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FACTORING AND STAMP DUTY IN SINGAPORE AND MALAYSIA

Arab-Malaysian Merchant Bank Bhd v
Boustead Trading (1985) Sdn Bhd[1]

Background

IT is conventional wisdom in the legal profession that master factoring agreements do not have to be stamped for the purposes of the Singapore Stamp Duties Act.[2] Stamp duty is a tax payable on instruments, not transactions, which effect the sale of any property at law or in equity. If the factoring agreement results in the conveyance of a debt, the sums involved would not be small since *ad valorem* stamp duty is payable.[3] Most lawyers have therefore taken the view that the master agreement, if drafted properly, results only in an equitable assignment which does not immediately effect the transfer of debts. The actual conveyance takes place subsequently without any stampable documentation. The holding of Abdul Malek J of the High Court of Kuala Lumpur in *Arab-Malaysian Merchant Bank Bhd* v *Boustead Trading (1985) Sdn Bhd* that the master agreement is a statutory assignment is therefore bound to cause some disquiet in Singapore.[4]

The facts were unexceptional. The plaintiffs, Arab-Malaysian, entered into an agreement with Chemitrade Sdn Bhd on 23 October 1989 in which Chemitrade factored or assigned all debts owing to it to the plaintiffs. It was provided that the plaintiff had an absolute discretion whether to accept any of the debts offered by communicating its acceptance verbally or otherwise.

1 [1994] 1 MLJ 624.

2 (Cap 312, 1985 Rev Ed). In Malaysia this would be the Stamp Duty Act 1949.

3 In the following order in Art 16, Sched 1, Stamp Duties Act: 1% on the first $90,000, 2% on the next $60,000 and 3% on the remainder. In England, Section 109, Finance Act 1984 imposes a duty of 1% *ad valorem* on conveyances or transfers of property with a certified value of above 30,000 pounds.

4 *Supra,* n 1. There is little concern in Malaysia since their equivalent provision, Item 32, Sched 1, Stamp Duty Act 1949, has a subsection (c) which only imposes a RM 5 duty "On the absolute sale of any accounts receivable or book debts to a bank, merchant bank, or borrowing company in Malaysia approved by the Minister of Finance, pursuant to a factoring agreement."

On 15 November 1989, the defendant, Boustead Trading (1985) Sdn Bhd, was appointed by Chemitrade as its sole distributor. Chemitrade would sell goods to the defendant for the latter to resell. An invoice would be issued at that time, payment to be made 60 days after that. In the interim, there would be an unpaid debt due from the defendant to Chemitrade. Pursuant to the factoring agreement, Chemitrade notified the defendant of the assignment by letter of notification on 13 February 1990 which was acknowledged by the defendant. The plaintiff also sent a similar letter of notification to the defendant on 14 February 1990. Further, all of Chemitrade's invoices to the defendant were endorsed with the notice of assignment from Chemitrade to the plaintiff.

The defendant refused to pay the plaintiff on the ground that the assignment was incomplete. It was argued that the master agreement required a further act of assignment. Clause 18 of the agreement stated that "whenever requested by the plaintiff, Chemitrade at its own cost is to execute, stamp and deliver to the plaintiff a deed assigning to the plaintiff any purchased debt." Simply put, the master agreement was only a standing offer of sorts for the subsequent transfer of debts arising from time to time, which had to be by deed.

Abdul Malek J, quite rightly, held that Clause 18 was not mandatory so that there was no necessary act contemplated by both parties before an assignment was effected. The difficulty is that the learned judge went on to say that

> The said factoring agreement, therefore, has complied with section 4(3) of the Civil Law Act 1956 in that it is an absolute assignment in writing under the hand of Chemitrade of a debt of which express notice in writing had been given to the defendant from whom the plaintiff would have been entitled to claim without the concurrence of Chemitrade.[5]

Is the Master Factoring Agreement a Statutory Assignment?

That the learned judge found it necessary to find that there was a statutory assignment could be due to defence counsel's lengthy submission on section 4(3) of the Civil Law Act 1956. Indeed, it has been held by the High Court of Australia in *Olsson* v *Dyson*[6] that since the introduction of statutory assignment, the equitable form of assignment has been truncated, so that where a *legal* chose is concerned, as the debt here was, a valid assignment would require compliance with section 4(3) of the Civil Law Act 1956. However, Professor Furmston states that this view does not represent English

[5] *Supra*, n 1, at 628. In Singapore, statutory assignments are effected by s 4(6) of the Civil Law Act (Cap 43, 1988 Rev Ed).

