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ASIA PACIFIC BUSINESS REGULATIONS

Doing Business in Asia Pacific

IBA Asia Pacific Regional Forum

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Acknowledgments

The Asia Pacific Regional Forum of the International Bar Association is proud to present *Doing Business in Asia Pacific*, which covers the main topics for 11 jurisdictions in the region.

We are thankful for the contributions from all participants, who made a tremendous effort not only to cover the legal aspects but also to work together in the best interest of our legal community.

We believe that this publication is an important tool for both investors and the legal profession when approaching certain critical aspects in our jurisdictions.

We also thank the International Bar Association for its continuing support of this initiative, and encourage all members of the Asia Pacific Regional Forum to contribute to future editions.

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Preface

We are proud to present the first edition of *Doing Business in Asia Pacific* for the Asia Pacific Region, which has been made possible due to the efforts of our colleagues in the Asia Pacific Regional Forum of the International Bar Association (IBA).

The Asia Pacific Region has become one of the most important market blocs in the world. Home to the two most populous countries in the world, China and India, more than 60 per cent of the global population lives in this region. The human capital of the Asia Pacific region has been a driver of the tremendous growth here in the last decade or more. At the same time, foreign investors doing business in this region encounter multiple challenges, due to cultural diversity and differences, lack of familiarity with local legal systems, the pace of development and implementation of local legislation or the dynamic geopolitical situation in the region. Lawyers play a key role in assisting investors to meet these challenges head on and continue their investment in this region.

Doing Business in Asia Pacific is one of the symbolic achievements in the longstanding activities of the Asia Pacific Regional Forum. The Asia Pacific Regional Forum is a very active forum within the IBA, and has provided a variety of opportunities for lawyers to establish a network of legal experts in and outside the region who practice in diverse areas of law, and to keep abreast of legal business developments in the region. This guidebook covers 11 jurisdictions in Asia Pacific, namely: Australia, China, Hong Kong SAR, India, Indonesia, Japan, Malaysia, the Philippines, Singapore, South Korea and Vietnam. Expert lawyers in each jurisdiction have contributed to each section of this handbook to explain not only the basics, but also present practical insights and up-to-date information for each topic in each jurisdiction. The wide-ranging topics covered include business environment, business and corporate structures, takeovers (friendly M&A), foreign investment, restructuring and insolvency, employment, industrial relations, and work health and safety, tax law, intellectual property, financing, privacy laws and data protection, competition law and dispute resolution. Some jurisdictions also cover additional topics that are unique to them.

We would like to thank all of the contributors in each jurisdiction for their tremendous efforts and support in completing this project, especially during the unprecedented challenges caused by novel coronavirus, or Covid-19, which continue at the time of writing this. We sincerely hope that this guidebook will be of great assistance to everybody doing business in this region, or to those who simply wish to deepen their legal understanding of this huge market, which, by all indications, is poised for even greater growth in the coming years. We hope to be able to update this guidebook periodically, covering more jurisdictions in the Asia Pacific Region in future editions. We would be grateful for any comments or suggestions from our readers to further improve this resource.

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Australia

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Chapter 1: Introduction

Clare Corke, Corrs Chambers Westgarth, Brisbane

Jeremy Horwood, Corrs Chambers Westgarth, Brisbane

Australia is a stable parliamentary democracy, offering international investors a cost-effective, low-risk and innovative business environment.

Now in its 28th year of consecutive annual economic growth, Australia's economy is underpinned by strong institutions, an exceptional services sector and the ability to respond to global changes. Australia offers significant opportunities for foreign investment in a range of growth sectors, including agribusiness, education, tourism, mining and wealth management. Investors regard Australia as an excellent place to invest because of its strategic location, population growth, highly skilled workforce, strong record of economic growth, and stable governance and regulatory environment.

Australia's economy is primarily services-based, complemented by a strong resources sector. Australia is a major global commodity producer of natural resources, such as coal, iron ore, uranium, gold and natural gas. The five biggest industries in Australia are financial and insurance services, mining, construction, manufacturing, and scientific and technical services. Other significant industries include education, agriculture, forestry and fishing.

Chapter 2: The business environment

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2.1 Government structure

The Commonwealth of Australia is a federation of six states (New South Wales (NSW), Victoria, Queensland, South Australia, Western Australia and Tasmania), two internal territories (Northern Territory and Australian Capital Territory) and a number of minor external territories.

A written constitution divides power between the central Federal Parliament, located in Canberra in the Australian Capital Territory, and the eight state and territory parliaments. The constitution gives the Federal Parliament the power to make laws relating to foreign investment, including legislation concerning corporations, taxation, trade and commerce, communications, banking, insurance, bankruptcy and insolvency, intellectual property, immigration and industrial disputes.

Each state has legislative power to make any laws it desires, except in relation to a few matters reserved to the Federal Parliament. Federal law prevails over state or territory law in the instance of any inconsistency.

Any foreign investment proposal must comply with both federal law and the law of the state or territory in which the investment is located. In some cases, local government law is also relevant, especially in relation to planning and building approvals.

2.2 Legal system

There are two primary sources of law in Australia: statute law and common law.

Statute law is the body of legislation enacted by the various levels of government, and includes subordinate legislation, such as regulations, rules and by-laws. Common law is the body of law arising out of decisions of the various federal, state and territory courts.

Each state and territory has its own court system, consisting of a Supreme Court and a number of minor courts. The Federal Government has its own court system, consisting of the High Court, Federal Court, Family Court and Federal Circuit Court. The High Court hears appeals (if leave is granted) in civil and criminal matters from the Federal Court, and the state and territory Supreme Courts. In addition, there are numerous panels and tribunals administering particular areas of law. The High Court also functions as Australia's superior constitutional court. Both the High Court and Federal Courts may hear matters requiring the interpretation of the Australian Constitution.

