CHAPTER 3

SHARES, DEBENTURES, CAPITAL MAINTENANCE, SCHEMES OF ARRANGEMENT, COMPULSORY ACQUISITIONS AND AMALGAMATIONS

I. INTRODUCTION

1 The provisions reviewed under this section relate to capital maintenance and shares, debentures, schemes, compulsory acquisitions and amalgamations.

2 The Steering Committee has reviewed the relevancy of the legal concepts connected to the above said areas in the present business environment, sought to streamline and update the Companies Act in the light of evolving accounting standards and practices and enable companies to design appropriate capital structures which best suit their needs, while providing adequate safeguards and transparency.

II. PREFERENCE AND EQUITY SHARES

(a) Definition of "preference shares"

3 Section 4 of the Companies Act has a definition of "preference shares". Although in commercial practice preference shares may be voting and/or participating, the Companies Act states that ""preference share", in relation to sections 5, 64 and 180 means a share, by whatever name called, which does not entitle the holder thereof to the right to vote at a general meeting (except in the circumstances specified in section 180(2)(a),(b) and (c)) or to any right to participate beyond a specified amount in any distribution whether by way of dividend, or on redemption, in a winding up, or otherwise."

4 The section 4 definition applies only to sections 5, 64 and 180 of the Companies Act. However there are also references to preference shares in other parts of the Companies Act such as section 74 and 75, to which the commercial understanding of the term would apply. A number of difficulties arise from this inconsistent use of the term "preference share".

5 The Australian, New Zealand and UK legislation do not have a statutory definition of preference shares. Whilst the phrase "preference shares" can be found in the Australian legislation, it is completely absent from the New Zealand Companies Act 1993 and UK Companies Act 2006. The provisions in the Australian, New Zealand and UK legislation which are parallel to sections 5 and 64 of the Singapore Companies Act do not exclude "preference shares". There is no direct equivalent of section 180(2) in Australia, New Zealand and the UK. Instead preference shares would presumably be a class of shares to which the general provisions on classes of shares would apply.

6 In view of the above, the Steering Committee is of the view that the definition of "preference share" should be deleted. Consequential amendments which will be required for sections 5, 64 and 180 (to which the section 4 definition currently applies) are set out in the following paragraphs.

7 When consulted, there were no opposing views received.

Recommendation 3.1

The definition of "preference share" in section 4 should be deleted.

(b) Voting rights of holders of preference shares

8 Section 180(2) of the Companies Act states that holders of preference shares shall have the right to at least one vote per share if (i) preferential dividends are in arrears for 12 months or such shorter period as the Articles provide; (ii) upon any resolution to vary the rights attached to those share; or (iii) upon any resolution for winding up.

9 It is the recommendation of the Steering Committee that a company should have the latitude to determine what rights attach to shares issued by the company and there is no cogent reason for the mandatory prescription of the rights of preference shares in the Act. The rights that attach to preference shares can be set out in the Articles. There is no direct equivalent of section 180(2) in Australia, New Zealand or the UK. Section 180(2) should be deleted.

10 When consulted, most respondents agreed with the recommendation. The Steering Committee recommends transitional arrangements to preserve the rights currently attached under section 180(2) to preference shares issued before the proposed amendment.

Recommendation 3.2

Section 180(2) should be deleted. Transitional arrangements should be made to preserve the rights currently attached under section 180(2) to preference shares issued before the proposed amendment.

(c) Definition and use of the term "equity share"

11 Section 4 of the Companies Act currently defines "equity share" to mean "any share which is not a preference share." There is no such term in the Australian or New Zealand legislation. The term "equity share capital" is used in the UK Companies Act 2006 and is defined at section 548 as "its issued share capital excluding any part of that capital that, neither as respects dividends nor as respects capital, carries any right to participate beyond a specified amount in a distribution".

12 To be consistent with the recommendation that the definition of "preference share" should be deleted, the Steering Committee is of the view that the definition of "equity share" as "any share which is not a preference share" should also be deleted. When consulted, most of the respondents agreed to the recommendation.

Recommendation 3.3

The definition of "equity share" be removed and "equity share" be amended to "share" or some other appropriate term wherever it appears in the Companies Act.

(d) Non-voting/multiple vote shares

13 Section 64(1) of the Companies Act provides that each equity share issued by a public company confers the right at a poll to one vote, and to one vote only. This differs from other major jurisdictions like the UK, New Zealand and Australia. The UK and New Zealand both statutorily confer shareholders a right to vote but this is subject to the Articles. Australia also allows the issue of non-voting shares; although the Australian Securities Exchange (ASX) Listing Rules requires listed shares to carry a vote, changes to this are being considered so that listed companies can issue non-voting shares.

14 The Steering Committee considered if the law should be amended to allow public companies to issue non-voting shares (other than preference shares as currently defined under section 4 of the Companies Act) and shares carrying multiple votes. When consulted, most of the respondents agreed that public companies should be allowed to issue non-voting shares or shares with multiple votes, subject to certain safeguards. This would allow companies greater flexibility in capital management. The Singapore Exchange may determine whether listed companies should be allowed to issue such shares.

15 The proposed safeguards are:

(a) Subject the issue of shares with differential voting rights (particularly super-voting shares) to a higher approval threshold, such as special resolution rather than ordinary resolution. The UK requires super majority for super-voting shares and simple majority for non-voting shares.

(b) Holders of non-voting shares should be accorded equal voting rights for a resolution to wind up the company or a resolution which varies the rights of the non-voting shares.

(c) Where there is more than one class of shares, the notice of a meeting at which a resolution is proposed to be passed should be accompanied by an explanatory statement setting out the voting rights (or the lack thereof) attached to each class of shares.

16 However, a minority of the respondents who did not support the proposal cited the risk of undermining minority rights and compromising standards of corporate governance. It was also commented that the UK, New Zealand and Australian markets are distinct from ours. In markets like ours with companies predominantly controlled by a group of shareholders, non-voting shares and shares with multiple rights can be used to severely undermine minority interests. The Steering Committee notes these views but opines that the necessary safeguards and restrictions should be imposed on the listed companies under the

applicable rules imposed solely on listed companies. Hence section 64 should be removed entirely.

Recommendation 3.4

Companies should be allowed to issue non-voting shares and shares with multiple votes.

Recommendation 3.5

Section 64 should be deleted.

III. HOLDING AND SUBSIDIARY COMPANIES

(a) Amend the definition of "subsidiary"

17 Section 5 of the Companies Act defines when one corporation is a subsidiary of another. Section 5(1)(a)(iii) deems a corporation to be a subsidiary of another corporation if that other corporation "holds more than half of the issued share capital of the first-mentioned corporation (excluding any part thereof which consists of preference shares and treasury shares)".

18 By comparison, section 46 of the Australia Corporations Act 2001 excludes not preference/treasury shares but "any part of that issued share capital that carries no right to participate beyond a specified amount in a distribution of either profits or capital". Similarly section 5(1)(iii) of the New Zealand Companies Act 1993 excludes not preference/treasury shares but "shares that carry no right to participate beyond a specified amount in a distribution of either profits or capital".

19 There is no comparable UK provision. The definition of "subsidiary" in the UK Companies Act 2006 is at section 1159. In short, the UK recognise "control" rather than percentage of shareholding which determines a holding/subsidiary relationship. During consultation, the UK position was examined in greater depth.

20 The Steering Committee recommends that section 5(1)(a)(iii) be deleted. The section 5(a)(iii) definition can be traced back to the requirement for consolidation of accounts, which should be set only by financial reporting standards. The definition of "subsidiary" in the Companies Act should not be the determining factor for consolidation. Instead, section 5(1)(a) should be amended to recognize that a company S is a subsidiary of another company H if company H holds the majority of the voting rights in company S. This would bring the Singapore position in line with the UK to recognize director control, control through voting agreements and voting control to determine whether one company is the subsidiary of another.

<u>Recommendation 3.6</u>

Section 5(1)(a)(iii) should be deleted. Section 5(1)(a) should be amended to recognize that a company S is a subsidiary of another company H if company H holds a majority of the voting rights in company S.

(b) Subsidiary holding shares of its holding company

21 Section 21(4) of the Companies Act requires that a subsidiary "shall, within the period of 12 months or such longer period as the Court may allow after becoming the subsidiary of the holding company, dispose of all its shares in the holding company".

22 Treasury shares now being permitted, the Steering Committee initially considered allowing the shares held by a subsidiary in its holding company to be deemed treasury shares. This was supported by majority of the respondents consulted. However, comments were received that this may be unfair. As treasury shares are not entitled to receive dividends, a minority shareholder in the subsidiary that is not wholly-owned would realize a loss in value associated with its shareholding in the subsidiary through no fault of his own. One further query was whether the Act would provide guidance as to the timeline for disposal of any shares in excess of the 10% threshold.

23 The Inland Revenue Authority of Singapore ("IRAS") commented that treasury shares held by a holding company are accounted for differently when held by its subsidiary. Hence there is a possibility that investors may be misled when reading the financials. The Steering Committee took the view that this can be resolved by further disclosures in the financials if necessary.

24 After due consideration, the Steering Committee recommends retaining the current 12-month time-frame for a subsidiary to dispose of shares in its holding company and only convert the shares held to treasury shares thereafter. Once these shares are converted to treasury shares, they would be regulated in accordance with the rules governing treasury shares, which means the maximum holding is 10% of the total number of shares in that class at that time. The subsidiary would have to dispose of shares in excess of the 10% threshold within 6 months under section 76I(3).

25 In addition, section 21(4) should be amended to allow retention of up to an aggregate 10% of such treasury shares. This means if company X acquires another company Y which owns company X's shares, those company X shares owned by company Y should be aggregated with all other company X shares owned by company X (be it through X or X's subsidiaries) in order to determine the 10 % limit. Otherwise, there may be a situation where company X may own a very substantial amount of its own shares (either directly or through subsidiaries). When consulted, most respondents agreed.

26 The position in Australia (section 259D of the Australia Corporations Act 2001) is similar to that in Singapore. In the UK (section 136 of the UK Companies Act 2006) and

New Zealand (section 82(1) of the New Zealand Companies Act 1993) also, the general rule is that a subsidiary may not hold shares in its holding company. However, section 82(4) of the New Zealand Companies Act 1993 provides that "where a company that holds shares in another company becomes a subsidiary of that other company — The company may … continue to hold those shares".

Recommendation 3.7

The current 12-month time-frame for a subsidiary to dispose of shares in its holding company should be retained. Such shares will be converted to treasury shares thereafter. Once these shares are converted to treasury shares, they would be regulated in accordance with the rules governing treasury shares.

Recommendation 3.8

Section 21(4) should be amended to allow retention of up to an aggregate 10% of such treasury shares, taking into account shares held both by the company as well as its subsidiaries.

IV OTHER ISSUES RELATING TO SHARES

(a) Redenomination of shares

27 Currently the Companies Act does not specify a mechanism for redenomination of capital and where such redenomination involves a capital reduction, court sanction would be required. The position is similar in Australia and New Zealand where no statutory mechanism for redenomination is prescribed.

28 In the UK, a comprehensive procedure in respect of redenomination of share capital by shareholder resolution has been introduced with the new Companies Act 2006 (sections 622 to 628) and has taken effect on 1 October 2009. In short, the law provides that a limited company may redenominate its share capital and the conversion must be made at an appropriate spot rate of exchange specified in the resolution. There are prescribed rules on when to ascertain the rate of exchange, calculation of the new nominal value, effect of redenomination, and notification to authorities and the creation of a redenomination reserve. A special resolution is required if the redenomination involves a reduction in capital.

29 The Steering Committee considered if Singapore should introduce a statutory mechanism for denomination of shares similar to the UK model. When consulted, most respondents agreed. Alternate views received however queried if the suggestion was relevant to Singapore as the change in the UK may be prompted by the UK joining the European Union thereby allowing the redenomination of pound to euro. The Steering Committee is of the view that it is common for companies with foreign businesses to re-denominate their share structure and hence the statutory mechanism will be useful and provides greater certainty.

<u>Recommendation 3.9</u>

A statutory mechanism for redenomination of shares similar to the UK provisions, with appropriate modifications, should be inserted into the Companies Act.

(b) Interest in shares

30 The definition of "interest in shares" at section 7 of the Companies Act differs from the definition of "interest in securities" at section 4 of the Securities and Futures Act (SFA). The section 7 definition does not include similar wording to sections 4(1) and 4(2) which deems a person who has the right to dispose of securities as having an interest in those securities.

31 Under section 146 of the New Zealand Companies Act 1993, the director's right to dispose of shares confers a 'relevant interest' in those shares. Section 608(1) of the Australia Corporations Act 2001 extends relevant interests in securities to any person who has the power to dispose of the securities or control the exercise of the power to dispose of the securities. The UK Companies Act 2006 adopts a similar policy though it uses different wording[1].

32 The Steering Committee is of the opinion that amending the definition in the Companies Act to make it consistent with that in the SFA would not have any unintended consequences on the provisions in the Companies Act which refer to an "interest in shares". Although "interest in shares" is more applicable for listed companies, there is merit to align the definition in both Acts for greater consistency. When consulted, most respondents agreed with the Steering Committee's views. Those in support further commented that the proposed change would more accurately reflect the concept of share ownership as understood by most investment managers, who consider themselves to be shareholders if they have the right to dispose of shares in a company regardless of the existence or absence of any other rights like voting rights. The definition of "interest in shares" should also be reconsidered in light of present day brokerage services and banking activities. However, the law should not require multiple disclosures by companies which are deemed to have an interest in shares beyond certain levels.

<u>Recommendation 3.10</u>

Section 7 of the Companies Act should be amended to be consistent with section 4 of the SFA.

[1] See Schedule 1 of the UK Companies Act 2006.

(c) Economic interests in shares

33 In the UK, after a public consultation, on 2 July 2008 the Financial Services Authority (FSA) announced plans to implement a general disclosure regime of long Contracts for Difference (CfD) positions. However, since the FSA reached its decision after extensive research on conditions in the UK market, the conclusions may not be directly applicable to the Singapore environment.

