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# Put and call option Q&A: Singapore

**by Mark Cooper, Adrian Chan, Joel Teo and Enoch Ang, Hogan Lovells Lee & Lee**

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This Q&A provides country-specific commentary on *Standard document, Put and call option agreement: Cross-border* and forms part of *Cross-border private company acquisitions*.

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Country Q&A

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JURISDICTION

Singapore

## Put and call option

### 1. Are there any statutory provisions in your jurisdiction granting pre-emption rights to private company shareholders that would need to be waived before an option is granted or exercised?

There are no statutory pre-emption rights for existing shareholders under Singapore law. However, for listed companies, under the Singapore Exchange Securities Trading Limited (SGX-ST) listing manual (Listing Manual) the company's constitution must give pre-emption rights to existing shareholders (subject to any contrary direction by the shareholders in a general meeting or elsewhere in the Listing Manual).

### 2. Is a form of consideration required for the grant of a call or put option? Can this consideration be a nominal amount or the grant of a call option (with respect to a put) or the grant of a put option (with respect to a call)?

If the contract containing the call or put option is executed as an agreement (as opposed to a deed), consideration must be given for it to be enforceable. However, if the contract under which the call or put option is granted is executed as a deed, consideration is not necessary to ensure enforceability.

The consideration given does not need to be monetary; it can be the reciprocal grant of a call or put option, or some other right that has value to the receiver. It is not necessary for the "value" to be appraised or to be objectively sufficient; it need only be sufficiently valuable to the particular receiver to support the option being granted.

### 3. Is there any mandatory provision in your jurisdiction that limits the freedom of the parties to decide how dividends (or other distributions) related to shares subject to an option should be apportioned (for example, the seller's right to retain the benefit of the dividends until the option is exercised by the buyer)?

There is no mandatory provision that limits the freedom of the parties to decide how dividends (or other distributions) related to shares subject to an option should be apportioned. The parties to a contract can agree how to treat distributions related to shares subject to an option (if this complies with the rules under the relevant company's constitution and the prevailing laws on distributions).

### 4. If the consideration payable by the buyer on exercise of an option is shares to be issued by the buyer, what undertakings should the seller consider obtaining from the buyer (for example, the buyer has proper authority to issue the relevant shares and/or valid authority for the disapplication of any applicable pre-emption rights)?

In this scenario, the seller would be entitled to expect a standard set of fundamental warranties, including:

- The buyer is duly incorporated and validly existing under the laws of the jurisdiction of its incorporation.
- The buyer has the right, power and authority to enter into and perform its obligations under the option agreement and any related agreement.
- The buyer has taken all necessary corporate or other actions to authorise the execution, and performance by it, of its obligations under the option agreement.
- The option agreement and any related document constitute binding obligations on the buyer.
- The shares have been properly and validly issued.
- The shares are fully paid or credited as fully paid.
- The portion of the buyer's allotted and issued share capital that the shares comprise in percentage terms.

- The entry into and/or performance of the buyer's obligations under the option agreement will not violate the constitution of the buyer or any law applicable to the buyer.
- The buyer:
  - is the sole legal and beneficial owner of the shares;
  - has requisite power and authority to transfer the shares; and
  - has taken all necessary corporate or other actions to authorise the transfer of the shares including obtaining all necessary consents.
- There are no encumbrances over the shares and neither the buyer nor any other person so entitled has agreed to create any encumbrance over the shares. "Encumbrance" can be defined broadly (in favour of the seller in this context) or narrowly (in favour of the buyer in this context).

In addition, the seller should include undertakings on the buyer surrounding anti-dilution or similar measures, such that the seller receives the proportion of shares in the buyer it is expecting, to the extent relevant.

If the buyer is the sole or majority shareholder of the company, the seller can seek more protection by requesting warranties to be given in respect of the business and operations of the company itself.

## 5. If the consideration payable by the buyer on exercise of an option is cash, what are the most common calculation methods to determine the relevant amount (for example, "fair market value")? Is there any statutory provision that applies? Do the parties usually set out specific valuation procedures in put and call option agreements?