Australia is also a party to various international treaties and conventions. However, these do not create rights or obligations for individuals in Australia unless they are given effect by an Australian statute. International law may be used by an Australian court as an interpretative aid should the court find a statute ambiguous.

Chapter 3: Business and corporate structures

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3.1 Common forms of legal entities

The range of legal structures in Australia include:

- companies incorporated in Australia, including Australian subsidiaries of foreign companies;
- registered foreign companies;
- partnerships and limited partnerships;
- joint ventures;
- trusts;
- sole proprietors; and
- associations.

3.2 Incorporation process

3.2.1 Companies

The Corporations Act 2001 (Cth) (the 'Corporations Act') and the Corporations Regulation 2001 (Cth) are the primary sources of company regulation in Australia and are administered by the Australian Securities and Investments Commission (ASlC) in tandem with the powers granted to ASIC under the Australian Securities and Investments Commission Act 2001 (Cth).

The following sets out how business is conducted in Australia via a company structure, either incorporated in Australia or overseas. We also consider some of the alternative structures.

Companies incorporated in Australia

Companies have separate legal personalities under the law of Australia. Companies assume the rights and liabilities of their members and can also hold property. They can sue and be sued in their own name. Generally, the liability of the members is limited to the amount unpaid on their shares (if any) and any liability or obligation expressly provided for in the company's constitution or shareholders' agreement. This is in contrast to companies limited by guarantee and no liability companies, which are not as common in the Australian market as they mainly operate in the not-for-profit and mining sectors, respectively.

Actual management and control of a company is vested in the board of directors, who are usually appointed by the members but may also be appointed by the other directors of the company (subject to the company's constitution). Companies must, if they are carrying on a business or deriving income for the purposes of income tax legislation, appoint a public officer. The public officer is responsible for undertaking all activities required for income tax purposes. This person is liable for the same penalties that may be imposed on the company for any default, but is not personally liable for payment of the company's taxes. The Commissioner of Taxation may exempt a company from the requirement to appoint a public officer.

There are various types of companies, but by far the most common is a company limited by shares, being either a proprietary company (called a private company in many other countries) or a public company. A proprietary company must have at least one member, but may not have more than 50 non-employee members, whereas a public company has no limits on membership. Public companies may be listed on the Australian Securities Exchange (ASX), in which case they must also comply with the ASX Listing Rules.

Relative to public companies, proprietary companies are less stringently regulated and subject to less onerous reporting requirements. Areas in which this more relaxed regulatory approach is evident include the regulations and restrictions in relation to meetings; the appointment, qualification and removal of directors; the giving of financial benefits to directors and related parties; the power to allot shares; and the required content of annual reports.

A proprietary company is further classified under the Corporations Act as being either 'small' or 'large'. Generally, large proprietary companies have more onerous reporting obligations than small proprietary companies. As of 1 July 2019, a proprietary company will be 'large' for the purposes of the Corporations Act if (together with its controlled entities) it satisfies any two of the following criteria:

- the consolidated revenue of the company and any entities it controls for the financial year is AU$50m or more;
- the value of the consolidated gross assets of the company and any entities it controls at the end of the financial year is AU$25m or more; and
- the company and any entities it controls have 100 or more employees at the end of the financial year.

Large proprietary companies must prepare and lodge a financial report and director's report for each financial year. The accounts must be audited unless ASIC grants relief.

If the company does not meet at least two of the above criteria, it is considered 'small'. In some circumstances, small proprietary companies may also have to lodge financial reports.

A company limited by shares must have the word 'Limited' or 'Ltd' at the end of its name (to indicate the limited liability of the company's members), while a proprietary company limited by shares must also have the word 'Proprietary' or 'Pty' as the second last word in its name. In addition, all companies must state their Australian Company Number or Australian Business Number on all of their public documents.

Companies that are residents of Australia for taxation purposes will be taxed on income and gains from sources both in and outside of Australia, reduced by any allowable deductions. Conversely, companies that are non-residents of Australia will generally only be taxed on income with sources in Australia and gains arising from dealing with certain assets that have the 'necessary connection' with Australia.

Company groups are not regulated as groups and are treated as individual companies. However, some company groups may be treated as a single entity for income tax purposes.

Registered foreign companies

Companies that are incorporated outside of Australia that wish to carry on business in Australia must be registered with ASIC. Unincorporated bodies that do not have their head office or principal place of business in Australia must also register with ASIC if they wish to carry on doing business in Australia. A foreign company applying for registration must lodge an application accompanied by certain prescribed documentation, including a copy of its constitution or equivalent (if any) and a list of its directors, with ASIC.

A determination of whether or not a foreign company is 'carrying on business' in Australia requires an examination of all of the circumstances of the company's activities in Australia in light of several provisions of the Corporations Act as well as a body of common law principles. Specific advice should be sought in each case.

A registered foreign company is given the power to hold land in Australia under the Corporations Act. Under common law, a foreign company may sue and be sued in its own name; however, a failure to register under the Corporations Act as a foreign company, when required to do so, may inhibit that company's right to sue.

Some of the more important obligations imposed upon foreign companies registered to carry on business in Australia are set out below.

3.2.2 Partnerships

A partnership consists of two or more partners (to a maximum of 20, except in the case of certain professional partnerships) carrying on business in common with a view to profit. Partners may be individuals or companies. A partnership is not a separate legal entity from the partners themselves. Partners are jointly and severally liable for all liabilities of the partnership, and this liability is unlimited. Each state and territory has its own partnership legislation which, together with the terms of any partnership agreement and the principles of equity and common law, governs the relationship of the partners.

3.2.3 Limited partnerships

Legislation in all states provides for limited partnerships, which are partnerships consisting of at least one general partner and at least one limited partner. Limited partners contribute to the capital of the partnership and share in its profits but do not take part in its management. They cannot bind the firm and their liability to contribute to the debts or obligations of the partnership is limited to their capital contributions as recorded in the relevant register for each state or territory. The obligations of general partners are similar to those in an ordinary partnership and their liability remains unlimited.