34 In the FSA Consultation Document, the position in other jurisdictions was also considered. In relation to Australia it was stated:

> "Australia requires disclosure of substantial holdings in shares or interests in a listed company. 'Relevant interest' is defined in section 608 of the Corporations Act 2001 and includes the power to exercise, or control the exercise of, a right to vote attached to the securities. It is understood that purely cash settled derivatives generally do not fall within the definition of 'relevant interest', while the disclosure obligation in such a case would lie with the investment bank holding the hedge.
>
> The Australian Takeover Panel recently outlined its plans to prohibit the use of equity derivatives to mask the ownership of takeover targets, in response to several high-profile cases. The Panel said it had developed the draft guidance over two years following numerous instances where controlling interests had used equity derivatives to hide 'substantial holdings'. The central proposition is that for control and substantial holding disclosure purposes long equity derivatives (cash settled or deliverable) should be treated in the same way as physical holdings of the relevant securities. These proposals would apply to all derivative holdings, not just in takeover situations."

35 On 11 April 2008, the Australian Takeovers Panel (Panel) released Guidance Note 20 - Equity Derivatives outlining when, and in what circumstances, the use of equity derivatives may constitute unacceptable circumstances and require disclosure to the market. In short, the Guidance Note indicates that disclosure is required where (i) there is a "long position" in existence or created; (ii) there is a "control transaction"; and (iii) the "long position" relates to 5% or more of an ASX listed company's voting securities.

36 The New Zealand position was described in the FSA Consultation Document as follows:

> "New Zealand requires disclosure of 'relevant interests' in 5% or more of the voting securities of a public issuer. According to article 5 of the Securities and Markets Act, a person has a 'relevant interest', amongst other criteria, if that person: (i) has the power to exercise (or control) any right to vote attached to the security; (ii) has the power to acquire or dispose the security; or (iii) has the power (or may at any time have the power) under an arrangement, to exercise any right to vote attached to the security, to acquire or dispose of the security. The courts have taken a broad approach to what represents a possible future power to acquire shares."

37 The Steering Committee is of the opinion that in Singapore, it would be premature to recognise economic interests as being an "interest in shares". Developments overseas should

be monitored and it may be considered later whether such a step is warranted. When consulted, most respondents agreed with the Steering Committee's views.

Recommendation 3.11

Section 7 need not be amended to bring economic interests in shares within the definition of "interest in shares" at this point.

(d) Exemption under section 63(1A)

38 Section 63(1)(d) of the Companies Act requires a company to lodge a return of allotment within 14 days of allotment, stating the full name, identification, nationality and address of each member, and the number and class of shares held; or if there are more than 50 members as a result of the allotment, each of the 50 members who, hold the most number of shares in the company (excluding treasury shares). This was introduced in 2003; previously disclosure was not limited to the top 50 members. Section 63(1A) of the Companies Act exempts a company whose shares are listed on a stock exchange in Singapore from section 63(1)(d). This was also introduced in 2003 as shares of such companies are traded daily and compliance with this requirement would be onerous.

39 Representations were received that some countries such as the USA or certain European states have privacy laws which protect their citizens' right to non-disclosure of their personal identification details. As a result, Singapore companies listed in such countries face difficulties in compelling disclosure of such information. However to date, ACRA has not received any conclusive evidence that it is impossible to comply with our laws.

40 Like Singapore, the UK formerly required the shareholders' details to be reported but this was abolished in October 2009[2]. Australia (section 254X of the Corporations Act 2001) and New Zealand (section 43 of the New Zealand Companies Act 1993) only require reporting of details of shares issued.

41 The respondents consulted were in favour of leaving the exemption under section 63(1A) to the Registrar's discretion, as a sweeping exemption might go too far. The respondents are of the opinion that it would be preferable to exempt only foreign exchanges with comparable investor protection laws. Contrary to the comments received, the Steering Committee recommends an extension of the exemption under section 63(1A) to all listed companies, wherever listed. The reasons are (1) the information in section 63(1)(d) is from the Register of Members which is open to public inspection and so there should be no difficulty for anyone who is interested to obtain the information from the company register in any case; and (2) it is in line with the vision of Singapore to be a trusted place for business, hence there should not be a distinction drawn between the information available on Singapore-listed and foreign-listed Singapore companies. As for the concern that a sweeping exemption goes too far and only certain foreign exchanges with credible investor protection laws should be recognised, it would be difficult to draw up such a list.

[2] UK's "The Companies (Shares and Share Capital) Order 2009" has come into effect from 1 October 2009 and there will no longer be any requirement for shareholders' details to be reported.

Recommendation 3.12

The exemption afforded under section 63(1A) should be extended to all listed companies, wherever listed.

(e) Introduction of a carve-out for reporting of share issuances pursuant to shareholder-approved equity-based employee incentive plans

42 Related to the above, another proposal was to amend section 63(1) of the Companies Act to replace the 14-day reporting timeline with quarterly reporting (on an aggregate basis) of all shares allotted and issued during each financial quarter where the allotment takes place under equity-based incentive plans pursuant to which shares are issued to employees and other service providers of issuers, subject to the following conditions:

(a) the total number of shares allotted and issued pursuant to the equity-based incentive plans during any financial year does not cumulatively exceed 15% of the total number of issued shares in the capital of the company as disclosed in the last annual return of the company;

(b) the aggregate number of employee-plan shares allotted and issued must be notified to ACRA, on a cumulative bulk basis, within 45 days from the end of each financial quarter; and

(c) the batch report would have to permit reporting the consideration received on a weighted-average basis for the batch, rather than based upon the individual issuances within the batch[3].

43 The argument in favour of this is that companies listed in the USA would have complied with the reporting requirements under US securities laws and these are publicly available and provide sufficiently meaningful information to investors. In any case, members of the public and shareholders also have access to the register of members which will allow them to ascertain the identities of all shareholders and their shareholdings.

44 Australia, the UK and New Zealand do not have a similar concept.

45 Mixed views were received from the respondents during consultation. After consideration, the Steering Committee recommends to maintain status quo for section 63(1) to ensure greater transparency and prompt reporting.

[3] By way of illustration, this translates to reporting the issuance of an aggregate of X shares in the period (ideally aligned with one fiscal quarter) for an aggregate consideration of $Y, or for a weighted average issuance price of $Z per share. The need to identify the individual allottee, personal identifiable information and the issue price per share on an issuance-by-issuance basis, as currently contemplated by section 63(1) of the Companies Act, will require modification.

<u>Recommendation 3.13</u>

Section 63(1) should not be amended to replace the 14-day reporting timeline with quarterly reporting (on an aggregate basis) of all shares allotted and issued during each financial quarter where the allotment takes place under equity-based incentive plans pursuant to which shares are issued to employees and other service providers of issuers.

(f) Definition of "share"

46 The definition of a "share" in section 4 of the Companies Act is similar to the UK definition except for the recognition of stocks as shares. New Zealand and Australia do not provide a basic definition of shares in their legislative equivalents. Australia relies on the common law to define shares[4]. However, section 2 of the New Zealand Securities Transfer Act 1991 does define shares to include options. Section 121 of the Companies Act goes on to clarify the nature of shares as "movable property", but the UK and New Zealand only refer to shares being "personal property" while Australia included an additional reference to shares as "personal property" which is transferable.

47 The Steering Committee is of the view that the differences in the definition of "share" and the nature of shares in the different jurisdictions do not lead to any difficulties and hence no change is required.

48 When consulted, there were no opposing views received.

<u>Recommendation 3.14</u>

Section 4 definition of "share" and section 121 which defines the nature of shares should not be changed.

(g) Dematerialisation of shares

49 By virtue of section 130(1) of the Companies Act a share certificate must be issued to the holder of shares within two months of an allotment or within one month of a transfer. Although Singapore has not dematerialised shares, immobilisation has been achieved for listed companies but shareholders still have the option of withdrawing listed company share certificates from the Central Depository Pte Ltd (CDP)[5]. This is administratively burdensome without any compensating benefit.

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[4] E.g. "A share is a type of contractual claim against a company. It is an example of intangible property called a 'chose in action' or 'thing in action'." Archibald Howie Pty Ltd v Commissioner of Stamp Duties (NSW) (1948) 77 CLR 143 at 154.

[5] Regulation 20 of the Companies (Central Depository System) Regulations states that "A depositor may, on application in writing to the Depository, withdraw any documents evidencing title relating to his book-entry securities that are standing to the credit of his account with the Depository."

50 In the UK, since the Uncertificated Securities Regulations came into effect in 2001, most shares have been dematerialised. Notably this was achieved by subsidiary legislation although the default position under the UK Companies Act 2006 is that share certificates should still be issued. In New Zealand, share certificates have been largely dematerialised[6]. In Australia, ASX listed shares have been dematerialised for about 10 years.

51 When consulted, most respondents agreed that Singapore should follow suit. SGX had no objections but commented that the Central Depository System should still be designated as the master register for listed companies. Some however is of the opinion that dematerialization should only be considered for public listed companies. For private companies, the certificates show evidence of ownership and may be needed by the shareholders who should be issued with share certificates. Also, fresh issues and transfers of shares are not likely to be so frequent for private companies, hence it is more cost efficient to retain share certificates. After consideration, the Steering Committee recommends dematerializing shares of public companies, but dematerialization shall not be mandatory at this point in time.

<u>Recommendation 3.15</u>

Shares of public companies should eventually be dematerialised but the law need not mandate such a requirement at this time.

(h) Central Depository System ("CDP") Provisions

52 In line with the aim of retaining only core company law in the Companies Act, the Steering Committee considered whether the provisions in the Companies Act which relate to the CDP should be extracted and inserted into other legislation.

53 When consulted, most respondents agreed that the CDP provisions should be extracted and migrated out of the Companies Act as it is not core company law.

54 The Steering Committee recommends that the CDP provisions be extracted and moved into a separate stand-alone Act.

<u>Recommendation 3.16</u>

The provisions in the Companies Act which relate to the CDP should be extracted and inserted into a separate stand-alone Act.

[6] They are only mandated for public companies whose shares cannot be transferred under an approved scheme which does not require a share certificate for transfer – presumably a small number given that New Zealand Securities Exchange's FASTER system can be so transferred.

V. DEBENTURES

55 Currently section 93 of the Companies Act requires every company which issues debentures (not being debentures transferable by delivery) to keep a register of holders of the debentures. The register is open to inspection by debenture holders and shareholders.

56 In the UK, maintenance of a register of debenture holders is not mandatory. However, if there is such a register then it is open for inspection not only by shareholders and debenture holders but also by any other person. The relevant provisions in the UK Companies Act 2006 are at sections 743 to 747.

57 The New Zealand Companies Act 1993 has only 3 sections (95A to 95C) on debentures – similar to sections 95 and 96 of the Singapore Companies Act. No register of debenture holders is mentioned. However, where debentures are secured, they would fall under the Personal Property Security Act 1999 effective from 1 May 2002. This does have a registration mechanism applicable if the creditor is not in possession of the security. The Australian legislation has no mention of a register of debenture holders.

58 The Steering Committee consulted on whether we should adopt the UK approach. There were mixed views received from the respondents. After review, the Steering Committee recommends no change to section 93 since there was no call to abandon the current regime. However, the current regime can be improved for better transparency. There is no reason that the register of debenture holders and trust deed should stand on a higher level of confidentiality than the register of members which is open to public inspection. In fact it will promote corporate transparency to allow public inspection, in particular for convertible debentures and debt restructuring deals.

Recommendation 3.17

Section 93 of the Companies Act on debentures should be retained. However the register of debenture holders and trust deed should be open to public inspection.

VI. SOLVENCY STATEMENTS

59 The Companies (Amendment) Act 2005 reformed the law on capital maintenance substantially. It introduced capital reductions without the necessity for court intervention, further liberalised financial assistance restrictions, permitted share buybacks and redemption of redeemable preference share from capital and introduced treasury shares. One of the safeguards introduced was the satisfaction of the requisite solvency test. The Steering Committee considered but is not persuaded that the capital maintenance regime should be entirely abolished in favour of solvency tests as a means to protect creditors. The Steering Committee acknowledges that this is a possible development in the longer term but is of the opinion that it is not necessary to adopt such a policy at present. Instead, the Steering Committee proposes the following refinements to further improve the capital maintenance regimes.

(a) Uniform solvency statement

60 Under section 7A of the Companies Act (which applies to financial assistance, redemption of preference shares and capital reduction) the test imposed on directors is:

"(a) that they have formed the opinion that, as regards the company's situation at the date of the statement, there is no ground on which the company could then be found to be unable to pay its debts;

(b) that they have formed the opinion —

(i) if it is intended to commence winding up of the company within the period of 12 months immediately following the date of the statement, that the company will be able to pay its debts in full within the period of 12 months beginning with the commencement of the winding up; or

(ii) if it is not intended so to commence winding up, that the company will be able to pay its debts as they fall due during the period of 12 months immediately following the date of the statement; and

(c) that they have formed the opinion that the value of the company's assets is not less than the value of its liabilities (including contingent liabilities) and will not, after the proposed redemption, giving of financial assistance or reduction (as the case may be), become less than the value of its liabilities (including contingent liabilities)."

61 Under section 76F(4) of the Companies Act (which applies to share buybacks) the test is that:

"(a) the company is able to pay its debts in full at the time of the payment and will be able to pay its debts as they fall due in the normal course of business during the period of 12 months immediately following the date of the payment; and

(b) the value of the company's assets is not less than the value of its liabilities (including contingent liabilities) and will not after the proposed purchase, acquisition or release, become less than the value of its liabilities (including contingent liabilities)."

62 The key reasons for a similar but non-identical solvency test, both in content and form, for buyback transactions was to provide a pro-business policy given the continuous nature of such transactions and to retain some consistency with the former test which the market was familiar and comfortable with. After review, the Steering Committee recommends that it is timely to consider an identical solvency test for all transactions. In addition, the requirement in the section 76F(4) test that the company should be "able to pay its debts in full at the time of the payment" is unduly onerous and rather hypothetical since most companies would hold non-cash assets which would have to be liquidated if they were to pay their debts. The amount that may be recovered in the event of such liquidation would be difficult to estimate. As such, the section 7A test is preferable to the section 76F(4) test. When consulted, most respondents agreed with the Steering Committee. One alternative view was the solvency tests in section 7A are in principle more onerous than section 76F(4), though in practice the differences are likely to amount to little.