It is up to the parties to either agree the purchase price outright or to agree on a formula to calculate it at a particular date and to build this into the option agreement. There is no statutory provision that applies. The purchase price or valuation mechanism should be clearly set out in the option agreement, to avoid any dispute. Some common valuation methods include:

- Discounted cash flow model: this looks at the company's discounted future cash flows. This method can work where the company has predictable positive cash flows, but may be unsuitable for valuing companies with significant capital expenditure.
- A multiple of EBITDA (earnings before interest, tax, depreciation and amortisation) or a variant of this, for example, using the ratio of EBITDA to sales or net debt.

## 6. What are the warranties that the seller usually gives to the buyer in call and put option agreements?

The seller of the relevant shares would usually give the following warranties:

- The seller is duly incorporated and validly existing under the laws of the jurisdiction of its incorporation.
- The seller has the right, power and authority to enter into and perform its obligations under the option agreement and any related agreement.
- The seller has taken all necessary corporate or other actions to authorise the execution, and performance by it, of its obligations under the option agreement.
- The option agreement and any related document constitute binding obligations on the seller.
- The seller is the sole legal and beneficial owner of the shares.
- The shares have been properly and validly issued.
- The shares are fully paid or credited as fully paid.
- The portion of the seller's allotted and issued share capital that the shares comprise in percentage terms.
- The entry into and/or performance of the seller's obligations under the option agreement will not violate the constitution of the seller or any law applicable to the seller.
- The seller has requisite power and authority to transfer the shares and has taken all necessary corporate or other actions to authorise the transfer of the shares including obtaining all necessary consents.
- There are no encumbrances over the shares and neither the seller nor any other person so entitled has agreed to create any encumbrance over the shares. "Encumbrance" can be defined broadly (in favour of the buyer in this context) or narrowly (in favour of the seller in this context).

In addition, the seller should include undertakings on the buyer surrounding anti-dilution or analogous measures, such that the seller receives the proportion of shares in the buyer it is expecting, to the extent relevant.

If the seller is the sole or majority shareholder of the company, the buyer can seek more protection by requesting warranties to be given in respect of the business and operations of the company itself.

### 7. Is it common for the put and call option agreement to set out that any dispute regarding the consideration or the reorganisation of the company should be referred to an independent expert? How is the independent expert appointed? What is usually the independent expert's remit?

Where reorganisation provisions are included, they usually provide for an independent expert to be appointed. This expert is typically an independent firm of accountants, and first and second choices of such firms may be named in the option agreement. If no such experts are named or if the named experts are unable to act, then it may be stipulated that the parties are to agree on an expert within a certain period of time. If no agreement is reached, then either party may have the right to request an individual, typically the president of the Institute of Singapore Chartered Accountants, to select an appropriate accountant.

The remit of the accountant will typically be to act as an expert, not arbiter, and certify the price of the shares after the relevant reorganisation, taking into account the price originally agreed between the parties. The expert's certification of the revised share price is usually stated to be final and binding absent manifest error or fraud.

Separately, to the extent the consideration is not explicitly stated in the option agreement and is instead to be calculated based on a formula or specific bases of valuation, the option agreement may include provisions that refer any dispute concerning the calculation of the consideration to an independent expert. The expert's appointment and remit will be similar to that in a reorganisation scenario, as outlined above.

### 8. What are the anti-dilution mechanisms (if any) that are commonly set out in a put and call option agreement?

Anti-dilution mechanisms only apply where the buyer of the relevant shares intends to acquire a fixed percentage of a company's issued share capital. For example, if the buyer only wants to acquire a certain number (rather than a percentage) of the issued shares, then anti-dilution mechanisms are of less value.

Assuming the call option is for a fixed percentage of shares, the ability to force the seller of the shares to maintain its relevant percentage of the total issued shares, although dependent on the actions taken by the company, would include:

- An undertaking not to vote in favour of any dilutive equity issuances. This undertaking would be of more value where the seller holds a large majority of the shares and can therefore block relevant resolutions.
- An adjustment mechanism, such that should the percentage of the total issued shares represented by the option shares decrease, so would the consideration payable.

### 9. If the put and call option agreement does not specify the time within which the option(s) must be exercised, is there any mandatory provision that would set out a specific timeframe or will the option(s) need to be exercised within a reasonable time? In this case, is there any definition under applicable law or court interpretation of "reasonable time"?