Limited partnerships are formed upon registration as a limited partnership and they are generally taxed as if they are companies. Since 1 July 2002, certain classes of non-resident investors (eg, certain tax-exempt entities and taxable foreign residents of specified jurisdictions) investing in eligible venture capital investments through a limited partnership have been able to access the existing exemption for capital gains on venture capital investments.

3.2.4 Joint ventures

In Australian commercial circles, the term 'joint venture' is a label for a variety of forms of legal association between investors. Generally speaking, a joint venture is an agreement between two or more parties for the purposes of carrying on a business or undertaking. There is no settled statutory or common law definition of what constitutes a joint venture.

Three relatively common variations exist in Australia:

1. an incorporated joint venture, where a separate legal entity is incorporated to pursue the interests of the joint venturers, who are shareholders in the company, in a specific project; the taxation implications of this form of joint venture (assuming it to be resident in Australia for tax purposes) are the same as for an Australian company;

2. a unit trust, where the beneficial interest in the trust property is divided into units that can reflect the percentage of equity held by each participant and may be independently dealt with; unit trusts normally have a corporate trustee; and

3. an unincorporated joint venture, where the investors have a contractual association that lacks both corporate form and equity capital, and may or may not be a partnership for taxation purposes or under partnership legislation. If it is not a partnership at law or for taxation purposes, no partnership tax return is required and each joint venturer must lodge a separate tax return and may adopt a differing tax treatment for the income and expenses referable to its share of the joint venture.

Joint ventures are a common form of business association, especially in the energy and resources industries. For example, unincorporated mining joint ventures have been developed by the mining and petroleum industry in which several companies contract with one another to operate a mine or well but they each separately sell their share of the resources mined.

3.2.5 Trusts

A trust is a legal relationship whereby a trustee, being the legal owner of trust property, deals with that property for the benefit of some other person or persons (the beneficiaries) or for some object permitted by law, such as a charitable object. A trust is not a separate legal entity and does not enjoy limited liability, although it is common to use a company as the trustee and thereby limit the potential liability of the trustee.

A trustee owes a high standard of care to beneficiaries, and is subject to a number of duties. These include the duty to act in good faith, to avoid conflicts of interest, to make full disclosure to beneficiaries and not to make secret profit or gain.

Trusts commonly used to carry on businesses are unit trusts or discretionary trusts. In a unit trust, the beneficial interests in the trust are divided into units, which may be transferred in a similar fashion to shares in a company. The holder of a unit is entitled to a fixed share of the profit of the trust. In a discretionary trust, however, the identity or interest of the beneficiary is not determined at the time the trust is created.

Trust income is usually taxed in the hands of beneficiaries according to their respective share of the net trust income, and the trustee is not usually taxed on it. It should be noted, however, that:

- depending on the ownership and business activities of the trust or the business activities of entities controlled by the trust, a unit trust may be taxed as if it is a company;
- the trustee can be liable for tax in a variety of situations (eg, where there are non-resident beneficiaries); and
- tax losses are generally trapped within the trust and their future use is subject to satisfying certain complicated tests.

3.2.6 Associations

When a group of people agree to act together as an organisation, club or group, they form an association. An association can either be unincorporated or incorporated. Associations are regulated at a state and territory level, with each jurisdiction having slightly different legislation. The basic principles of unincorporated associations and incorporated associations are set out below.

Unincorporated associations

An unincorporated association is not recognised as a separate legal entity to the members associated with it. It is a group of people who agree to act together as an organisation and form an association. The group can remain informal and its members make their own rules on how the group is managed. The rules may also be referred to as a constitution. An unincorporated association is, however, an entity under tax law and treated as a company for income tax purposes.

Incorporated associations

An incorporated association is a legal entity separate from its individual members. Associations are incorporated under the state or territory legislation in which they operate. An incorporated association may operate outside the state and territory in which it is incorporated if the entity is registered as a registrable Australian body under the Corporations Act.

An incorporated association may continue operating regardless of changes to its membership. It also provides financial protection usually by limiting personal liability to outstanding membership and subscription fees, or to a guarantee.

3.3 Ongoing reporting and disclosure obligations

3.3.1 Companies

Financial reporting

All companies must keep appropriate and adequate financial records, but only some need to produce a financial report. Financial reports and directors' reports must be prepared for each financial year by all:

- disclosing entities incorporated or formed in Australia;
- public companies;
- large proprietary companies; and
- registered schemes.

Financial reports must comply with accounting standards and regulations set out in the Corporations Act; however, there are some exceptions for small proprietary companies and small companies limited by guarantee.

Continuous disclosure obligations

Continuous disclosure is the obligation imposed on companies under Chapter 6CA of the Corporations Act and, in the case of listed companies, by Chapter 3 of the ASX Listing Rules. The Corporations Act imposes strict continuous reporting obligations on disclosing entities. Disclosing entities carry continuous reporting obligations, which arise when certain material events occur in relation to the company's operational or financial position. The information that must be disclosed is that which is likely to affect the price or value of the entity's securities.

The nature and scope of these obligations depend on whether the entities are listed or unlisted disclosing entities. As a general rule, listed disclosing entities must disclose price-sensitive information 'immediately' once the entity becomes aware of it, whereas unlisted disclosing entities must disclose the information 'as soon as practicable'.

Registered foreign companies

Subject to certain exemptions, registered foreign companies must annually lodge with ASIC a copy of their balance sheet, profit and loss statement, and cashflow statement for the previous financial year, which must be prepared in accordance with the laws of the company's place of incorporation. These financial reports must be accompanied by any other documents that the company is required to prepare under the laws applicable in its place of incorporation.