63 The UK solvency statement under section 643 of the UK Companies Act 2006 is similar to section 7A of the Singapore Companies Act but it does not include an equivalent of section 7A(1)(c). The New Zealand solvency test at section 4 of the New Zealand Companies Act 1993 requires that the company should be able to pay its debts as they become due and should have assets exceeding its liabilities. There is no comparable Australian provision.

Recommendation 3.18

One uniform solvency test should be applied for all transactions (except amalgamations).

Recommendation 3.19

Section 7A solvency test should be adopted as the uniform solvency test and be applied to share buybacks (replacing section 76F(4)).

(b) Declaration, not statutory declaration

64 Currently section 7A(2) of the Companies Act requires that the solvency statement should be in the form of a statutory declaration. Section 7A(2)(b) provides an alternative to the statutory declaration requirement – it provides that a company which is subject to audit requirements may use a solvency statement which is not in the form of a statutory declaration if accompanied by a report from its auditors that the statement is not unreasonable. Similarly, as part of the amalgamation process, various solvency statements are required to be made by way of a statutory declaration (sections 215I(2) and 215J(1) of the Companies Act).

65 In practice, directors are very reluctant to sign statutory declarations because of the perceived implications under the Oaths and Declarations Act. Auditors are also apparently unwilling to provide a report in accordance with section 7A(2)(b) probably due to the forward-looking nature of the solvency statement.

66 The Steering Committee is of the view that it would not be pro-business to impose statutory declarations. A normal declaration could still be subject to adequate criminal sanctions under section 402 of the Companies Act if it is false. When consulted, most respondents agreed with the Steering Committee.

67 Section 643 of the UK Companies Act 2006 on solvency statements does not require a statutory declaration and neither do the relevant New Zealand provisions like section 52(2) or 70(2) where the directors are only required to sign a certificate. There is no comparable Australian provision. In view of the above, the Singapore requirement for statutory declarations should be done away with. Section 157 of the Companies Act on directors' duties and section 401(2) of the Companies Act on misleading statements should be adequate to police solvency statements.

<u>Recommendation 3.20</u>

Solvency statements under sections 7A(2), 215(2) and 215J(1) should be by way of declaration rather than statutory declaration.

(c) Solvency statement by the Board of Directors

68 The solvency statement required under sections 70(4)(a), 76(9A)(e), 76(9B)(c), 78B(3)(a) and 78C(3)(a) of the Companies Act require the approval of "all the directors" of the company. However, companies normally operate by majority vote of the Board of Directors. It is therefore anomalous to require the approval of "all the directors" for a transaction. Also, in practice, the requirement can be defeated by some directors resigning and rejoining after the formalities have been executed. The Steering Committee considered if the requirement for all directors to approve the solvency statement can be simplified.

69 In New Zealand, it is the board that must be satisfied that the solvency test is satisfied and only the directors who vote in favour of the corporate action need sign the certificate (see eg sections 52 and 70 of the New Zealand Companies Act 1993). However, the UK solvency statement as defined at section 643 is a statement by "each of the directors". There is no comparable Australian provision.

70 When consulted, majority of the respondents agreed that solvency statements should only require the approval from the board of directors, rather than all directors. However, the minority which disagreed (including MAS) preferred that the status quo be retained. Their reasons were that the making of solvency statements should not be regarded as part of the ordinary business of the company where a majority vote will suffice. The unwillingness of one or more directors to sign the solvency statement calls into question the veracity of the statement. It is unlikely that directors of listed companies will try to circumvent the requirements in the manner highlighted, as their resignation/or re-appointment will have to be disclosed and subject to public scrutiny. Also, having all the directors make the solvency statement provides better protection for the creditors. In view of the fact that our wrongful-trading provisions present more obstacles for creditors to seek redress than those found in other jurisdictions, a more stringent approach should be taken in relation to the declaration of solvency. After review, the Steering Committee was persuaded that the present position should remain.

<u>Recommendation 3.21</u>

There should be no change to the requirement for all directors to make the solvency statements under sections 70(4)(a), 76(9A)(e), 76(9B)(c), 78B(3)(a), and 78C(3)(a).

VII. SHARE BUYBACKS AND TREASURY SHARES

(a) Relevant period for share buybacks

71 Whilst a company may now acquire its own shares, section 76B of the Companies Act specifies a cap on such share buybacks. Section 76B(3) states that "The total number of ordinary shares and stocks that may be purchased or acquired by a company during the relevant period shall not exceed 10% … ".

72 The "relevant period" is defined in section 76B(4) as "the period commencing from the date the last annual general meeting of the company was held or if no such meeting was held the date it was required by law to be held before the resolution in question is passed, and expiring on the date the next annual general meeting is or is required by law to be held, whichever is earlier, after the date the resolution in question is passed".

73 The definition of the "relevant period" can lead to different lengths of time permitted, depending on when the buyback mandate was adopted. For example, if the resolution approving the share buyback is passed at an Annual General Meeting (AGM), the relevant period would start from the last AGM, one year before the resolution, to the next AGM, one year after the resolution. The one year before the resolution might also have been the "relevant period" for an earlier share buyback resolution and if the 10% cap on purchases had been reached in that period then the current resolution would effectively be a dead letter.

74 The "relevant period" should not be defined by reference to the resolution date. Instead any period between two consecutive AGMs should be a "relevant period" during which the 10% cap cannot be exceeded.

75 In Australia, a "10/12 limit" is applied, beyond which shareholder approval is required (see section 257C of the Corporations Act 2001) for share buybacks. Section 257B(4) of the Australian Corporations Act 2001 states that "The 10/12 limit for a company proposing to make a buy-back is 10% of the smallest number, at any time during the last 12 months, of votes attaching to voting shares of the company". The position in other jurisdictions is not comparable.

76 In New Zealand, for buyback of shares without prior notice to shareholders under section 65(1)(b) of the New Zealand Companies Act 1993, "the number of shares acquired together with any other shares acquired … in the preceding 12 months does not exceed 5 percent of the shares in the same class as at the date 12 months prior to the acquisition of the shares". If that limit is exceeded[7] then a different procedure under section 63 involving notice to shareholders applies.

77 In the UK, section 725 of the UK Companies Act 2006 provides that "the aggregate nominal value of shares held as treasury shares must not at any time exceed 10% of the nominal value of the issued share capital of the company at that time".

78 The Steering Committee recommends that the definition of the "relevant period" for share buybacks in section 76B(4) be amended to be from "the date an AGM was held, or if

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[7] Section 67A(1) sets a 5% limit to the treasury shares that a company may hold; with any excess being deemed cancelled.

no such meeting was held as required by law, then the date it should have been held and expiring on the date the next AGM after that is or is required by law to be held, whichever is earlier". When consulted, majority of the respondents agreed with the recommendation.

Recommendation 3.22

The definition of the "relevant period" for share buybacks in section 76B(4) should be amended to be from "the date an AGM was held, or if no such meeting was held as required by law, then the date it should have been held and expiring on the date the next AGM after that is or is required by law to be held, whichever is earlier".

(b) Time periods for measuring threshold of share buybacks

79 The foregoing recommendation amounts to a conceptual change in the definition of the "relevant period" from a defined period for a particular resolution to a general period from one AGM to the next AGM. Accordingly, some consequential amendments to section 76B of the Companies Act will be required.

80 In sections 76B(3)(a) and 76B(3B)(a), the reference to "the last AGM ... held before any resolution passed ..." should be replaced with "the beginning of the relevant period". Also wherever "the relevant period" appears, it should be replaced with "a relevant period". When consulted, majority of the respondents agreed with the Steering Committee.

Recommendation 3.23

The reference to "the last AGM ... held before any resolution passed ..." in sections 76B(3)(a) and 76B(3B)(a) should be replaced with "the beginning of the relevant period".

Recommendation 3.24

Also wherever "*the* relevant period" appears in section 76B, it should be replaced with "*a* relevant period".

(c) Repurchase of "odd-lot" shares through a discriminatory offer (an "odd-lot" refers to shareholdings of less than 100 shares)

81 Where a listed company has substantial number of odd-lot shareholders, it will incur administrative costs to secure compliance with the Companies Act. Apart from the cost of dispatching notices of general meetings and annual reports to such shareholders, the odd-lot shareholders would be discouraged from attempting to dispose of their small shareholdings given the relatively high transaction costs.

82 Sections 76B to 76G of the Companies Act preclude a listed company from repurchasing odd-lots from the odd-lot shareholders through a discriminatory repurchase

offer. Section 76(1) also prohibits a company from financing dealings in its shares, unless they fall within the exceptions (including buybacks).

83 Like Singapore, both the UK (section 694 of the UK Companies Act 2006) and New Zealand (sections 60(1)(b) and 107(1)(c) of the New Zealand Companies Act 1993) do not allow buyback of odd-lot shares through a discriminatory repurchase offer[8]. US laws also do not specifically authorise odd-lot programs. However the US Securities and Exchange Commission (SEC) will issue a "no-action" letter to facilitate such odd-lot repurchase programs in USA. A no-action letter serves as a precedent vis-à-vis the SEC in the same way that a prior published case serves as a precedent for the courts.

84 Australia (section 257B(1) of the Corporations Act 2001 read with the Australian Listing Rules) allows repurchase of odd-lots from the odd-lot shareholders through a discriminatory repurchase offer[9].

85 When consulted, all the respondents agreed with the Steering Committee to amend the Companies Act to provide for an additional exception to the share acquisition prohibition for listed companies to enable such companies to make discriminatory repurchase offers to odd-lot shareholders. While this may seem discriminatory against holders of odd-lots of more than 100 shares, the number of such holders is very small. The disparity in prices is also not a valid concern since it is not compulsory for the seller to sell his odd-lot shares.

Recommendation 3.25

The Companies Act should be amended to provide for an additional exception to the share acquisition prohibition, viz, that listed companies be allowed to make discriminatory repurchase offers to odd-lot shareholders.

(d) Treasury Shares

86 Section 76K(1)(b) of the Companies Act states that treasury shares may be transferred for the purposes of "an employees' share scheme". The Steering Committee is of the opinion that this is unduly restrictive. The Steering Committee recommended that companies should have the latitude to use treasury shares pursuant to schemes meant to benefit persons other than employees as well, for example directors, consultants, spouses and family members of employees and directors. The majority of the respondents consulted agreed, though some commented that the provision should be confined to employees, so as not to be exploited by

[8] The UK (section 694) allows buyback of shares (including odd-lot shares) subject to the terms of the contract authorised by a special resolution of the company. New Zealand allows buyback of odd-lot shares subject to shareholders' consent. Section 60(1)(b) allows a company to make an offer to certain shareholders to buy their shares, provided that certain conditions are fulfilled including consent in writing of all shareholders, or if the offer is expressly permitted by the constitution and is made in accordance with the prescribed procedure. Alternatively, shares in the company may be acquired where all entitled persons agree or concur (section 107(1)(c)). Entitled persons are defined to mean a shareholder or person upon whom the constitution confers the rights and powers of a shareholder.

[9] Section 257B(1) allows the purchase of all of a holder's shares in a listed corporation if the shares are less than a marketable parcel within the meaning of the rules of the relevant financial market. Under the ASX Market Rules Procedure 2.10, a marketable parcel of equity securities is a parcel of not less than $500 based on certain criteria.

directors for their own benefit or used for the benefit of third parties who have not contributed economic value to the company. The Steering Committee disagreed, as there is no apparent reason to disallow directors from benefitting from a share scheme under section 76K(1)(b). The restricted uses of treasury shares were introduced as a measure of prudence when treasury shares were introduced for the first time in Singapore. It is timely to review if such restrictions are necessary. After review, the Steering Committee is of the opinion that if specific safeguards are necessary for listed companies, these should be imposed by rules applicable to only listed companies.

87 In the UK, treasury shares may be transferred by a company "pursuant to an employees' share scheme" (section 727(1)(b) of the UK Companies Act 2006). There is no comparable provision in the New Zealand Companies Act 1993[10]. In Australia there is no provision for treasury shares[11].

88 The Steering Committee also considered but disagreed with increasing the section 76I maximum treasury shareholding from the current 10% to 15%. The UK recently suggested removing the 10% cap on companies holding shares in treasury and extending the period for which authorisation may be given from 18 months to 5 years[12]. This proposal arose from the implementation of a EU Directive and applies to certain types of shares bought from profits. Given that Singapore allows shares to be bought from capital, it is debatable whether we should also similarly remove the maximum treasury shareholding restriction and extend the period of authorisation[13]. Section 67A(1)(c) of the New Zealand Companies Act 1993 imposes a cap of up to 5% of treasury shares in a particular class.

Recommendation 3.26

Section 76K(1)(b) should be amended by deleting the word "employees", in order to remove the restriction imposed on the use of treasury shares. If specific safeguards are necessary for listed companies, these should be imposed by rules applicable solely to listed companies.

VIII. FINANCIAL ASSISTANCE FOR THE ACQUISITION OF SHARES

89 Under the Companies Act a company is not permitted to give financial assistance for acquisition of its own shares or those of its holding company, unless the company falls within the excepted situations under subsections (8), (9), (9A), (9B) or (10) of section 76. In particular, subsections (9A) and (9B) were introduced to allow financial assistance when a solvency statement is given by the directors, the directors agree that the financial assistance should be given, it is in the best interest of the company to do so and the terms/conditions of

[10] The provisions relevant to treasury stock are at sections 67A to 67C of the New Zealand Companies Act 1993.

[11] Section 257H(3) of the Australia Corporations Act 2001 provides that "Immediately after the registration of the transfer to the company of the shares bought back, the shares are cancelled."

[12] Draft Companies (Share Capital and Acquisition by Company of its Own Shares) Regulations 2009 at www.berr.gov.uk.