There is no provision under Singapore law governing the time within which the option must be exercised or stating that the option must be exercised within a reasonable period of time. The parties are free to contractually agree the period for which the option is valid. From a commercial perspective, however, the parties may want to ensure that the exercise period is not unduly long.

### 10. Is it common for call and put option agreements to set out any acceleration event (for example, a provision allowing the call/put option to be exercised earlier in the event the company is subject to a third party offer)?

The parties are free to include an acceleration event in the option agreement. Whether or not one is included is transaction-specific and should reflect the particular circumstances and concerns of the parties. It may be appropriate to include acceleration events where, for example (including where the put/call options are included in a joint venture agreement):

- The company is subject to a third party offer in a sale scenario.
- The parties cannot agree on key aspects of the management of the business in a joint ownership scenario.
- There is a change in law resulting in it no longer being legally viable to continue the existing ownership structure of the company, where the put/call options are included in a shareholders' agreement.
- Material breach of a joint venture agreement by one of the parties.

In situations where the acceleration event is triggered by the default of one of the parties, the put/call option may provide for a different method of calculation of the price at which the shares are to be transferred, which would usually be at a discount to the market value of shares to be transferred.

### 11. How are the shares transferred once an option has been exercised (for example, is any registration of the new holder of the shares required)?

Up until the point of transfer, the shares are simply registered in the name of the seller. They are not marked in any way to indicate that they are subject to a put or call option.

The basic documents required for a share transfer are:

- Board resolutions of the company in which shares are being transferred approving the transfer, the updating of the register of members, the issue of a share certificate in the name of the buyer, and the share transfer form.
- Share transfer form.
- Existing share certificates to be cancelled and new ones to be issued (where these have been lost, alternative arrangements can be made, which usually include the giving of an indemnity and a statutory declaration by the registered holder).

On a transfer of shares, stamp duty is paid (usually by the buyer) at the rate of 0.2% of the higher of the net asset value of the shares transferred and the purchase price paid for the shares.

The following stamp duty forms should be completed by the company:

- Form E4A (Transfer of Shares).
- Working Sheet D (for transferring ordinary shares).
- Working Sheet E (for transferring preference shares).

These forms are issued by the Inland Revenue Authority of Singapore.

Where the company has been incorporated for more than 18 months, the values to be entered to these forms should be drawn from the company's net asset value as computed from its latest statement of accounts (ideally the audited accounts, if available), which should not be dated more than 24 months from the date of the share transfer. There is no need to obtain an independent or formal valuation of the company to work out the stamp duty payable. The statement of accounts should be certified by a director of the company or the company secretary. If the value attached to the seller's shares cannot be properly justified in a subsequent audit, there is a risk that the transfer may be unwound, so it is important to ensure that the value stated is justifiable.

Where the company has been incorporated for 18 months or less, the value of the shares transferred is the allotment price if the target company does not own any property. Where the target company owns any property, the management accounts must be prepared to determine the net asset value of the shares.

Once stamp duty has been paid, the company secretary can update the company's register of members, the authoritative version of which is maintained electronically by the Accounting and Corporate Regulatory Authority of Singapore. A share transfer can be effected in one working day.


### Contributor details

**Mark Cooper, Partner**
**Hogan Lovells Lee & Lee**
**E** *mark.cooper@hoganlovells.com*
**Areas of practice.** Corporate, including mergers and acquisitions, commercial, private equity.

**Adrian Chan, Partner**
**Hogan Lovells Lee & Lee**
**E** *adrian.chan@leenlee@com.sg*
**Areas of practice.** Corporate, including mergers and acquisitions, commercial, private equity.

**Joel Teo, Associate**
**Hogan Lovells Lee & Lee**
**E** *joelteo@leenlee.com.sg*
**Areas of practice.** Corporate, including mergers and acquisitions, commercial, private equity.

**Enoch Ang, Associate**
**Hogan Lovells Lee & Lee**
**E** *enoch.ang@hoganlovells.com*
**Areas of practice.** Corporate, including mergers and acquisitions, commercial, private equity.