[6] (1969) 120 CLR 365. The five-judge court was unanimous on this point.

law, which treats the statutory form of assignment as a procedural convenience that does not create or abolish substantive rights.[7] FR Salinger also says that "the statute has in no way detracted from the efficacy of equitable assignments and the position in relation to them remains exactly as it was before 1873."[8]

Certainly in Singapore, Lai Kew Chai J had no difficulty in finding that there was an equitable assignment of a debt in *Interschiff Schiffahrtsagentur GmbH* v *Southern Star Shipping & Trading Pte Ltd*.[9] The doctrine that equity will not perfect an imperfect gift assumes that the transfer has not been perfected, given a prescribed method of perfection. With choses there is no reason why there cannot exist two different methods of perfection, one statutory, the other equitable.[10] Put differently, the efficacy of the factoring arrangement did not require the judge to hold that it was a statutory assignment, especially since consideration was clearly furnished. The factor is not a volunteer seeking the assistance of equity.

The danger with finding a statutory assignment in such a situation in England is best put by AN Cox and JA Mackenzie: "Equitable assignments are more usual since they avoid the 1% ad valorem stamp duty imposed on legal assignments. Stamp duty, illogically, applied to legal assignments because it is a stamp on values shown in documents and not on transactions."[11] If the giving of notice retrospectively converts the master agreement, at its inception an equitable assignment due to the lack of notice, into a statutory assignment, the ramifications are not hard to imagine. This consideration did not trouble Abdul Malek J since *ad valorem* duty is not imposed on factoring agreements in Malaysia by virtue of Item 32(c) of the First Schedule to the Malaysian Stamp Duty Act 1949.[12] Yet the learned judge only lifted the veil on what was transparently a tax avoidance scheme.

It cannot be questioned that an equitable assignment can be perfected into a statutory one. However, whereas a statutory assignment requires an absolute assignment of an existing chose in action, equitable assignments can take one of three forms, not all of which are capable of conversion into statutory assignments without fresh documentation. First, there is the absolute assignment which fails for some reason as a statutory assignment. Second, a declaration of trust which serves to transfer the beneficial interest

7 Cheshire, Fifoot and Furmston, *Law of Contract* (12th ed, 1991), at 511-512.

8 *Factoring Law and Practice* (1991), at 131-133.

9 [1984] 1 MLJ 342.

10 The advantage of the former is that there is no need to join the assignor for a legal chose to be enforced. Equitable assignments of equitable choses never faced this procedural problem either.

11 *International Factoring* (1986), at 32-34.

12 See *supra*, n 4.

in the chose to the donee. Third, a promise for consideration to assign which is contractually binding on the assignor.

The courts will not construe one mode of transfer as another, so that a trust, for example, will not be spelt out of a failed absolute assignment.[13] The converse must be true. Consequently, it is likely that only the first form of equitable assignment can be converted into a statutory assignment once the other requirements of the statute are fulfilled, *viz*, written notice to the debtor, so that the original written instrument of assignment forms the basis of the statutory assignment. The reason for this is that an absolute assignment envisages an immediate transfer of the donor's entire interest, which a declaration of trust and an agreement to assign cannot achieve.

Most master factoring agreements take the third form. This is normally referred to as a facultative agreement in the sense that debts will be offered to the factor as they arise, to which the factor can give an unwritten acceptance by conduct. Such was the agreement in *Arab-Malaysian*. F Oditah refers to this as an option or unilateral contract.[14] This though is not strictly correct since there can be no contract before the acceptance of an offer. The reason why it looks like a contract is that the supplier cannot revoke the offer, but this is not because of a unilateral contract, which is a fiction, but a collateral contract that keeps the offer open. If so the act that assigns the debt is the acceptance or acquiescence of the factor, not the master agreement.[15] Most factoring transactions also cover future debts which can only take effect as a binding promise to assign as and when those debts arise. The common law does not envisage the present transfer of future property and demands that a fresh conveyance be executed once the property exists. Equity looks upon it in the same way as a future transfer of present property, which is only possible via a contract.

The facultative agreement is thus not an absolute assignment itself and cannot satisfy the requirements of section 4(6) of the Civil Law Act in Singapore. An analogy can be drawn with the transfer of goods or choses in possession, the other category of personal property.[16] While a gift (assignment) is a conveyance without contract, a sale (agreement to assign) is a conveyance preceded by a contract. No doubt the presumption in the sale of specific

[13] See *Milroy* v *Lord* (1862) 4 De GF & J 264; *Olsson* v *Dyson*, *supra*, n 6.