ASIC may require registered foreign companies to provide further information if the accounts provided do not sufficiently disclose the company's financial position.

A small proprietary company controlled by a foreign company must prepare a financial report and directors' report only if it was controlled by a foreign company for all or part of the year and it was not consolidated for that period in the financial statements for that year lodged with ASIC by a registered foreign company.

3.3.2 Partnerships

Partnerships are not required to file any financial information concerning the partnership on any public register. Accordingly, partnerships and partners (except corporate partners) are able to keep their financial performance confidential. A partnership need not be audited, but partners are bound to render true accounts and full information regarding all things affecting the partnership to all other partners or their legal representatives.

3.4 Management structures

3.4.1 Company directors

Directors are elected to guide and monitor the management of a company. A public company must have at least three directors. At least two directors of a public company must ordinarily reside in Australia. A proprietary company must have at least one director. At least one director of a proprietary company must ordinarily reside in Australia.

Only an individual (ie, a natural person) who is at least 18 years of age may be appointed as a director. A person must give written consent to act as a director of a company before being appointed.

Directors are usually appointed by the members of the company in a general meeting or by the other directors. Directors leave office if they resign, retire, are removed in accordance with the Corporations Act or the company's constitution, or are disqualified from managing companies.

3.5 Director, officer and shareholder liability

3.5.1 Directors and officers

In performing their role, directors are subject to a range of duties and obligations under the Corporations Act, the common law and the company's constitution (if it has one).

The key duties of directors are to:

- act in good faith in the best interests of the company;
- exercise their powers for the purposes for which they were conferred;
- act with reasonable care and diligence;
- avoid conflicts of interest; and
- not improperly use company information or their position to gain an advantage for themselves or someone else or to cause detriment to the company.

Similar duties (except for the duty to avoid conflicts of interest) apply to all company officers, including secretaries.

A director may rely on certain information or advice given by certain people, provided the reliance was made in good faith and after making an independent assessment of the information or advice.

Unless the company's constitution provides otherwise, the directors may delegate any of their powers to others, and are in the first instance responsible for the exercise of the power by the delegate as if the power had been exercised by the director itself, unless the director satisfies a test of reasonableness, in which case the director will not be responsible for the delegate's exercise of power.

A director who breaches any of its duties is liable to civil penalties. If the breach is reckless or dishonest the director may also incur criminal penalties.

Liabilities of a trustee company

If a company that acts as trustee:

(1) incurs a liability that it cannot discharge; and

(ii) is not entitled to be indemnified by the trust against that liability due to the terms of the trust or because the company committed a breach of trust or acted outside the scope of the trust, the directors are jointly and severally liable to discharge the trustee company's liability (unless any particular director is held responsible).

3.5.2 Member liability

Members are not liable (in their capacity as members) for the company's debts. Their only financial obligation, subject to the company's constitution and shareholders' agreement (if any), is to pay the company any amount unpaid on their shares if called upon to do so. If the company is not a company limited by shares, in some circumstances, members may have to contribute to the costs of winding up the company (and any incidental costs).

Chapter 4: Takeovers (friendly M&A)

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4.1 Takeovers and schemes of arrangement

Takeovers in Australia are highly regulated and based on a broad prohibition against increasing a bidder's voting power in public entities above 20 per cent. The takeovers rules are outlined in the Corporations Act and specifically regulate acquisitions of substantial interests in companies or trusts listed on the ASX and unlisted Australian companies with more than 50 members.

4.1.1 The 20 per cent rule

The takeovers rules limit a person from acquiring a 'relevant interest' in voting shares of a regulated entity where a person's voting power increases from:

- 20 per cent or below to more than 20 per cent; or
- a starting point that is above 20 per cent and below 90 per cent.

Where the listed entity is not the subject of a takeover bid, disclosure is required within two business days of a party acquiring a five per cent interest and every increase or decrease of one per cent or more above this five per cent level. Disclosure must be made in a prescribed format that includes details of the number of shares and all parties with a relevant interest in the shares, including 'associates', and details of any 'relevant agreement' (formal or informal, in writing or oral, and whether or not it has legal or equitable force) through which the relevant interest arises.

The Takeovers Panel expects that where there is a control transaction and a bidder holds or acquires a long equity derivative position (eg, a holding in cash settled derivatives), it should be disclosed to the ASX unless it is under the notional five per cent level.

4.1.2 Off-market bids

There are a number of ways in which relevant interests in voting shares exceeding 20 per cent may be acquired, but an off-market bid is the most commonly used takeover method.

In an off-market bid, the bidder prepares an offer document or bidder's statement, which is sent to the target for two weeks and then to shareholders by mail (unless the target consents to early despatch). Shareholders have at least a month to consider the offer.

The target prepares a target's statement, which is also mailed to shareholders and includes the target directors' recommendation. If the directors do not recommend the bid, the bid is considered hostile. The offers are accepted by shareholders completing and returning acceptance forms prior to the offer expiry date.

Once a bidder decides to make an off-market bid, the bidder must serve a bidder's statement on ASIC and the target, and dispatch it to shareholders between 14 and 28 days later (in a friendly bid, early dispatch is often granted by the target).

Where an offer includes scrip (ie, consideration by way of an issue of shares), the bidder's statement must comply with the prospectus requirements of the Corporations Act, which requires inclusion of all the information that investors and their professional advisers would reasonably expect to enable them to make an informed assessment of the rights and liabilities of the securities being offered as well as the assets and liabilities, financial position and performance, profits, losses and prospects of the company issuing the securities. The position is somewhat more fluid when the issue of scrip is in a proprietary company; however, ASIC has released guidance to the effect that the prospectus requirements should nevertheless apply in these instances. Reduced disclosure rules may apply if the shares offered have been continuously quoted on ASX during the previous 12 months.

