheme, then if -

(a) the unit trust scheme is an approved pooled investment fund; and

(b) such deemed transfer is effected by extinguishing the unit,

the instrument that is deemed under that section to be a transfer of the unit is not chargeable with stamp duty.

(5) In this section -

"approved pooled investment fund" (核准匯集投資基金) has the same meaning as in section 2 of the Mandatory Provident Fund Schemes (General) Regulation (Cap. 485 sub. leg.);

"constituent fund" (成分基金) has the same meaning as in section 2 of the Mandatory Provident Fund Schemes (General) Regulation (Cap. 485 sub. leg.);

"registered scheme" (註冊計劃) has the same meaning as in section 2(1) of the Mandatory Provident Fund Schemes Ordinance (Cap. 485);

"scheme member" (計劃成員) has the same meaning as in section 2(1) of the Mandatory Provident Fund Schemes Ordinance (Cap. 485).".

3. First Schedule amended

The First Schedule is amended in head 2(4) by repealing "and 30" and substituting ", 30 and 47A".

Explanatory Memorandum

The purpose of this Bill is to amend the Stamp Duty Ordinance (Cap. 117) to exempt the stamp duty chargeable on a transfer of units when the units are issued or redeemed if a constituent fund of a mandatory provident fund scheme is a party to the transfer.