[14] *Legal Aspects of Receivables Financing* (1991), at 47.

[15] A sample clause would read: "The Vendor may from time to time offer to sell and the Purchaser may purchase upon the terms and conditions contained below all or any debts which are now owing or during the continuance in force of this agreement become owing to the Vendor from a customer in respect of goods or services supplied or contracted to be supplied to such customer PROVIDED that nothing either in this agreement or elsewhere shall impose upon the Purchaser any obligation to purchase all or any of the debts so offered." *Encyclopedia of Forms and Precedents* (5th ed, 1986), Vol 4, Form 45 at 180.

[16] Leaseholds are a peculiar category of personal property; chattels real, which the law treats more as real property.

goods is that property passes at the time of contract,[17] but this is subject to the contrary intention of the parties.[18] With the factoring of existing debts, that the commencement date of the assignment is sometime in the future, shows clearly that the parties intend to delay the passing of property in the debts. With future choses, much like future goods, it is impossible for property to pass until the choses mature or the goods become existing, as the case may be.[19] In such sale of goods agreements, it is clear that the contract is not the conveyance and never can be so. The master factoring agreement, unless drafted as an absolute assignment, cannot therefore be a statutory assignment without a further instrument of assignment. The court will not search for validity through one form when another was intended.

In *Arab-Malaysian*, Abdul Malek J left open the issue of whether the written notification could itself form the basis of the statutory assignment. That the written notification could itself be the relevant stampable instrument even if the property interest passed *de hors* of it is supported by the majority of the House of Lords in *Oughtred* v *IRC*.[20] There, even though the relevant company shares had passed under the contract of sale through the imposition of a constructive trust, a subsequent superfluous deed of transfer was stampable. The case, however, has been much criticised since the deed itself was clearly not an assignment but only evidence of it.[21] Besides the problem is easily side-stepped by not having written notification since there is no requirement of formal notice in equitable assignments, which is something that would have commended itself to four of the five Law Lords in *Oughtred's* case.[22]

Is Stamp Duty Payable Regardless?

The proposition that the master factoring agreement is not a statutory assignment is premised on the primacy of form over substance in that one method of assignment will not be upheld as another. This does not rule out the possibility that an agreement to assign does in itself effect the transfer of a debt in equity and hence come within the purview of the stamp duty legislation. It can be argued that a constructive trust arises on a contract of sale which is specifically enforceable, as equity deems done that which ought to be done. We have recently seen liberal use of this doctrine by

17 S 18 r 1, Sale of Goods Act 1979.

18 S 17, Sale of Goods Act 1979.

19 S 5(3), Sale of Goods Act 1979. This has been reaffirmed recently by the Privy Council on appeal from New Zealand in *Kensington* v *Unrepresented Non-allocated Claimants, Liggett* (The Times, 2 June 1994).

20 [1960] AC 206.

21 F Oditah, *supra*, n 14, at 48.

22 See further *Re Holt's Settlement* [1969] 1 Ch 100; *DHN Food Distributors Ltd* v *Tower Hamlets Borough Council* [1976] 1 WLR 852.

the Privy Council in *A-G of Hong Kong* v *Reid*.[23] Were the doctrine of conversion to operate in the factoring context, the supplier would be deemed a trustee of the existing debts for the factor from the moment of contracting, and at the time the debts arise for future debts.[24]

The equitable maxim does, however, have its limits. With factoring arrangements, if what equity deems done were in fact done, the debts would still not be transferred by the master agreement for the reasons above: the parties' intentions and the impossibility of transferring future debts presently. Further, liberal use of the doctrine of conversion could allow for the recovery of personal property *in rem*, when the general rule is that protection of such property is normally through an award of damages for breach of contract or for the tort of conversion. The distinction between land and personalty would be eroded.[25]

But that is not dispositive of the matter. True it is that courts today are more prepared to accept that the form of an agreement reflects the substance of the parties' intentions.[26] However, the contest in such situations is often restricted to private actors. Where the state has a compelling interest, the law is less reticent to go behind the observable facts to impute intentions. Section 22(1) of the Singapore Stamp Duties Act states that:

> Any contract or agreement for the sale of any equitable estate or interest in any property whatsoever,... shall be charged with the same ad valorem duty, to be paid by the purchaser, as if it were an actual conveyance on sale of the estate, interest or property contracted or agreed to be sold.