An off-market bid may be subject to a wide variety of 'defeating conditions' that prevent a binding contract from being formed if not satisfied or waived. Common conditions include:

- a minimum acceptance condition, often set at 90 per cent, allowing offers to be withdrawn unless the bidder can proceed to compulsory acquisition and outright control. The condition may be fixed at 50 per cent or less if the bidder is satisfied with less than complete control;
- regulatory considerations, including the Foreign Investment Review Board (FIRB), where the bidder is a foreign person, and the Australian Competition and Consumer Commission (ACCC), where there are competition (antitrust) concerns; and
- negative conditions relating to certain events not occurring during the bid period, such as the target altering its share capital, disposing of all or a substantial part of its business or assets, or an insolvency event.

4.1.3 Market bids

A market bid must be an unconditional cash offer for securities quoted on ASX and is carried out by purchasing the target's securities at market. Because of the unconditional nature of this bid (among other considerations), this is a far less common method of takeover than an off-market bid.

The major steps of a market bid are as follows:

- the bidder arranges a broker to make an announcement to stand in the market and purchase all shares offered at the offer price for a minimum of one month; the market bid commences 14 days later, although the bidder may start acquiring shares shortly after the announcement;
- the bidder gives its bidder's statement to the target, ASX and ASIC on the day of the announcement and to target shareholders within 14 days. Disclosure requirements are similar to an off-market bid; and
- to accept, each shareholder must arrange for the sale of its shares on the stock market. The sale is subject to the normal three-day trade settlement process.

4.1.4 Schemes of arrangement

Schemes are commonly used as an alternative to 'friendly' off-market takeovers, but are mainly used in complex, large-scale mergers that would be difficult to arrange through a takeover bid. The notice of scheme meeting sent to shareholders must be accompanied by a detailed explanatory memorandom. An independent expert's report advising whether the offer terms are fair and reasonable for shareholders may also be required. Unlike takeover bids, schemes require the involvement of the court.

Shareholders' meetings are convened by court order. After shareholders approve the scheme by the requisite majorities (75 per cent of the votes cast on the scheme resolution, and over 50 per cent of the shareholders present and voting at the scheme meeting), the court is asked to grant orders to implement the scheme. As part of the approval process, ASIC reviews the scheme documents and, if satisfied with them, gives a no objection statement to the court.

The flexible structure of a scheme of arrangement is a key advantage over the relatively prescriptive regime for takeover bids. It allows the bidder not only to pay any combination of cash or scrip as consideration for an acquisition (eg, having a maximum cash pool available), but also enables an acquisition simultaneous to incorporation of additional complexities, such as the transfer or demerger of specified assets or liabilities.

Chapter 5: Foreign investment

Stephanie Daveson, Clayton Utz, Brisbane

5.1 Foreign investment control/restriction

5.1.1 Background

In Australia, foreign investment is generally encouraged, but notification and approval is required for certain types of investments.

Foreign investment in Australia is regulated by a framework that includes:

- Foreign Acquisitions and Takeovers Act, 1975 (Cth);
- Foreign Acquisitions and Takeovers Regulation, 2015 (Cth) and;
- Federal Government's Foreign Investment Policy.

Foreign investors in certain industries may also be subject to requirements under the recently enacted Security of Critical Infrastructure Act, 2018 (Cth). The Australian Tax Office also keeps a record of all foreign persons who hold agricultural land and registrable water entitlements in accordance with the Register of Foreign Ownership of Water or Agricultural Land Act, 2015 (Cth).

FIRB examines foreign investment proposals and makes recommendations to the Australian Government on those proposals.[1] The Australian Government minister responsible for foreign investment decisions is the Australian Treasurer.

5.1.2 National interest considerations

The Treasurer (or its delegate) reviews foreign investment proposals against the 'national interest' on a case-by-case basis. The national interest is not defined and is given a flexible meaning having regard to all relevant circumstances, but the Treasurer will typically consider national security, impact on competition, Australian Government policies (including tax revenue and environmental objectives), impact on the Australian economy and community, and the character of the investor. Additional considerations apply to investments in the agriculture sector and those made by foreign governments and foreign government investors.

For significant decisions, the Treasurer consults broadly with its consult agencies, which include the Australian Government and its instrumentalities, state and territory governments and their instrumentalities, national security agencies and authorities with responsibilities relevant to the proposed action.

The Treasurer can block foreign investment proposals that are contrary to the national interest or apply conditions to the way these proposals are implemented to ensure that they are not contrary to the national interest.

5.1.3 Foreign persons

Australia's foreign investment legislation applies to investment proposals by foreign persons. A foreign person is defined to mean:

- an individual who is not ordinarily resident in Australia;
- a foreign government or foreign government investor;[2] or

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1 Further information about FIRB and Australia's foreign investment framework is available at FIRB's website https://firb.gov.au accessed 13 May 2020.

2 Foreign government investors include not only a foreign government but also any corporation, trustee of a trust or a limited partnership (the general partner of which is treated as a foreign person) in which a foreign government has a 20 per cent or more interest or in which two or more foreign governments have a 40 per cent or more interest in aggregate.

- any corporation, trustee of a trust or general partner of a limited partnership in which:
  - a foreigner (ie, an individual not ordinarily resident in Australia, a foreign corporation or a foreign government) has a 20 per cent or more interest; or
  - two or more foreigners have a 40 per cent or more interest in aggregate.

5.1.4 Notification of transactions to the Foreign Investment Review Board

Whether notification of an investment by a foreign person is required is determined by reference to the type of investor and the type of investment, the industry sector in which the investment will be made; and the value of the proposed investment.

The Treasurer must be notified of any proposed investment by a foreign person before that action can be taken. This is known as a 'Notifiable Action'. An offence may be committed and civil penalties may apply if notice is not given. An action is only notifiable if it meets certain threshold tests.