[13] Draft Companies (Share Capital and Acquisition by Company of its Own Shares) Regulations 2009 at www.berr.gov.uk

the financial assistance are fair and reasonable. Subsection (9A) applies only in the limited situations where less than 10% of the company's paid up capital and reserves is involved, in which case only a directors' resolution is required. Where larger amounts are involved, subsection (9B) applies, requiring both directors' and shareholders' approval. If the directors elect not to provide the solvency statement, they can also rely on the process under subsection (10).

90 All leading jurisdictions have reformed this area, moving towards eliminating or relaxing restrictions on financial assistance. The UK has abolished financial assistance prohibitions with respect to private companies but had to retain them for public companies as that is required by a EU directive, subject to limited exceptions. Australia reformed this area in 1998 to transform financial assistance prohibitions to qualified authorization. New Zealand abolished financial assistance restrictions and now allows distributions to shareholders subject to a solvency test. The common reasons that prompted the changes included concerns of uncertainty in what amounts to financial assistance and impediments to commercial transactions.

91 The Steering Committee was initially in favour of abolition of financial assistance prohibitions for all companies because:

(a) Financial assistance restrictions exist to protect creditors and shareholders against misuse and depletion of a company's assets. However, abusive transactions can be controlled in other ways, e.g. through provisions on directors' duties or through fraudulent/wrongful trading provisions. If necessary, both directors' duties and section 339 on wrongful trading could be beefed up or suitably clarified to provide greater certainty.

(b) Section 76 (in particular subsections (3) and (4)) is overly complex and has been interpreted differently by judges. This has resulted in uncertainty and difficulty in application. In any case, with the extensive and substantial exceptions introduced by subsections (8) to (9B), financial assistance prohibitions have lost their potency.

(c) Financial assistance provisions cause difficulty in structuring transactions since they tend to cause delay.

92 The respondents consulted had mixed views on this issue. Alternative views expressed were:

(a) While financial assistance prohibitions raise legal uncertainties and might not be beneficial to the business community as a whole, there is still a genuine danger of misuse of the company's capital and assets at the cost of creditors and shareholders. The rationale for financial assistance prohibitions is still valid to a certain extent.

(b) The abuses which the financial assistance provisions sought to remedy would not be sufficiently addressed by relying on directors' fiduciary duties and statutory wrongful trading provisions.

(c) The Australian approach to financial assistance (Corporations Act 2001 Part 2J section 260A to section 260D) should be recommended.

93 In particular, MAS was of the opinion that while the current financial assistance provisions can be abolished for private companies, it would **not** be prudent to abandon the provisions for public companies for the following reasons:

(a) Public companies tend to have a larger shareholder base. There are currently over 1,500 public companies in Singapore of which more than half are unlisted. More importantly, there are quite a number of public companies that have de-listed from SGX over the years but are still held by a large number of public shareholders for various reasons.

(b) Public companies (listed or unlisted) raise capital from the public for the specific purpose of furthering their businesses, and these businesses would not ordinarily include the giving of assistance to acquire their shares. While there may be legitimate reasons why a company needs to undertake such a transaction in furthering its business objectives, at the minimum there should be some conditions that the company has to fulfil.

(c) If left unfettered, financial assistance transactions can be used to circumvent the prohibition on a company acquiring its own shares. Where financial assistance is provided on a non-arm's length basis, minority shareholders and creditors will be prejudiced. Financial assistance restrictions are important in getting boards to apply their mind to the transaction and assess whether the transaction is in the best interest of the company.

(d) Provisions on directors' duties and fraudulent/wrongful trading tend to be either too general or too narrowly circumscribed. Seeking a remedy under these provisions is also likely to be more challenging, with the need to establish the necessary intent (eg for fraudulent trading), and consequently expensive. Abusive transactions may not be effectively curtailed through provisions relating to market manipulation in Part XII of the Securities and Futures Act (eg, creation of false market). Hence, these provisions may not have a strong deterrent effect on controlling shareholders or directors.

(e) Total abolition of financial assistance restrictions for public companies would also put us out of line with other major jurisdictions (eg Australia, New Zealand, Hong Kong and EU countries) which continue to maintain limitations on financial assistance. The UK has abolished financial assistance restrictions for private companies but kept them for public companies.

(f) Under the Singapore regime, for financial assistance to fall under an exception and thus be allowed, resolutions of the board and shareholders' resolutions will generally need to be obtained unless all the directors make a solvency statement and the board resolves, *inter alia*, that financial assistance is in the best interests of the company and the terms and conditions are fair and reasonable (even then, the amount of financial assistance is capped at 10% of the capital of the company). MAS proposed that the Steering Committee consider Australia's qualified authorisation regime. The Australian Corporations Act allows financial assistance if the giving of assistance does not materially prejudice the interests of the company or its shareholders, or the company's ability to pay its creditors. The determination of whether a transaction involves "material prejudice" is made by the board and if a transaction is found not to involve "material prejudice," shareholder approval is not required. In this way, MAS sees the Australian regime as a middle ground between removing financial assistance provisions altogether and retaining the current prohibition on financial assistance. Under the Australian regime, potentially beneficial or innocuous transactions will arguably not be seen as involving "material prejudice" and will be allowed without the need for further shareholder approval. The Australian regime also provides more commercial certainty and comfort for counterparties who have sold shares to parties involved in financial assistance, as such transactions will not be invalid by reason of a contravention of financial assistance provisions (although the directors of the company may be punished). In contrast, under the Singapore regime, such transactions will either be void or voidable.

(g) If financial assistance restrictions prevent or render more expensive a range of potentially beneficial or at least innocuous transactions, the solution is not to abandon the current regime entirely but rather to refine the financial assistance restrictions to more clearly define the conduct which they seek to prohibit. This seems to be the route that some Singapore judges have taken in recent years[14].

94 The Steering Committee acknowledges that the rationale for financial assistance prohibitions is still valid. The prohibitions are to ensure that the capital of a company is preserved intact and not eroded by deliberate acts done otherwise than in the ordinary operations of the company undertaken in the pursuit of its objects for which it was established. Other secondary purposes of financial assistance prohibitions are to prevent market manipulation and to inhibit management of the company interfering with the normal market in the company's shares by providing support from the company's resources to selected purchasers. However, the determining question is whether financial assistance prohibitions are effective as an ex ante rule against the improper dissipation of a company's capital. For an ex ante rule to work well, it should be clear when it is breached and it should not be so broad as to cover necessary and acceptable transactions. Bearing this in mind, the Steering Committee recommends the following refinements.

95 As private companies are closely held, shareholders have greater control over how they can have a say in the company's decision to give financial assistance. Creditors can also rely on breach of directors' duties and provisions on fraudulent and wrongful trading. Also as private companies have fewer resources and the cost of obtaining legal advice is relatively heavier to them, on balance the Steering Committee proposes the abolition of financial assistance prohibitions for private companies (unless they are subsidiaries of public companies). This is consistent with the position in the UK and HK, though in HK, the intended abolition for private companies in the long run is supported in principle, but would not be included in the pending HK Companies Bill.

96 In contrast, public companies have a larger number of shareholders and they have limited control over the company's decision to give financial assistance. It is therefore important to retain financial assistance prohibitions on public companies and their

[14] For instance, in *PP v Lew Syn Pau* [2006] 4 SLR(R) 210, Sundaresh Menon JC (as he then was) sought to limit the prohibition in two ways. Firstly, he inferred a requirement that the FA must result in a depletion of the corporate assets, or at least put them at risk. Secondly, even if the corporate assets are depleted (or put to such risk), the prohibition is not contravened if the transaction is genuinely entered into in the company's own commercial interest, and not merely to financially assist the acquisition of its shares.

subsidiaries, to ensure adequate protection of shareholders and creditors.

97 To address the concern that the present financial assistance restrictions may prevent or render more expensive a range of potentially beneficial or innocuous transactions, the Steering Committee accepts MAS's suggestion to include an additional exception to allow a public company or its subsidiary to assist a person to acquire shares (or units of shares) in the company or a holding company of the company if giving the assistance does not materially prejudice the interests of the company or its shareholders or the company's ability to pay its creditors. This is adapted from the Australian approach of authorized assistance.

98 As for the question of whether any of the alternative exceptions under section 76(9A), (9B), (9C) and (10) should be removed, the Steering Committee prefers not to do so. There is some uncertainty surrounding the materiality threshold while the solvency test may not be suitable for some situations. The limitations of these two options may impede legitimate financial transactions which directors should be able to consider under the alternative options.

99 Section 76(8) and (9) should be reviewed against the list of excepted financial assistance transactions in the UK to determine if they should be updated.

Recommendation 3.27

Section 76(1)(a) and associated provisions relating to financial assistance should be abolished for private companies, but continue to apply to public companies and their subsidiary companies. A new exception should be introduced to allow a public company or its subsidiary to assist a person to acquire shares (or units of shares) in the company or a holding company of the company if giving the assistance does not materially prejudice the interests of the company or its shareholders or the company's ability to pay its creditors.

Recommendation 3.28

Section 76(8) and (9) should be reviewed against the list of excepted financial assistance transactions in the UK to determine if they should be updated.

Recommendation 3.29

Section 76(1)(b), (c) and associated provisions should be integrated with the provisions on share buybacks.

IX. REDUCTION OF CAPITAL

(a) Solvency statements for capital reductions without court sanction

100 Under the Companies Act, a company may reduce its share capital without court sanction if approved by special resolution of its shareholders. The relevant provisions are section 78B for private companies and section 78C for public companies. Unless the reduction is solely by way of cancellation of any lost paid-up capital, all directors must

provide a statutory declaration of solvency which conforms with section 7A.[15] Creditors are protected by section 78D which allows any creditor to apply to court for cancellation of the special resolution for capital reduction. Notice of the special resolution must be lodged with ACRA within 8 days in accordance with the publicity requirements as prescribed at regulation 6 of the Companies Regulations.

101 Court-sanctioned capital reduction under section 78G does not require a solvency statement.

102 The Steering Committee has considered whether the solvency statement requirement is unnecessary for capital reductions, particularly since directors are already duty bound to act in the best interests of the company. One alternative considered in lieu of solvency statements is sending a notification to all creditors giving them opportunity to object. However the reality is that creditors may overlook any such notice or may not be able to respond in time.

103 In the UK the position is similar for private companies in that a solvency statement is required for capital reduction without court sanction. In New Zealand, the reduction of shareholders' liability may amount to a distribution, for which a solvency statement is required. In Australia, capital reductions are not governed by a solvency test.

104 On the whole it was felt that the solvency statement is an objective measure which does serve a useful purpose and so should be retained. When consulted, all the respondents agreed with the proposal.

Recommendation 3.30

The requirement for a solvency statement in capital reductions without the sanction of the court should be maintained.

(b) Capital reductions not involving a distribution or release of liability

105 Although sections 78B(1) and 78C(1) of the Companies Act provide that solvency requirements apply for capital reduction, sections 78B(2) and 78C(2) provide that they do not apply if the reduction of capital is in respect of the cancellation of capital lost or unrepresented by available assets. Reduction of capital in these circumstances does not involve either a reduction of liability in respect of unpaid share capital or the distribution to a shareholder of any assets.

106 In the UK, a solvency statement is required for capital reduction without court sanction, but this avenue is only available to private companies. In Australia, under section 256B of the Corporations Act 2001, capital reduction is allowed if it is fair and reasonable, does not prejudice creditors and is approved by shareholders – no solvency statement is required. The New Zealand Companies Act 1993 has no comparable provisions on capital reduction but relies on a solvency test for distributions in general.

[15] Sections 78B(3) and78C(3).

107 The Steering Committee recommends that the dispensation of solvency requirements should be extended to generally cover all situations which do not involve a reduction/distribution of cash or other assets by the company or a release of any liability owed by the company. When consulted, majority of the respondents agreed.

Recommendation 3.31

Sections 78B(2) and 78C(2) should be amended to dispense with solvency requirements as long as the capital reduction does not involve a reduction/distribution of cash or other assets by the company or a release of any liability owed to the company.

(c) Time frames for capital reduction

108 Sections 78B(3) and 78C(3) of the Companies Act prescribe that the solvency statement required for capital reduction should be made before the resolution approving the capital reduction but should precede the resolution by not more than 15 days in the case of private companies or 22 days in the case of public companies.

109 In the UK, the time frame specified at section 642 of the UK Companies Act 2006 for the solvency statement relating to a private company is “not more than 15 days before the date on which the resolution is passed”. There is no comparable provision for public companies in the UK. Australia and New Zealand have no comparable provisions whether for public or private companies.

110 Given that notice of 14 and 21 days is required before the meeting to pass the resolution in the case of private and public companies respectively, this leaves an allowance of only a single day for the solvency statement to be made. The Steering Committee is of the view that a little bit more latitude should be allowed instead of having such a tight time frame and this was supported by all the respondents consulted.

Recommendation 3.32

The time frame specified in sections 78B(3)(b)(ii) and 78C(3)(b)(ii) should be amended from the current 15 days and 22 days to 20 days and 30 days respectively.

(d) Declaration by directors

111 Directors are under a fiduciary duty to act in the best interests of the company. Although requiring a declaration that any capital reduction is in the best interests of the company may serve the purpose of highlighting this duty at a point when it is particularly important to be aware of it, doing so may lead to a misunderstanding that there is some higher standard of duty associated with capital reduction in particular. This might also deter companies from using this procedure. The UK, Australia and New Zealand do not require such a declaration of directors. This was supported by most of the respondents consulted.

<u>Recommendation 3.33</u>

A provision requiring directors to declare that their decision to reduce capital was made in the best interests of the company is not required as the obligation to act in the best interests of the company is already covered by existing directors' duties.