The argument that the master agreement only constitutes an offer for the subsequent transfer of debts lacks subtlety since it is obvious that the postponement of the commencement date is only for the purposes of avoiding stamp duty. The reality is that the supplier is bound, by the collateral contract or option paid for by the advance from the factor, to offer the debts listed in the schedule to the master agreement. Additionally, the subsequent written notification could be stampable, even if it does not effect the assignment, if the court finds that the notification and the actual assignment, which

[23] (1993) 3 WLR 1143. See RC Nolan, Note (1994), Vol 15 No 1 The Company Lawyer 3. Further reservations over the use of the maxim are expressed by P Watts (1994) 110 LQR 178; AJ Oakley [1994] CLJ 31.

[24] It seems unquestioned that contracts concerning choses in action are specifically enforceable; see *Tailby* v *Official Receiver* (1888) 13 App Cas 523. *Cf* E Ferran, *Mortgage Securitisation* (1992), at 43.

[25] Which does not sit comfortably with *Re Wait* [1927] 1 Ch 606. *Cf Holroyd* v *Marshall* (1862) 10 HL Cas 191.

[26] *Welsh Development Agency* v *Export Finance Co Ltd* [1992] BCLC 148.

occurred orally or through the factor's acquiescence, were "all one transaction".[27]

If so the only reason why the Inland Revenue Authorities have not come down hard on master factoring agreements is that it is often impossible to ascertain the value of the consideration for the purchase of debts, given that the commencement date of the agreement is normally sometime in the future. The factor can reject a particular debt that is offered to it, which has a purchase price adjustable according to the maturity of the debt and the rate of discount. The discounting of future debts subsequent to the commencement date is also envisaged, which value cannot be ascertained. As F Oditah points out it would be difficult to assign a contingent figure to the assignment since there is no minimum, maximum or specified amount payable under the master agreement.[28] For most lawyers, however, this would not be a satisfactory way to hinge the matter since it is dependant on the goodwill of the authorities which could easily decide that a prospective *ad hoc* figure first be imputed to the master agreement and then varied over time as the debts are actually assigned.

Solutions

One possible way to get round the problem is to invoice discount rather than factor. Here the transaction would be perceived as a loan by the factor to the supplier which is secured by a mortgage over the receivables.[29] The maximum stamp duty payable on such secured transactions in Singapore is $500.[30] The balance sheet of the supplier would, however, be weakened since factoring is a means of off-balance sheet financing. Furthermore its efficacy depends ultimately on whether the courts view the transaction as a sham, in that the transaction is really one of sale rather than a loan.[31] Since the doctrine of sham, seldom successfully invoked, addresses the reverse situation where what is really a secured loan is dressed up as a sale to avoid problems of registration of charges, this should not be a major concern.

27 *Sergeant & Sims on Stamp Duties* (10th ed, 1992), at 29.

28 *Supra*, n 14, at 48.

29 Interestingly, a legal mortgage is considered an absolute assignment, *Tancred* v *Delagoa Bay Railway Co* (1889) 23 QBD 239.

30 Art 31, Sched 1, Stamp Duties Act. See R Chandran "Stamp Duty Implications in an 'Open' or 'All Monies' Mortgage" (1993) 5 S Ac LJ 102. The Malaysian equivalent, Item 27(d), Sched 1, Stamp Duty Act 1949 only imposes a RM 5 duty on "A charge or a mortgage on or an assignment by security of accounts receivable to a bank, merchant bank or borrowing company in Malaysia approved by the Minister of Finance, pursuant to an agreement for discounting invoices or hire purchase receivables."

31 *Snook* v *London & West Riding Investments Ltd* [1967] 2 QB 786 at 802.

It is no credit to the law if it is constantly circumscribed. Good rules bring about a coincidence between theory and practice. If we do believe that factoring is an economically useful activity, the way forward surely must be to follow the lead of the Malaysian Stamp Duty Act 1949, which imposes a fixed duty of only RM 5 on the assignment of debts, whether absolutely or by way of charge.[32] Stamp duty might already be payable on the transaction that gives rise to the debt, so that having the assignment of the debt stamped once more is a disincentive for economic activity. The philosophy behind the Stamp Duties Act probably does not extend far beyond revenue enhancement, and on balance it is difficult to see why it should impinge on transactions which are inherently non-speculative in nature.

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[32] See *supra*, n 4 and *supra*, n 30.

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