Certain other transactions, referred to as 'Significant Actions', do not require prior notification or approval from the Treasurer, but as the Treasurer holds the power to make a variety of orders in relation to a Significant Action, including prohibiting the transaction because it is contrary to Australia's national interest, it is common voluntarily to notify the Treasurer that a Significant Action is proposed.

Parties may enter into agreements relating to a Significant Action or a Notifiable Action prior to the Treasurer's decision; however, such agreements must be conditional upon the Treasurer granting the transaction.

Foreign investment applications involve submitting an online form and certain additional information via the FIRB Application Portal. Application fees are due to the Australian Government in respect of foreign investment notifications.

Civil and criminal penalties may be imposed on foreign persons for failing to give notice regarding an investment that is subject to Australia's foreign investment laws and for other breaches of these laws.

5.1.5 Monetary thresholds

In most cases, a foreign person need only notify the Treasurer of its investment if the investment meets certain monetary thresholds. The thresholds depend on the type of investor and the actions proposed by that investor. The FIRB website holds the most up-to-date information rergarding the thresholds, which are subject to change.[3]

5.1.6 Special industry sectors

Specific additional restrictions on foreign investment apply to the industry sectors of media, telecommunications, transport, defence and military-related industries and activities, encryption and

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3 See https://firb.gov.au/exemptions-thresholds/monetary-thresholds accessed 13 May 2020.

securities technologies and communications systems, and the extraction of uranium or plutonium, or the operation of nuclear facilities.

Where a transaction involves a foreign person acquiring an interest in agricultural land that will be used for a primary production business or residential development, the applicant is required to demonstrate that Australian investors had an opportunity to acquire the land in question. Advertising widely and providing equal opportunity for bids will generally suffice.

5.1.7 Exemption certificates

Exemption certificates may be applied for certain acquisitions in relation to Australian land, or in relation to acquisitions of interests in either, or both of, the assets of an Australian business and the securities in an Australian entity (including interests acquired through the business of underwriting).[4]

An exemption certificate is usually granted to foreign persons (although not usually individuals) with a high volume of acquisitions in relation to land, where the administrative burden of a number of applications outweighs the granting of the exemption certificate. A certificate will generally specify the maximum value of interests that can be acquired and also the period during which acquisitions can be made.

5.1.8 Timeframe for decisions

Under the Foreign Acquisitions and Takeovers Act, the Treasurer has 30 days to consider a formal notification and make a decision for both voluntary Significant Actions and compulsory ‘Notifiable Actions’. The 30-day period starts when the Australian Government receives the correct filing fee (the ‘Statutory Deadline’).[5]

In routine cases, a decision is usually made within 30 days of lodgement of a notification. In circumstances where notifications relate to sensitive sectors or involve investors with broader political or strategic objectives that may be contrary to Australia’s national interest, then the timeframe to obtain a decision is likely to exceed 30 days. In such circumstances FIRB will invite the applicant to request an extension to the Statutory Deadline. It is common practice that an applicant will voluntarily make such an extension request if FIRB indicates that it will not be able to meet the 30-day Statutory Deadline, as the alternative would be the imposition of an interim order, which is not desirable.

On 29 March 2020 the Treasurer of Australia announced that the timeframes had been extended with immediate effect to six months to accommodate the reduction in all thresholds to AU$0.00 as a consequence of the Covid-19 outbreak.

5.1.9 Conditions placed on foreign investment

Approval of the transaction may be subject to conditions imposed to satisfy the Treasurer that the transaction is not contrary to the national interest. Compliance with these conditions is compulsory.

4 Further details in relation to exemption certificates and other exemptions are available on the following FIRB webpages: https://firb.gov.au/investment/land-exemption-certificates, https://firb.gov.au/guidance-resources/guidance-notes/gn26 and https://firb.gov.au/exemptions-thresholds/exemptions accessed 13 May 2020.

5 The Treasurer may make an interim order if a proposal is complicated or further information is required, which extends the timeframe for the making of a decision by a maximum of 90 days. Once it does so, no further voluntary extensions are permitted.

Standard tax conditions are now routinely imposed for most transactions. Examples of the standard conditions include providing documents or information to the Australian Tax Office, and the payment of outstanding tax debts.

Conditions also apply to transactions involving vacant non-agricultural land, with approval generally conditional on the foreign investor commencing construction of a proposed development within five years of approval, and retaining the land until construction is complete.

5.2 Foreign exchange control

There are various anti-money laundering and counterterrorism financing reporting requirements associated with bringing physical currency into and out of Australia, as well as international electronic funds transfers. However, Australia does not have foreign exchange controls that restrict currency inflows or outflows

5.3 Applicable tax incentive or grant

The Australian Government offers a range of tax incentives to encourage investment in Australia. Some common incentives include:

- a research and development (R&D) tax incentive, which provides eligible entities with an aggregated turnover of less than AU$20m per annum a 43.5 per cent refundable tax offset for expenditure on eligible R&D activities. A 38.5 per cent non-refundable tax offset is available for all other eligible entities on eligible R&D activities;
- an early stage innovation company (ESIC) tax incentive, which provides eligible investors who purchase shares in an ESIC with a non-refundable carry forward tax offset equal to 20 per cent of the amount paid for their newly issued shares in the ESIC and a concessional capital gains tax (CGT) treatment for all interest in the Australian ESIC in certain circumstances; and
- a range of venture capital tax concessions.

In addition, the Federal Government has various grant programmes, and the state and territory governments also offer various incentives and grants to local and foreign companies.

Australia’s tax system is highly complex and continually evolving. It is important to stay updated on the latest tax policies as incentives and grant programmes are amended frequently.

Chapter 6: Restructuring and insolvency

Stephanie Daveson, Clayton Utz, Brisbane

6.1 The significance of insolvency in Australia

A company is considered insolvent in Australia if it is unable to pay all of its debts as and when they fall due. Solvency is assessed primarily on a cashflow basis, but the company's balance sheet may also be considered. Australian law seeks to protect creditors and third parties dealing with insolvent companies.