X. DIVIDENDS

112 Section 403(1) of the Companies Act provides that "No dividend shall be payable to the share-holders of any company except out of profits". The observations and recommendation in the 2002 report of the Company Legislation and Regulatory Framework Committee (CLRFC) were:

> "3.3 Dividends
>
> 3.3.1 We have considered the prevailing common law rules relating to dividends and developments in the UK and Australia with a view to modernising the Singapore position. Under common law, dividends are payable if there are profits in a particular year, even if the company has accumulated losses on its balance sheet.
>
> 3.3.2 We also considered the meaning and scope of "profits". Pursuant to s. 39 of the UK Companies Act 1980 (now s. 263 and s. 275 of the UK Companies Act 1985), dividends are only distributable out of accumulated realised gains minus accumulated realised losses (so far as not written off in a prior reduction of capital exercise). The UK regulators have proposed to leave it to the accounting profession to prescribe the meaning of 'realised'.
>
> 3.3.3 In Australia, dividends are in theory payable even though there are revenue deficits in previous years. However, the profits must be available at the date of payment, and not the date of declaration. New Zealand has a statutory solvency test that applies to all types of distribution.
>
> 3.3.4 We propose adoption of the UK approach that distributions may only be made out of accumulated realised gains minus accumulated realised losses and to leave it to prescribed accounting standards and rules to determine the meaning of "realised". We note that the Accounting Standards Board in the UK is proposing to move away from the concept of "realised profits" and would recommend that developments be reviewed by the CCDG.
>
> **<u>RECOMMENDATION 2.20</u>**
>
> **The CLRFC recommends that the Council on Corporate Disclosure and Governance review the accounting standards and rules to limit distributions to be made only out of accumulated realised gains minus accumulated realised losses in the light of international developments moving away from the concept of 'realised profits'."**

113 Recommendation 2.20 of the CLRFC has not been implemented to date. The position in New Zealand remains unchanged.

114 Australia amended their legislation in June 2010[16] to repeal the profits test and allow a company to pay dividend if:

(a) the company's assets exceed its liabilities and the excess is sufficient for the payment of the dividend;
(b) it is fair and reasonable to the company's shareholders as a whole; and
(c) it does not materially prejudice the company' ability to pay its creditors.

115 The reforms came about as the Australian Corporations Act does not provide guidance on or a definition of the term "profits". In addition, the legal precedents were outdated, complex and may not be in line with present accounting principles. The nature of the accounting principles for the calculation of profits has changed over time and the requirement for companies to pay dividends only out of profits was inconsistent with the trend to lessen the capital maintenance doctrine in Australia[17].

116 In the UK the use of "realised profits" had not led to certainty in the amounts available for distribution. Towards the end of 2008, the Institute of Chartered Accountants of England and Wales and the Institute of Chartered Accountants of Scotland issued Technical Release 07/08[18] which provides over a hundred pages of draft guidance on the determination of realised profits and losses in the context of distributions under the Companies Act 2006. This shows that the concept of "realised profits" is difficult to define in itself. There has been no concrete development on the UK proposal to move away from the concept of "realised profits" as recorded in the CLRFC report.

117 The Steering Committee first considered the New Zealand approach, i.e. whether a solvency test rather than profits for dividend distribution would be more consistent with the current capital maintenance framework. However any change in dividend distribution rules might have a negative impact on the market, since current rules are well known and have the advantage of being simple and straightforward. Also, there has been no practical difficulty in the application of the current section 403 rule for dividend distribution.

118 The Steering Committee also considered the Australian approach but is of the opinion that other than the observations applicable to the NZ approach, there may be further uncertainties with the Australian approach as an assessment would be needed when determining if a dividend distribution is "fair and reasonable to shareholders" or if it would "materially prejudice the company's ability to pay creditors". Companies are likely to face practical difficulties when making such assessments.

119 The Steering Committee considered the UK approach and also whether section 403 is clear enough in specifying that dividends may be distributed out of "profits". The issue is whether section 403 should be modified so that dividends are payable only out of

[16] Access http://www.comlaw.gov.au for the Corporations Amendment (Corporate Reporting Reform) Bill 2010
[17] Access http://aph.gov.au for the explanatory memorandum and digest of the Corporations Amendment (Corporate Reporting Reform) Bill 2010
[18] Updating previous guidelines of the ICAEW & ICAS (Institute of Chartered Accountants of England and Wales & Institute of Chartered Accountants of Scotland), to be found at http://www.icaew.com.

accumulated realised gains minus accumulated realised losses rather than simply profits. The question is whether or not prior accumulated losses should be cleared before payment of dividends is allowed. There are reasons why this should not be required, viz, current shareholders should not be burdened with disadvantages arising from accumulated losses. Also, accumulated losses may be caused purely by accounting conventions rather than trading losses. This may be one reason not to require clearance of accumulated losses. In any case, moving to the UK model of allowing only "realised" profits to be distributable would not be an improvement because it would complicate the issue, particularly considering that Singapore would then probably have to adopt something similar to the voluminous guidance on what amounts to "realised" profits issued by the Institute of Chartered Accountants of England and Wales.

120 During consultation, about half of the respondents supported no change in the current position. The opposing school conveyed their objections to the current regime based on two main grounds namely (i) ambiguity on the definition of 'profits' and (ii) changes in accounting rules. One other respondent also cited possible abuses on declaration of interim dividend prior to year end impairment review.

121 On the definition of profits, the opposing school is of the opinion that while current shareholders should not be burdened with disadvantages arising from accumulated losses, all else being equal, the presence of accumulated losses would imply that there are insufficient assets to satisfy the liabilities (disregarding other equity "reserves" items which could represent unrealized gains/losses from revaluation of assets). Hence, allowing distribution when there are accumulated losses may be perceived to be prejudicial to the interests of creditors. While accumulated losses may be caused purely by accounting conventions rather than trading losses, it is the same issue with current year's profits. In other words, the issue of whether accumulated losses should be taken into consideration remains contentious and the respondent commented that the issue should be further studied.

122 On the changes in accounting rules, the current requirement in Section 403 of the Companies Act does not adequately address accounting developments. For example, certain profit/loss items are to be taken to equity/reserve, but there is no guidance as to whether such equity items constitute distributable reserves. There should be further clarification on the types of reserves that would be deemed to be distributable as dividends. The opposing school also commented that the law should recognize that, with the development of the International Financial Reporting Standards (IFRSs), the traditional notion of "profits" may be inadequate at times. For instance, under IFRS 9 Financial Instruments, which is slated to replace International Accounting Standard 39 Financial Instruments: Recognition and Measurement (from which the Singapore Financial Reporting Standard 39 has been adapted), a company will face a situation whereby it will no longer have "profits" or "losses" arising from derecognition of an investment designated under the Fair Value through Other Comprehensive Income category, or "losses" from impairment of investment designated under such category.

123 The opposing school suggested that while adopting the "realised profits" regime in the UK may create more confusion, a middle-of-the-road approach as follows can be considered. No dividend shall be payable to the shareholders of any company except:

(a) where the company has accumulated profits (after taking into account profits/ loss for the period); or

(b) where the company is in an accumulated loss position, it would have to satisfy a solvency test (that can be modelled after the New Zealand's approach).

It was contended that the above-proposed approach promotes more prudent business practice than the current "profit" test. In addition, the solvency test would address a situation where a company does not have "profits" to show but is nonetheless able to make distributions without compromising its capital maintenance position (arising from changes in accounting rules e.g. IFRS 9). Alternatively, some respondents suggested imposing the solvency test on companies with negative equity to safeguard the interests of the creditors.

124 Taking into account all views submitted, the Steering Committee nevertheless proposes no change to the present position. The NZ, Australian and UK models were studied but not recommended for the reasons given above. As for the respondent's proposed middle-of-the-road approach, the Steering Committee acknowledges that there are some merits to this. However as this approach contains some aspects of the UK, NZ and Australian regimes, the Steering Committee recommends that the developments in other leading jurisdictions and the impact of the recent changes in Australia be monitored for the time being, before this issue is reconsidered.

125 Also, after considering the position in various jurisdictions, the Steering Committee has decided that breach of section 403 should not be decriminalised. Although not a crime in the UK or Hong Kong, making an unlawful distribution without satisfying the profits test is a crime in Singapore[19] and Australia[20]. In New Zealand, a similar crime is committed when an unlawful distribution is made without satisfying the solvency test[21]. The Steering Committee has also considered but decided that it is not necessary to amend section 403 to state that even if there is a profit for the purposes of section 403, the directors' duties under section 157 of the Companies Act still apply in respect of the directors' decision to distribute dividends.

126 The Steering Committee also considered the regulation of interim dividends. Presently the common law position is that where interim dividends are paid, there must be a reasonable expectation that there will be profits for the year to cover such interim dividends, failing which the directors may be held personally liable. The Steering Committee considered whether the Companies Act should provide that distribution of interim dividends based on the most recent financial statements (not more than about 3 months old from the date of approval of payment by directors) should be beyond reproach, no matter how the final year financial

[19] In Singapore, under section 403(2) of the Companies Act, making an unlawful distribution is a criminal offence for any director or manager who does so wilfully, punishable with fine up to $5,000 or up to 12 months in prison. In addition, section 339(3) of the Companies Act imposes criminal sanctions for insolvent trading, section 340(1) of the Companies Act imposes civil sanctions for fraudulent trading and section 401 of the Criminal Procedure Code provides for payment of costs of prosecution and compensation.

[20] Section 254T read with section 1311(1A) and Schedule 3 of the Corporations Act 2001. Furthermore, under section 588G(1A) of the Act, if it leads to insolvency then it would amount to insolvent trading which may, if in an aggravated form (i.e. involving dishonesty), be a criminal offence under section 588G(3) punishable with a maximum of $200,000 fine and/or imprisonment of 5 years and 5 years disqualification.

[21] Despite the similarity that distributions made without satisfying the relevant test is criminal in both New Zealand and Singapore, it should be appreciated that the positions are not very easily comparable given the different tests applied. Non-compliance with the New Zealand provisions would occur only if an unlawful distribution leads to insolvency, an understandably serious misdeed likely to cause harm to creditors whereas in the Singapore/Australia context, an unlawful distribution may be made by a perfectly solvent company simply because the company has no profit in its books. If the unlawful distribution is made by an insolvent Singapore company, that could amount to a breach of directors' duties or possibly insolvent trading – both themselves criminal offences in Singapore.

statements may turn out. In addition, the financial statements based on which interim dividends were paid would not have to be audited as long as they are prepared in accordance with the Financial Reporting Standards (FRS) that are applicable to that financial period.

127 The consultation process elicited mixed views from the respondents. Some alternate views were that financial results may be "lumpy" and directors could very well be aware of how the financial statements may turn out. Unlike final dividends, interim dividends are wholly provisional and anticipate the profits to be disclosed in the final accounts. Hence, requiring directors to reasonably believe that there will be profits for the year to cover such interim dividends should be retained as a necessary safeguard. In conclusion, the Steering Committee was persuaded to retain status quo. While one possible consequence was the loss of business from fund companies which aspire to pay a regular quarterly dividend, there was no basis to accord preferential treatment for such businesses.

Recommendation 3.34

The section 403 test for dividend distributions should be retained.

XI. OTHER ISSUES PERTAINING TO CAPITAL MAINTENANCE

(a) Permitted uses of capital for share issues and buybacks

128 Prior to the commencement of the Companies (Amendment) Act 2005 (hereinafter referred to as "the Amendment Act") on 30 January 2006, a company could use its share premium account to pay commissions as well as other permitted expenses incurred for an issue of shares.[22] The Amendment Act repealed the applicable provisions pursuant to the recommendations of the CLRFC.[23]

129 Whilst the Amendment Act also allowed any amount remaining in the share premium account (which has been added to and now forms part of the company's share capital after 30 January 2006) to be used for payment of expenses connected with an issue of shares incurred before 30 January 2006,[24] it does not however expressly provide that companies can use its share capital to pay for the permitted expenses, if these are incurred after 30 January 2006; neither does the Amendment Act introduce any prohibition on so doing.

[22] Section 67 of the former Companies Act (before it was amended by the Companies (Amendment) Act 2005) provided that a company may pay a commission to any person in consideration of his subscribing or agreeing to subscribe for any shares or procuring or agreeing to procure subscriptions, whether absolute or conditional, for any shares in the company if the respective conditions were fulfilled. In addition, section 69(2)(e) of the said Act expressly allowed the share premium account to be applied to write off preliminary expenses or the expenses of, the commissions or brokerage paid or discount allowed on, any duty, fee, or tax payable on or in connection with any issue of shares of the company.

[23] The relevant provisions were sections 67 to 69 of the Companies Act. They were repealed as they were no longer applicable as the concept of share premium ceased to apply with the abolition of the concept of par or nominal value. See CLRFC Final Report Para 3.1.8, Chapter 2.

[24] Section 62B (3)(b) of the current Companies Act allows a company to use the amount standing to the credit of its share premium account immediately before 30 January 2006 to write off the preliminary expenses incurred before that day or expenses incurred, or commissions or brokerages paid or discounts allowed, on or before 30 January 2006, for any duty, fee or tax payable on or in connection with any issue of shares of the company.

130 The business community and professionals commented that there is some uncertainty as to whether a company can utilise the proceeds of the issue or its share capital to meet the permitted expenses (by the prescribed accounting standards, with details in the latter part of this paragraph below) incurred after 30 January 2006, since there is no longer a share premium account mandated by law. One view taken is that all monies raised from a share issue is now part of share capital and as a general rule, any amount taken out of the share capital for the company's use amounts to a reduction of share capital. Under the Companies Act, a reduction of share capital can only take place following the procedures under Division 3A, Part IV of the Companies Act. The other (alternative) view is that Division 3A concerns a reduction in the number of shares rather than a mere reduction in share capital amount. In particular, the number of shares reduced in a reduction exercise is required to be reported and it is normal for a company to use the amount raised from its share capital for its business needs. Also, the second interpretation is consistent with the prescribed Accounting Standards which allows expenses directly related to any share issue or buyback to be deducted from the equity[25] portion of the company's balance sheet which can consist of share capital, reserves and retained earnings, ie, equity can comprise more than just the share capital.

131 Australia[26] allows a company to pay brokerage or commissions to a person in respect of that person or another person agreeing to take up shares in the company. The New Zealand Companies Act 1993 is silent on this issue. In the view of the Steering Committee, it is unclear whether share capital may be used to pay for brokerage or commissions incurred for shares bought back by the company. There is no reason why it should not apply to buybacks.

132 When consulted, most of the respondents agreed with the Steering Committee that it should be explicitly provided that a company may use its share capital to pay for expenses, brokerage or commissions incurred in an issue or buyback of shares.

<u>Recommendation 3.35</u>

Provisions should be made in law to allow a company to use its share capital to pay for expenses, brokerage or commissions incurred in an issue or buyback of shares.

(b) Reporting of amounts paid up on the shares in a share certificate

133 Prior to the commencement of the Companies (Amendment) Act 2005, companies were required to disclose the nominal value, class of the shares and the extent to which the shares are paid up in their share certificates under the repealed section 123(2)(c) of the Companies Act. Presently, companies are required to disclose the amounts paid, amounts unpaid (if any) on the shares, the class of the shares and the extent to which the shares are paid up. The reason is that with the abolition of par-value, the amount unpaid, if any, represents the outstanding amount due from the shareholders and should therefore be reflected.

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[25] Paragraph 37 of FRS 32 allows expenses that are incremental and directly attributable to the share issue or share buyback to be deducted from equity. It is generally accepted that "equity" consists of share capital, reserves and retained earnings.

[26] Section 258C of the Corporations Act 2001.

134 A share certificate must be issued by a company in various circumstances, viz, when shares are allotted, transferred or subdivided, and also when share certificates are spilt, consolidated, lost or destroyed. Fulfilling the requirement to report the amounts paid under the par-value shares regime in the share certificates is not a problem because companies reported the par-value. However, representations were received that after the par-value concept had been abolished, compliance with this requirement has posed a problem in cases where shares have been issued from time to time at a premium and the premium amount has varied. This is especially so for shares of listed companies, as explained below:

(a) Shares of listed companies are deposited with CDP to facilitate scripless trading. At the first instance when the company is listed, certificates are issued to CDP as the registered holder of the then-existing shares (which very often, have been sub-divided prior to the initial public offering) and the new shares offered under the listing exercise. Such shares deposited with CDP would have different issue prices. Most listed companies also have share option schemes. In addition, a listed company may undertake equity-based exercises such as rights issues, the issue of convertible securities, private placement, capital reduction, etc, all of which entail the issue of new share certificates which are deposited with CDP. If and when a depositor decides to withdraw his shares from the CDP system and a share certificate is to be issued in his name, it is administratively impossible to ascertain what should be the amount to be stated on the share certificate in respect of the shares withdrawn from CDP, as such shares become fungible within the CDP system.

(b) Some older listed companies also continue to have shareholders holding physical scrips even after the migration to the CDP system in the mid-1990s. Whenever such shares are transferred or a shareholder's holding is consolidated or sub-divided, new certificates have to be issued. Given that shares of a listed company are publicly traded and would have changed hands many times over the years, it is very difficult to trace the amount originally paid on each share as certificates could have been transferred, split, consolidated, partially transferred, etc.

(c) Similarly, a private company or unlisted public company which has had changes to its capital structure or shareholders, or issued shares at par as well as at a premium, would also encounter similar difficulties.

135 Companies also submitted that there is not much value including "the amount paid on the shares" on a share certificate for fully-paid shares as such information is historical and that has no bearing on the rights or liabilities in respect of the shares. Rather, it is the amount payable on a partly-paid or unpaid share that is relevant to the rights or liabilities in respect of those shares. There is also an issue of confidentiality regarding the amount paid on the share, as a transferor may not like the transferee to know how much he/she has paid.

136 Lastly, companies felt that as the issue price for shares issued after 30 January 2006 is not pegged at the nominal value, the risk of making an error in recording "the amount paid on the shares" in a share certificate is correspondingly higher as shares would be issued at different times and with different issue prices. The benefit of including information relating to "the amount paid on the shares" on a share certificate is outweighed by the adverse consequences (to a company as well as the parties of a share transfer transaction) of having inaccurate information on a share certificate. Instead, section 63(1)(b) of the Companies Act

requires every company, when it makes an allotment of shares, to record in a return to be lodged with the Registrar of Companies, inter alia, "the amount (if any) paid or deemed to be paid on the allotment of each share". The return of allotment lodged pursuant to section 63 is a better source of information for companies and shareholders to confirm the conclusive amounts paid on the shares as this is public information.

137 The UK has not abolished the par-value share concept. Australia requires share certificates to disclose the name of the company, class of shares and amount (if any) unpaid on the shares.[27] However, Australia generally requires both the amounts paid and unpaid on the shares to be disclosed in its register of members[28] while Singapore requires the amounts paid or agreed to be considered as paid on the shares of each member to be disclosed in the register of members.[29] New Zealand requires the name of the company, class of and number of shares to be disclosed on the share certificate.[30]

138 Most of the respondents supported the recommendation to remove the requirement to disclose the "amount paid" on the shares in the share certificate under section 123(2)(c) and to require companies to disclose the class of shares, the extent to which the shares are paid up (i.e. whether fully or partly paid) and the amounts unpaid on the shares, if applicable under section 123(2)(c).

Recommendation 3.36

The requirement to disclose the "amount paid" on the shares in the share certificate under section 123(2)(c) should be removed. Companies should be required to disclose the class of shares, the extent to which the shares are paid up (i.e. whether fully or partly paid) and the amounts unpaid on the shares, if applicable under section 123(2)(c).

(c) Financial Reporting Standards and section 63

139 Under FRS 102 equity-settled options granted by a company to its employees as part of a remuneration package will be recorded as an employee expense in the profit and loss statement, and a corresponding credit will be made to a reserve account (normally called the "share option reserve account"). When such options/warrants were exercised and shares issued, the reserve would be included as part of the share premium account. In a non-par value share regime today, companies are similarly permitted to transfer their reserves to share capital since share capital refers to the amounts received for the shares issued. When options or warrants are not exercised and shares are not issued, the accounting treatment and existing law do not prohibit capitalisation of reserves, which means that the reserves may be added to the share capital. The Steering Committee is of the view that such a policy should be retained as it is in line with the non-par regime now in place.

140 In addition, there are some differences on what amounts to share capital from the accounting perspective when compared with the legal perspective. Depending on the terms

[27] Section 1070B of the Corporations Act 2001.
[28] Section 169 of the Corporations Act 2001.
[29] Section 190 of the Companies Act.
[30] Section 95 of the Companies Act 1993.

they are issued on, redeemable preference shares may be classified in accounts as a liability rather than share capital by virtue of FRS 32. Interest-free loans between a parent and subsidiary could be deemed a capital contribution or distribution by virtue of FRS 39. However, no changes to the law are warranted on account of such changes in accounting treatment.

141 Australia and New Zealand are silent on whether the reserves can be transferred to capital, and whether deemed capital contribution and distributions such as those arising under FRS 39 are permitted in law. New Zealand does not require the consideration paid or agreed to be paid for the shares issued to be reported to the authority. However, New Zealand imposes specific duties on the board before they issue shares, options and convertible securities. These duties relate to the decision on the consideration for which the shares will be issued, the terms of the issue, determination of the reasonable cash value (if the consideration is not cash), a resolution that the consideration is fair and reasonable to the company and existing shareholders and a resolution that the present cash value for the consideration to be provided for the issue (if it is non-cash consideration) is not less than the amount to be credited for the issue of the shares. The Australian legislation is silent on this point.

142 The Steering Committee recommends that the law should be amended to require companies which have increased their capital (from both issue and non-issue of shares) to report such changes to ACRA by lodgment of a return with the Registrar of Companies under section 63(1) of the Companies Act. This will ensure that the amount of capital reflected in the financials will be consistent with the statutory records. The majority of the respondents consulted agreed.

Recommendation 3.37

There should be no changes made to the Companies Act on account of the new FRS 32, FRS 39 and FRS 102.

Recommendation 3.38

Section 63 should be amended so that a company is required to lodge with the Registrar a return whenever there is an increase in share capital regardless of whether it is accompanied by an issue of shares.

XII. SCHEMES OF ARRANGEMENT

143 Sections 210 to 212 of the Companies Act deal with schemes of compromise or arrangements proposed between a company and its creditors or members which may be made binding on all creditors or members as long as the requisite voting approval is obtained. Section 210 has come to be used as a means for takeover of a target company by an offeror.

(a) Holders of units of shares

144 Section 210 of the Companies Act provides the mechanism for a compromise or arrangement "between a company and its creditors or any class of them or between the

company and its members or any class of them". Based on the wording of section 210, there could be doubts as to whether or not holders of options and convertibles could be parties to a section 210 scheme.

145 In Australia, which has a similar provision, the predominant view is that holders of options and convertibles would be classified as "creditors" and so are within the scope of the scheme of arrangement provisions[31]. The UK and New Zealand also refer to "members or any class of them" for a similar provision. However, the Steering Committee is of the view that the position should be made clear by amending section 210 to state explicitly that it includes holders of units of company shares. When consulted, most of the respondents agreed.

Recommendation 3.39

Section 210 should be amended to state explicitly that it includes a compromise or arrangement between a company and holders of units of company shares.

(b) Share-splitting and voting by nominees

146 For section 210(3) of the Companies Act to be binding, a proposal must have the agreement of "a majority in number, representing three-fourths in value" of the creditors or members present and voting.

147 The issue of share-splitting (i.e. persons who transfer their shares to other members who are willing to vote according to their wishes) arose in a section 210-type scheme in the Australian case of *Re MIM Holdings Ltd* [2003] QSC 181. Although in that case share-splitting could not have affected the voting outcome on the scheme, Ambrose J observed that if it was likely or even possible that the majority in number had been achieved by reason of share-splitting, that might be a reason for withholding approval of the scheme. However, as long as the 50 percent test applies, the court cannot approve a scheme where that test is not passed, including where it is not passed by reason of share-splitting.

148 After *Re MIM Holdings Ltd,* Australia amended section 411(4)(ii) of the Corporations Act 2001 (equivalent to section 210(3) of Singapore Companies Act) so that "unless the Court orders otherwise" was added as set out below:

> "(ii) in the case of a compromise or arrangement between a body and its members or a class of members—a resolution in favour of the compromise or arrangement is:
>
> (A) unless the Court orders otherwise—passed by a majority in number of the members, or members in that class, present and voting (either in person or by proxy); and
>
> (B) if the body has a share capital—passed by 75% of the votes cast on the resolution; and…"

[31] Ford's Principles of Corporation Law, Volume 2, Chapter 24, paragraph 24.020.

149 The Explanatory Statement[32] for the Amendment Bill sheds light on the situation the amendment was intended to remedy:

“4.179 A members’ scheme could be defeated by parties opposed to the scheme engaging in ‘share-splitting’, which involves one or more members transferring small parcels of shares to a large number of other persons who are willing to attend the meeting and vote in accordance with the wishes of the transferor. By splitting shares to increase the number of members voting against the scheme, an individual or small group opposed to the scheme may cause the scheme to be defeated. This may occur even though a special majority is achieved in terms of voting rights attaching to share capital, and if the share split had not occurred, the majority of members were in favour of the scheme.”

150 For similar reasons as in Australia, a similar amendment should be made to section 210(3). The majority of the respondents agreed, with two respondents cautioning that the change remains subject to a number of limitations and that it would appear that the real problem with the numerical majority test lies in the existence of the test itself. Giving the court discretion to disregard the step may serve as a partial solution to some of the problems caused by the test. The respondent asked if total abolition of the test should be considered. In NZ, there is no longer provision for a statutory scheme of arrangement requiring approval from specified majority shareholders. Reconstructions can be effected by resolutions of the shareholders, amendments to the constitution or by application to the court under section 236 of the New Zealand Companies Act 1993. However, at meetings of creditors held for the purposes of section 230 (for compromises with creditors), a resolution is adopted if a majority in number representing 75% in value of the creditors or class of creditors voting in person or by proxy vote or by postal vote in favour of the resolution.[33]

151 The Steering Committee recommends that the test be retained. In the UK, although the Company Law Review Steering Group proposed a removal of the requirement for a majority in number to approve a scheme, the proposal was not implemented in the final amendments[34]. The UK government retained the measure as an important safeguard for minority shareholders and this was defended by the Attorney-General when the UK Companies Bill was debated in parliament[35].

152 The Steering Committee also recommends that if a majority in number of proxies and a majority in value of proxies representing the nominee member vote in favour of the scheme, it would count as the nominee member having voted in favour of the scheme.

[32] http://www.austlii.edu.au/au/legis/cth/bill_em/cab2007390/memo_0.html

[33] See Schedule 5, clause 5(2) of the New Zealand Companies Act 1993.

[34] See “Modern Company Law: For a Competitive Economy – Final Report”, London, Vol. 1, June 2001 at 278 [13.10]. House of Lords Hansard, 28 March 2006, column GC326).

[35] UK Companies Act 2006, House of Lords Hansard, 28 March 2006, column GC326 and 16 May 2006, column 217

Recommendation 3.40

The words "unless the Court orders otherwise" should be inserted preceding the numerical majority requirement in section 210(3). This would serve the twin purpose of dealing with cases of "share-splitting" and allowing the court latitude to decide who the members are in a particular case.

Recommendation 3.41

For the purposes of section 210, if a majority in number of proxies and a majority in value of proxies representing the nominee member voted in favor of the scheme, it would count as the nominee member having voted in favour of the scheme.

(c) Look-through to beneficial shareholders

153 Where shares are registered in the name of a nominee, the beneficial owners of shares currently do not have the right to vote on section 210 schemes. For example, there might be instances where a Singapore company has shares listed overseas which are held by a foreign depository in the same way that the CDP holds Singapore-listed shares. Section 130D of the Companies Act provides for a look-through to the members behind the CDP so that the actual owners of shares retain their rights as shareholders. But there is no such provision in relation to overseas-listed shares.

154 Technically, the beneficial owners of the shares are not "members" and hence cannot participate in the major decision involved in a section 210 proposal. Such issues may also arise in dual listing situations and so are likely to become more prevalent as the number of dual listings grows.