Directors and officers who trade a company while it is insolvent potentially expose themselves to civil and criminal liability under Australian law. Civil liability is more common and, if established, typically requires the directors to compensate the company (by then in liquidation) for the trading debts incurred during the period of insolvency. However, insolvent trading laws have recently been reformed to include a 'safe harbour' carve-out for directors from personal liability.

Under Australian law, insolvent companies may be subject to one of several forms of external administration, which aim to protect and maximise value for creditors. In all of these forms of external administration, the administrator appointed to the company or its assets will be an independent third party, typically a specialised insolvency accountant with official accreditation. The external administrator's remuneration, costs and expenses will usually be a first-ranking priority from the company's assets protected by a lien.

If a company is under external administration, that status will appear in company records maintained by ASIC. The Corporations Act also requires that the company include this status after its name in all communications.

6.2 Restructuring

Most modern international restructuring techniques used in the United Kingdom and the United States are available in a similar form under Australian law. Although there is no Australian equivalent of Chapter 11 of the US Bankruptcy Code, which involves the proposal and adoption of a plan of reorganisation, many of the benefits of that system can be achieved in Australia (including via creditor enforcement moratoriums and priority lending).

Restructuring can occur as part of, or separate to, external administration in Australia. Certain forms of external administration may be required to implement a restructuring plan. This will depend on the company's solvency and whether the company wishes to take advantage of statutory protections or rights available in certain forms of external administration to implement the restructure. Examples of protections or rights include a moratorium on creditor enforcement, a mechanism to extinguish creditor claims, and the suspension of the powers of directors in favour of an external administrator.

A company may also engage a chief restructuring officer or turnaround manager to assist with, manage or implement a restructuring plan. External legal and accounting advisers will typically be engaged to advise on the preparation and implementation of the restructuring plan.

6.3 Types of external administration

6.3.1 Receivership

A receivership is a form of external administration in which a receiver, or a receiver and manager (also referred to as a controller), is appointed by a secured creditor or the court to administer certain or all of a company's property.

The most common form of appointment is made by a secured creditor pursuant to a contractual right within a security instrument granted in its favour by the company. The court may also appoint a receiver where it considers it appropriate (typically where the security instrument does not contain a power to appoint a receiver), but this is not common.

The role of the receiver is to take possession of and sell the company's property subject to the security and to apply sale proceeds to the amount owed to the secured creditor. The receiver is required by law to take all reasonable care to sell the property for its market value or the best price obtainable in the circumstances.

The powers of a company's directors are limited during a receivership. A receiver has all the rights and powers to deal with the assets that are the subject of their appointment, to the exclusion of the directors.

A receivership ends when the appointing secured creditor is paid in full or all of the secured assets have been realised, or by order of the court.

6.3.2 Voluntary administration

Voluntary administration is a form of external administration in which a qualified insolvency accountant is appointed to take control of a company to investigate its financial affairs and report to creditors. The voluntary administrator has a statutory timeframe for investigations, reporting to creditors, as well as convening and holding meetings of creditors. The whole process typically takes 25–30 days unless extended by court order (which, in the case of complex corporate structures, is common).

To assist in this process, the administrator has all the powers of the company's directors (which are suspended during this period) and the benefit of a statutory moratorium preventing creditors or third parties taking action against the company or its property without the consent of the administrator or the leave of the court.

The administrator must ultimately recommend to, and have creditors vote on, the future direction of the company, namely whether the company should:

- be returned to its directors;
- enter into a deed of company arrangement (DOCA) (see below); or
- be placed in liquidation.

A secured creditor, with security over the whole (or substantially the whole) of a company's assets, may appoint a receiver or controller to the company's property within 13 business days of the appointment of a voluntary administrator (or otherwise with the consent of the administrator or by court order). The receiver's rights and powers in relation to that property will be superior to those of the voluntary administrator.

6.3.3 Deed of company arrangement

A DOCA is a form of external administration in which a deed administrator manages a contractual compromise between a company and its creditors. As noted above, a DOCA is one the potential outcomes of a voluntary administration.

A voluntary administrator will seek DOCA proposals prior to convening the second meeting of creditors in the administration, with the aim of tabling a proposal for creditors to vote on at that meeting. For a DOCA proposal to succeed, it usually needs to demonstrate to creditors that they will receive a greater return under the DOCA than they would in a liquidation scenario.

The typical objective of a DOCA is for the deed administrator to generate a monetary fund from the company's assets or through a contribution from a third party (often the directors or their associates) to be distributed to admitted creditors in full and final satisfaction of their claims (which will then be extinguished). The company would then be returned to its existing or new directors free from debt.

There is no standard form of DOCA. The Corporations Act provides significant flexibility for a DOCA to be tailored to suit most restructuring situations. These may involve selling or transferring assets, issuing shares, compromising debts and agreeing priority payments to creditors outside of the usual statutory order in a liquidation scenario.

6.3.4 Liquidation

Liquidation is a terminal process by which an appointed specialist insolvency accountant winds up a company's affairs, realises its assets, distributes the proceeds to admitted creditors in accordance with statutory priorities under the Corporations Act and ultimately deregisters the company. A company can be placed in liquidation in one of three ways:

1. by resolution of its members;
2. by resolution of its creditors; or
3. by order of the court.

Liquidation most commonly occurs where the company is insolvent. The liquidator will control the company during liquidation, and the powers of the directors and other office holders will cease.

In producing a fund for distributing to admitted creditors, a liquidator is also empowered to apply to the court to seek orders:

- requiring a director to compensate the company where that director has traded the company while it was insolvent; and

- to have certain company transactions declared void, such as unfair preferences, uncommercial transactions, unfair loans and unreasonable director-related transactions.