155 The Steering Committee has considered whether introducing a definition of "members" would be a feasible solution to this problem but decided against it as it would be impractical to formulate an all-encompassing definition which is not too wide.

156 The Steering Committee also considered if there should be a prescribed list of depositories (e.g. the Depository Trust Company (DTC) which is a limited-purpose trust company under New York State banking law and a registered clearing agency with the SEC, USA and CPF Nominee Banks) for which a look-through to the shareholder would apply, but decided against it. There were mixed views received from the consultation. Some agreed with observations regarding the problems faced in extending the 48-hour rule for notional closure of the membership register to overseas-listed Singapore-incorporated companies. Another alternative view was that the appointment of proxies to attend the meetings should suffice. In conclusion, the Steering Committee agrees that a consistent approach should be adopted on this issue and recognition of overseas depositors for all matters under the Companies Act.

<u>Recommendation 3.42:</u>

For the purposes of section 210, where shares are registered in the name of a nominee that is a foreign depository, there is no need to provide for a look-through to the actual beneficial shareholders.

(d) Definition of "company"

157 The word "company" is defined differently in sections 210(11) and 212(6) of the Companies Act, leading to different scope for each. The inconsistency should be resolved since section 212 is an extension of section 210 in that a scheme approved under section 210 may have to be carried into effect through section 212.

158 Section 210(11) states that "'company' means "any corporation or society liable to be wound up under this Act". Section 212(6) states that "Notwithstanding section 210 (11), "company" in this section does not include any company other than a company as defined in section 4."

159 The section 212(6) definition is more restrictive since it excludes foreign companies. Foreign companies can be wound up under section 351 of the Companies Act and so fall within the section 210(11) definition.

160 The reason for the narrower section 212 definition appears to be historical. Palmer's Company Law: Annotated Guide to the Companies Act 2006[36] suggests that the more restrictive definition of "company" in the UK equivalent of section 212[37] is derived from section 208 of the 1948 UK Act and best justified on the grounds of practicability. Presumably the reference to "practicability" is the avoidance of problems of cross-border administration of orders for the transfer of the whole or part of the property or liabilities and/or the dissolution (without winding up) of the company or corporation. However, these problems are not insurmountable today. In fact provisions in the Singapore Banking Act and Insurance Act akin to the Companies Act amalgamation provisions already extend to foreign companies. Part VIIA of the Banking Act deals with transfers of business involving *inter alia* Singapore branches of foreign-incorporated banks. In the Insurance Act, section 47 is a similar provision. Just as those extend to foreign entities, section 212 should also be extended to foreign companies to facilitate cross-border transactions.

161 By way of comparison, section 413 of the Australia Corporations Act 2001 (equivalent to section 212 of the Singapore Companies Act) includes foreign companies. There the term "Part 5.1 body" is used, defined at section 9 to include a registrable Australian body or a foreign company that is registered under Division 1 or 2 of Part 5B.2. The comparable New Zealand provisions at Part 15 of the New Zealand Companies Act 1993 also extend to foreign companies.[38]

[36] London: Sweet & Maxwell, 2007, pages 669 and 673.
[37] New section 900 of the UK Companies Act 2006.
[38] See section 235.

162 In view of the above, the Steering Committee recommends that sections 210 and 212 apply to both companies and foreign companies. All respondents consulted supported this proposal.

<u>Recommendation 3.43</u>

Sections 210 and 212 should apply to both "companies" and "foreign companies".

(e) Binding the offeror

163 Currently section 210 of the Companies Act and the associated provisions do not have binding force on the offeror. The offeror is not a party to section 210 arrangements and the court's approval does not render it binding on the offeror (although sometimes the offeror does voluntarily appear for court proceedings or agree to be bound). What binds the offeror is only the antecedent implementation agreement between the offeror and the target company. This can cause difficulties.

164 The Steering Committee has considered whether the law should require the offeror to be party to the scheme. However, this is unnecessary as the court already has the power to require that the offeror be a party to the scheme before granting approval. Shareholders may have recourse against errant offerors through the Securities Industry Council (SIC). Furthermore, the Singapore regime is in line with the other major jurisdictions considered. All respondents agreed with the Steering Committee.

<u>Recommendation 3.44</u>

Section 210 and associated provisions should not be amended to provide for the scheme to be binding on the offeror.

(f) Compliance with the Code of Takeovers and Mergers

165 Section 210 is sometimes used to effect takeovers and mergers but compliance with the Code of Takeovers and Mergers is not specifically mandated or provided for in the provisions.

166 By way of comparison, the Australia Corporations Act 2001 specifically states at section 411(17) that the Court must not approve a compromise or arrangement unless there is produced to the Court a statement in writing by the Australian Securities and Investments Commission (ASIC) stating that ASIC has no objection to the compromise or arrangement. There is no equivalent in the UK or New Zealand.

167 The Steering Committee has considered whether the SIC should be required to approve the transaction before court sanction. Another approach would be to state in the legislation that there must be compliance with the Code of Takeovers and Mergers in relation to companies which are regulated by the Code before court sanction can be obtained. After consideration, the Steering Committee is of the view that it would be more in keeping with

the self-regulatory nature of securities regulations to leave matters as they stand. The obligation to comply with the Code already exists. It remains open to the SIC or any aggrieved shareholder to make an application to the court in an appropriate case. All respondents consulted supported this approach.

Recommendation 3.45

Section 210 need not be amended to specifically provide that section 210 schemes should comply with the Code of Takeovers and Mergers or be approved by the Securities Industry Council.

XIII. COMPULSORY ACQUISITION

(a) Holders of units of shares

168 Unlike the relevant Australian[39] provision, the UK equivalent of section 215 of the Companies Act covers not only shares but extends to convertibles as well.[40] This makes sense as section 215 is meant to allow the offeror to mop up remaining minority positions to complete the takeover of a company. The Steering Committee is of the view that Section 215 should extend to options and convertibles of all sorts, and this is supported by all respondents consulted.

169 The comparable New Zealand provision is not in the New Zealand Companies Act 1993 but is at Part 7 of the Takeovers Code.[41] Compulsory acquisition extends to equity securities which includes convertibles.[42]

Recommendation 3.46

Section 215 should be amended to extend to units of a company's shares.

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[39] Section 414 of the Australia Corporations Act 2001

[40] Section 989(1) of the UK Companies Act 2006 states "(1) For the purposes of this Chapter securities of a company are treated as shares in the company if they are convertible into or entitle the holder to subscribe for such shares. References to the holder of shares or a shareholder are to be read accordingly." Section 979 (the UK equivalent of section 215) is within the same chapter as section 989 and so it extends to convertibles.

[41] At http://www.takeovers.govt.nz/code/index.html. This is not universally applicable though – it is generally restricted to listed companies and companies with 50 or more shareholders.

[42] "Equity Security" is defined in rule 3 of the New Zealand Takeovers Code. "Equity security" is defined as follows:

"Equity Interest -

(a) means any interest in or right to a share in, or in the share capital of, a company (whether carrying voting rights or not); and

(b) includes an option or right to acquire any such interest or right unless that option or right is exercisable only with the agreement of the issuer; but

(c) does not include redeemable securities that are redeemable only for cash".

(b) Individual offerors

170 Currently section 215 of the Companies Act applies to transfer of shares in one company to "another company or corporation". As noted in Walter Woon on Company Law at paragraph 15.165, "this section cannot be invoked by a natural person". However there is no good reason why it should not be.

171 The equivalent provision in the Australia Corporations Act 2001 is section 414. Section 414 uses the word "person" instead of "company or corporation" and so covers individuals as well. The position is similar in New Zealand.[43] Section 979 of the UK Companies Act 2006 uses "offeror" which can also encompass individuals.

172 The Steering Committee recommends that Section 215 should be broadened to include transferees who are individuals rather than being restricted to companies and corporations and this was supported by all respondents consulted.

<u>Recommendation 3.47</u>

Section 215 should be extended to cover individual offerors.

(c) Joint offers

173 Section 215 of the Companies Act confers squeeze-out rights to an offeror company in a takeover to acquire shares of the dissenting minority if 90% of the target company shareholders have approved the takeover offer. Subsection (3) provides sell-out rights to shareholders. It should be made clear that where a takeover offer is made jointly by more than one person, all the joint offerors have the same legal obligations. In the UK Companies Act 2006, section 987 deals specifically with joint offers. A similar provision should be added to the Singapore Companies Act. All respondents consulted agreed with the Steering Committee.

174 In the different wording used in Part 7 of the New Zealand Takeovers Code[44], joint offers are also covered. However, the equivalent provision in the Australia Corporations Act 2001, which is section 414(2), uses the word "person" with no specific mention of joint offers.

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[43] Part 7 of the New Zealand Takeovers Code uses the term 'dominant owner'.

[44] The relevant phrase in the New Zealand Takeovers Code is "dominant owner" and it is defined thus: "in relation to a code company, means a person who, after this code comes into force, becomes the holder or controller, or 2 or more persons acting jointly or in concert who, after this code comes into force, become the holders or controllers, of 90% or more of the voting rights in the code company (whether by reason of acceptances of an offer or otherwise)".

<u>Recommendation 3.48</u>

A provision similar to section 987 of the UK Companies Act 2006 on joint offers should be added to the Singapore Companies Act.

(d) Associates

175 In ascertaining whether the offeror has reached the 90% threshold, shares held by the offeror are excluded. Section 215(9) of the Companies Act states that shares held or acquired by the offeror's nominee or related corporation (or its nominee) are to be treated as held by the offeror. Section 6 of the Companies Act then defines a "related corporation". The rationale of the exclusions is that the offer should be accepted by 90% of the shareholders who are unaffiliated with the offeror before section 215 rights are activated. However, the scope of those excluded currently does not adequately cover persons connected to the offeror.

176 The UK approach is to exclude shares acquired by an "associate".[45] The definition of "associates" is very comprehensive and suitable for adoption in Singapore with any required modifications. It may be necessary to specifically provide exemption to very large holding companies with interests in many companies. Most respondents consulted agreed with this proposal.

177 The relevant provision in Australia is section 414(2) of the Corporations Act 2001 which excludes shares held by "the person or a nominee of the person; or if the person is a body corporate – a subsidiary of the body". There appears to be no comparable exclusion under the New Zealand Takeovers Code.

<u>Recommendation 3.49</u>

The UK definition of "associate" should be adopted for parties whose shares are to be excluded in calculating the 90% acceptances for section 215.

<u>Recommendation 3.50</u>

There should be provision for Ministerial exemptions for very large holding companies with interests in many companies.

(e) Threshold for squeeze-out rights

178 Section 215 only applies one test: agreement of 90% of unaffiliated shareholders. However, Bermuda allows squeeze-out rights to the holders of not less than 95% of the shares of a company with no restriction to unaffiliated shareholders.

[45] Section 983(8) of the UK Companies Act 2006. The definition of "associates" is in section 988.

179 The Steering Committee considered a suggestion to expand section 215 with an alternative threshold. The following justifications were offered:

(a) If the offeror has 95% shareholding, a listed company could be delisted thereby removing marketability and hence subjecting the shares to potential undervaluation arising from the imposition of a minority discount.

(b) A 5% minority has no meaningful rights in any event and so should not be allowed to block the progress of a transaction which such large majority of voting shares have weighed in favor of. With 95% shareholding, the majority can convene meetings at short notice whereas the minority has no right to convene meetings and no right to request for information except annual reports with no prescribed content. The only remedy for the minority is contractual or by an oppression action, which is a tough proposition likely to result in an order to sell at discount due to the small minority stake.

(c) Minority shareholders may be uncontactable or may include estates of deceased persons, which has its own complexities.

(d) In any event, if any shareholder is aggrieved, the right would remain to apply to court to block the acquisition and the court has a number of remedies including determining whether the price offered was fair. Although appraisal rights, as a concept and remedy to minority shareholders, is not explicitly provided for, it is in effect available as a remedy in an action for minority oppression under section 216 of the Companies Act.

180 The Steering Committee was not unanimous on this issue. When consulted, mixed views were received. The alternative views were :

(a) Other major jurisdictions like the UK, Hong Kong and Australia have not adopted such a policy. Foreign investors may be more comfortable with the existing system, which offers more protection to the minority shareholders but still provides for a sensible squeeze-out system. To maintain Singapore's reputation as a reputable international financial centre, it is preferable to maintain the present regime.

(b) The ability of the 5% minority to potentially block a transaction (unless approval of 90% of shares of unaffiliated shareholders is obtained) is itself a meaningful right. Further, a 5% shareholder would be regarded as a substantial shareholder, connoting a not-insignificant level of influence over the company. In the absence of countervailing public interest, minority shareholders ought to be given a choice whether to sell out or remain shareholders. Currently, the law provides a route for the majority to buy out the minority by meeting the test of 90% of shares of unaffiliated shareholders. Justification has to be shown as to why this test is inadequate and an alternative test introduced. In relation to the point that the company can be delisted and minorities subjected to a minority discount, this does not mean that the majority should therefore be allowed to squeeze out a minority shareholder who, for some reason, chooses to hold on to his shares.

181 In conclusion, the Steering Committee decided not to pursue the Bermuda model as no other leading jurisdictions have introduced such a policy and there were no strong calls for such a policy.

182 The proviso to section 102 of the Bermuda Companies Act, which is similar to that in section 414(5) of the Australia Corporations Act 2001, was also considered but was rejected as an unnecessary complication which serves no useful purpose. Under those provisions, if the offeror already holds over 10% of the target company shares, added restrictions are put in place before the buyout rights kick in. The added restrictions are that the offer must be extended to all shareholders and must be approved not only by 90% of unaffiliated shareholders' shares but also at least ¾ in number of unaffiliated shareholders. This issue does not arise in the New Zealand context where the Takeover Code focuses on the dominant shareholder having a 90% shareholding rather than acquiring 90% of excluded shares.

Recommendation 3.51

A new 95% alternative threshold for squeeze out rights along the lines of section 103(1) of the Bermudan Companies Act was considered but not recommended.

(f) Cut-off date

183 Section 215 of the Companies Act currently does not fix a point in time at which to determine whether the 90% threshold has been reached, presumably leading to the default position that shares issued after the takeover offer would have to be factored in to calculate whether the 90% threshold has been reached. This has the drawback of putting the offeror in the position of potentially having to shoot for a moving target of 90% since the number of shares needed to reach that target changes if new shares are issued in the interim.

184 In contrast, section 979(5) of the UK Companies Act 2006 provides that "shares that are allotted after the date of the offer" and "relevant treasury shares … that cease to be held as treasury shares after the date of the offer" should be excluded in calculating the 90% threshold. Neither section 414 of the Australia Corporations Act 2001 nor New Zealand's Takeover Code has a similar provision.

185 To create greater certainty for the offeror, the Steering Committee is of the view that a cut-off at the date of offer should be in place for determining the 90% threshold for the offeror to acquire buyout rights. There were no opposing views received during consultation.

Recommendation 3.52

A cut-off at the date of offer should be imposed for determining the 90% threshold for the offeror to acquire buyout rights so that shares issued after that date are not taken into account.

(g) Computation of 90% threshold

186 In computing whether the 90% threshold has been reached, the question arises whether treasury shares should be included or excluded. Different considerations apply when considering this issue from the perspective of the offeror (whether the offeror should have squeeze-out rights) and the perspective of the minority shareholder (whether the minority should have sell-out rights).

187 Dealing with the offeror's perspective of squeeze-out rights, section 215(1) of the Companies Act provides that treasury shares should be excluded. The UK position stated at section 979(5) of the UK Companies Act 2006 is similar. The Steering Committee is of the view that this should not be changed – since the offeror is being allowed to overbear the minority shareholders, the threshold should be high.

188 Dealing with the minority shareholders' perspective of sell-out rights, section 215(3) also provides that treasury shares should be excluded. This is different from the UK position under section 983(5) which provides that "For the purposes of … calculating 90% of the value of any shares, shares held by the company as treasury shares are to be treated as having been acquired by the offeror." Neither section 414 of the Australia Corporations Act 2001 nor the New Zealand Takeover Code mentions treasury shares.

189 The UK position is preferable. Since the minority is in a position of disadvantage, the law should lean in favour of granting sell-out rights when the reality is that the offeror has control over 90% of the shares, including treasury shares. Including treasury shares recognises the reality that the offeror who crosses the 90% threshold when treasury shares are included is in any event already in a position to control the target company (and therefore the treasury shares) by virtue of his majority shareholding. There were no opposing views received during consultation.

<u>Recommendation 3.53</u>

Section 215(3) should be amended by deleting "(*excluding* treasury shares)" and substituting "(*including* treasury shares)" so as to grant sell out rights when the offeror has control over 90% of the shares, including treasury shares.

(h) Dual consideration

190 Section 215 of the Companies Act currently does not provide any regulation of offers involving a choice of consideration to be paid to the target company shareholders by the offeror. This is similar to the position in New Zealand but contrasts with the position in the UK and Australia.

191 Section 981(3) of the UK Companies Act 2006 gives the shareholder six weeks to elect for his choice of consideration and also states that the offeror must specify a default consideration if no election is done.

192 Section 414(4) of the Australia Corporations Act 2001 provides a shorter time frame of 14 days to a month (depending on when the offer is delivered) for election and allows the offeror to choose in default of election.

193 A period of two weeks should be adequate for shareholders to elect any choice of consideration. Offerors should also be required to state the default position if no election is made. There were no opposing views received during consultation.

Recommendation 3.54

Where the terms of the offer give the shareholders a choice of consideration, the shareholder should be given 2 weeks to elect his choice of consideration and the offeror should also be required to state the default position if no election is made.

(i) Unclaimed consideration

194 When an offeror has acquired minority shareholdings, section 215(4) of the Companies Act provides for payment of the price to the target company and section 215(5) provides that the target company shall hold the consideration received in trust for the share owners.

195 Section 215(6) states: "Where any consideration other than cash is held in trust by a company for any person under this section, it may, after the expiration of two years and shall before the expiration of 10 years from the date on which such consideration was allotted or transferred to it, transfer such consideration to the Official Receiver".

196 Section 215(7) states: "The Official Receiver shall sell or dispose of any consideration so received in such manner as he thinks fit and shall deal with the proceeds of such sale or disposal as if it were moneys paid to him in pursuance of section 322 (Companies Act)".

197 Feedback from industry is that it would be useful for the Official Receiver to similarly handle cash consideration as well. This would also be in line with the law in the UK as stated in section 982 of the UK Companies Act 2006.

198 Given that unclaimed consideration may also arise from sections 210 and 215A to 215J situations, a separate section similar to sections 215(6) and 215(7) should be enacted to allow transfer of consideration to the Official Receiver in all such situations. When consulted, there were no opposing views received.

199 Section 982 of the UK Companies Act 2006, which deals with unclaimed consideration for compulsory acquisitions extends to "money or other consideration"[46], although there is no similar provision for the equivalent of section 210 of Singapore Companies Act. Section 414(15) of the Australia Corporations Act 2001 is equivalent to section 210 of Singapore Companies Act. Section 414(15) of the Australia Corporations Act 2001 deals not only with cash consideration but with "any other consideration" as well. The

[46] See section 981(9).

New Zealand Takeovers Code provides in rule 61 that “must be held in trust for the outstanding security holders until it is claimed.”

<u>Recommendation 3.55</u>

The words “other than cash” in section 215(6) should be deleted so that all forms of consideration may be transferred by the target company to the Official Receiver if the rightful owner cannot be located. Such powers should be available in sections 210 and 215A to 215J situations as well.

(j) Overseas shareholders

200 Section 215 of the Companies Act deals with a scheme “involving the transfer of all of the shares ...”. This can lead to an argument that section 215 does not apply if every one of the shareholders has not had the offer delivered to them. Delivering the offer to every single overseas shareholder may however be unduly onerous or impossible where shareholders have no local address.

201 Section 978 of the UK Companies Act 2006 provides that an offer is not prevented from being a takeover offer if not communicated to shareholders with no local address in order not to contravene foreign laws as long as published on a website.

202 The Steering Committee is of the view that a provision similar to section 978 of the UK Companies Act 2006 should be incorporated into the Singapore Companies Act, but with a broader ambit so that exemption applies whenever it is “unduly onerous” to serve the offer on the overseas shareholders or when it would contravene foreign law. It may for example be unduly onerous due to cost. It can be left to the court to decide whether in any case it is unduly onerous or not.

203 By way of comparison, section 414 of the Australia Corporations Act 2001 on compulsory acquisition deals with “a scheme or contract … involving a transfer of shares ...” and so does not require that the scheme involve a transfer of all shares.

<u>Recommendation 3.56</u>

An exemption should be added so that if overseas shareholders are not served with a takeover offer, that does not render section 215 inapplicable as long as service would have been unduly onerous or would contravene foreign law.

XIV. AMALGAMATIONS

(a) Short form amalgamation of holding company with wholly-owned subsidiary

204 Pursuant to the recommendation of the CLRFC, the Companies (Amendment) Act 2005 introduced two methods of amalgamation based on the New Zealand model. The provisions at sections 215A to 215J of the Companies Act allow amalgamation of companies with shareholder approval and solvency statements of the directors, without the necessity of court approval. Apart from normal amalgamations, short-form amalgamations involve either vertical amalgamation of a holding company and one or more wholly-owned subsidiaries or horizontal amalgamation of two or more wholly-owned subsidiaries.

205 It is currently not clear whether a holding company may amalgamate with its wholly-owned subsidiary by short form if it is the subsidiary which is to be the amalgamated company or whether it is only the holding company which can be the amalgamated company in a short-form amalgamation. There may be reasons why it may be preferred to have the subsidiary company survive – eg, for tax benefits. Accordingly it should be made clear that short-form amalgamations extend to those of a holding company with its subsidiary. When consulted, majority of the respondents agreed. However, IRAS pointed out that in most cases, the subsidiaries are the operating entities with tax losses and not the holding company. Allowing a holding company to amalgamate with its wholly-owned subsidiary by short form may encourage companies to amalgamate not for genuine commercial reasons but solely to derive a tax advantage through the amalgamation process thus defeating the original intention of the policy. However, the Steering Committee takes the view that the tax treatment should not dictate the policies but should instead be reviewed if necessary.

206 The comparable provision in New Zealand[47] is similar in this respect to the current Singapore provision in stating that short-form amalgamation applies where "A company and one or more other companies that is or that are directly or indirectly wholly owned by it may amalgamate and continue as one company (being the company first referred to)". There is no comparable UK or Australian provision as these jurisdictions do not have provisions specifically dealing with amalgamation, except for an equivalent of section 212 of the Singapore Companies Act.

<u>Recommendation 3.57</u>

It should be specifically stated that a holding company may amalgamate with its wholly-owned subsidiary by short form.

(b) Amalgamation of foreign companies

207 The Steering Committee has considered whether amalgamations involving foreign entities where the foreign entity survives should be allowed but decided against it because none of the other leading jurisdictions allows such amalgamations and it would be best to avoid potential jurisdictional issues that may arise from allowing them. When consulted, majority of the respondents agreed.

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[47] Section 222 Companies Act 1993.

Recommendation 3.58

The amalgamation provisions should not be extended to foreign companies.

(c) Amalgamation of companies limited by guarantee

208 Section 215A of the Companies Act contemplates that "two or more companies may amalgamate and continue as one company, which may be one of the amalgamating companies or a new company..". "Company" as defined in the Companies Act includes a company limited by guarantee.

209 However, section 215B(1)(d) indicates that the amalgamation proposal should state, amongst other things, the "share structure of the amalgamated company". There are also other references to "shares" and "share capital" of the amalgamating company, eg at sections 215B(1)(f) and (g), 215B(3), 215B(4), 215D(1)(a) and 215D(2)(a).

210 Paragraph 6.1 of the CLRFC report explained why the committee recommended amalgamations: "In today's business environment of mergers and amalgamations of companies, it is timely for Singapore to introduce a merger process that is clear and efficient and which is tax neutral".

211 It appears therefore that the amalgamation provisions were introduced to facilitate businesses rather than for companies limited by guarantee, which generally do not carry on business activities.

212 The Singapore provisions on amalgamation were based on those found in the New Zealand Companies Act 1993. However, this issue of amalgamation of companies limited by guarantee does not arise under New Zealand law because section 10 of the New Zealand Companies Act 1993 provides that, "A company must have … one or more shares". As such no guidance on this issue is provided by the New Zealand Act.

213 In keeping with the original intention of the CLRFC, amalgamation should not be available to companies limited by guarantee. When consulted, there were alternative views that companies limited by guarantee may also see the need to merge and amalgamate for greater efficiency and economies of scale. There is no good reason why companies limited by guarantee should not be permitted to do so via statutory means. Nevertheless, the Steering Committee was not persuaded.

Recommendation 3.59

The amalgamation provisions should not be extended to companies limited by guarantee.

(d) Solvency statement

214 On the requirement that directors of each amalgamating company should give a solvency statement in relation to the amalgamated company,[48] industry feedback is that the forward-looking solvency statement requirement for the amalgamated company is an onerous requirement. This is so especially for directors of the amalgamating company who would not be serving on the board of the amalgamated company, and where the transaction involves leveraged financing.

215 Sections 215A to 215J are similar to Part XIII of the New Zealand Companies Act 1993.[49] Like the Singapore amalgamation provisions, the New Zealand provisions also require the boards of each amalgamating company to be satisfied that the amalgamated company must pass a solvency test. However, unlike Singapore, New Zealand does not require each amalgamating company to assess its solvency status before the amalgamation.

216 The Steering Committee considered the following two options:

(a) Option One - The boards of the amalgamating companies must make a solvency statement regarding the amalgamating company at the point in question and within a 12-month forward-looking period. The components of the solvency test will be assets/liabilities and ability to pay debts. It is reasonable and logical that two solvent companies will form a solvent amalgamated company. However, as some companies may not feel comfortable or may not have sufficient knowledge to comment on the solvency status of an amalgamated company, such companies should still be permitted to amalgamate if they can be satisfied that they would nevertheless be solvent at the point in time and in the 12 months ahead, if they have not amalgamated. This is consistent with the solvency test imposed on capital maintenance transactions.

(b) Option Two - Retain the present solvency test for amalgamations, but only require the boards of the amalgamating companies to comment on the amalgamated company's ability to pay its debts as they fall due at the point when the amalgamated company is formed. It may be difficult to expect the amalgamated company to predict its solvency status in the 12 months ahead, considering that the board may consist of members from amalgamating companies and have a different business strategy.

217 When consulted, there were mixed views. Supporters of Option One were of the opinion that it is important to retain the forward-looking component to ensure that the directors involved have duly considered the financial consequences of the amalgamation and are satisfied that it will not result in an amalgamated company that is likely to become insolvent within a 12-month period. Supporters of Option Two were of the opinion that Option One is counter-factual while Option Two is consistent with the New Zealand/Canadian model and there was no evidence of adverse outcomes in these jurisdictions. Some commented that both options are workable and allowing the company to

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[48] Found in sections 215C(2)(c) and 215J(1).

[49] Sections 215A to 215J were modelled on sections 188 to 194A recommended by the New Zealand Law Commission Company Law Reform: Transition and Revision No. 16 – see paragraph 6.3 of the Report of the Company Legislation and Regulatory Framework Committee of Singapore, October 2002. The current New Zealand amalgamation provisions are at Part 13, sections 219 to 226 of the New Zealand Companies Act 1993.

elect one option suitable for its circumstances was ideal and would promote the amalgamation regime while another school of thought is of the opinion that allowing an option was not appropriate and it was preferable to impose one uniform requirement for consistency and fairness.

218 Having considered the differing views expressed, the Steering Committee recommends Option One as it is more meaningful and prudent as well as consistent with the solvency test imposed on capital maintenance transactions.

Recommendation 3.60

The boards of amalgamating companies should make a solvency statement regarding the amalgamating company at the point in question and within a 12-month forward-looking period. The components of the solvency test will be assets/liabilities and ability to pay debts.