A liquidator will call for proofs of debt from potential creditors, and formally adjudicate each proof to determine whether each party is a creditor. The liquidator also determines if creditors should be afforded any priority for payment under the Corporations Act, and the total amount of each creditor's admitted debt. There will be no return to shareholders unless all claims of admitted creditors are satisfied in full.

A secured creditor may appoint a receiver or controller to all or some of a company's property during a liquidation. The receiver's rights and powers to that property will be superior to those of the liquidator.

6.4 Recent reforms in Australian insolvency law

6.4.1 Safe harbour

Often, directors prematurely appoint a voluntary administrator to viable companies due to the risk of personal liability for potential insolvent trading and the uncertainty associated with determining whether a company is insolvent. In 2017 the Corporations Act was amended to introduce safe harbour provisions to encourage directors to remain in control of the company and to take steps to restructure and turn the company around in circumstances where directors would otherwise appoint a voluntary administrator.

To take advantage of the safe harbour carve-out, a director must, at the time the debts are incurred, suspect that the company is or may become insolvent, and must be developing or implementing one or more courses of action that are reasonably likely to lead to a better outcome for the company than an immediate voluntary administration or liquidation. A director seeking safe harbour protection must also ensure that financial records are adequately maintained and payments for employee entitlements and tax liabilities are up to date.

6.4.2 Ipso facto

An *ipso facto* clause in a contract allows one party to terminate the contract or exercise other rights as a result of certain events, including the insolvency of the counterparty. Such a clause allows termination or other steps despite the counterparty otherwise not being in default and able to perform all obligations under the contract. These provisions are 'grandfathered' so that a party to a contract entered into after 1 July 2018 is prohibited from enforcing any rights in a contract that are enlivened due to a voluntary administrator or a managing controller being appointed or the company being subject to a scheme of arrangement (proposed to avoid an insolvent winding-up). If one of these appointments occurs, the *ipso facto* stay will also apply if a counterparty enforces a right for a reason that:

- relates to the financial position of the company;
- is prescribed by the regulations; or
- is in substance contrary to *ipso facto* provisions of the Corporations Act.

Amendments to the Corporation Regulations and Ministerial Regulations exclude a significant number of contracts and types of rights from the operation of the *ipso facto* stay. Excluded contracts include certain debt capital markets arrangements, government licences and permits.

6.4.3 Covid-19 temporary relief

On 25 March 2020, a new temporary safe harbour from liability for insolvent trading was introduced in the context of the Covid-19 outbreak for debts incurred by the company in the ordinary course of its business on or after 25 March 2020 and for a period of at least six months.

Chapter 7: Employment, industrial relations, and work health and safety

Stephanie Daveson, Clayton Utz, Brisbane

7.1 Employees' rights and protection

Australia's industrial relations system is regulated by the Fair Work Act, 2009 (Cth). Most employers in Australia are subject to its requirements. This is regardless of whether its employees are employed in accordance with an award set by an industrial body, a collective agreement or an individual employment contract. The Fair Work Act covers basic minimum conditions of employment and also specifies the right to claim against an employer for unfair dismissal.

Employers must also comply with legal requirements regarding taxation, superannuation, and work health and safety.

7.1.1 Basic minimum conditions

Qualifying employees are entitled to the minimum conditions of the National Employment Standards set out in the Fair Work Act.

These include:

- a maximum of 38 ordinary hours per week plus 'reasonable additional hours';
- four weeks of paid annual leave per year (while an employee classified as a shift worker is entitled to five weeks of paid annual leave per year);
- ten days of paid personal/carer's leave (including sick leave) per year, together with an additional two days of unpaid carer's leave and a further two days of paid compassionate leave;
- 52 weeks of unpaid parental leave for both parents at the time of birth or adoption of a child, with the option for one parent to request an additional 52 weeks;

- the ability to request flexible working arrangements as parents or carers of children under school age or under 18 with a disability; the employee must have at least 12 months' continuous service and the request may be refused on reasonable business grounds;
- long service leave based on relevant federal or state law;
- unpaid community service leave of a reasonable period for an employee engaged in an 'eligible community service activity', such as jury service or voluntary emergency management; and
- severance pay where termination of employment is for redundancy and the employee has at least 12 months' continuous service.

These rights and entitlements can be supplemented, but cannot be undercut, by a contract of employment, modern award or enterprise agreement.

Employers and employees can enter into negotiations for an enterprise agreement and can take protected industrial action in support of the bargaining claims. Industrial action taken other than in support of bargaining will not be protected under the law.

7.1.2 Unfair dismissal and the general protections

The Fair Work Act gives eligible employees the right to make a claim against their employer for unfair dismissal if a termination can be demonstrated to be harsh, unjust or unreasonable.

Small businesses that employ 15 or fewer employees and comply with a code for dismissals are also exempt from unfair dismissal laws. Moreover, an employee is not protected if they have:

- not served the 'minimum employment period' (12 months for a small business employer or six months otherwise);
- been engaged on a fixed-term contract or for a specified task;
- been engaged on a short-term, casual basis;
- been engaged as a trainee for a specified time period; or
- been engaged as a seasonal employee.

Employees are also not protected if their dismissal was due to a 'genuine redundancy' or if they earn more than the high-income threshold (which is AU$148,700 after 1 July 2019), unless they are covered by an award or enterprise agreement. This threshold is adjusted every year on 1 July.

The Fair Work Act also contains protections for persons against certain 'adverse action'. The 'general protections' protect a person from adverse action resulting from attributes such as race, religion, sexual preference, pregnancy or age, or because an employee sought to exercise their legal rights.

7.1.3 Work health and safety

Work health and safety is governed by legislation at the state level, which imposes obligations on all employers to ensure the safety of their employees while at work. Laws have largely been harmonised in most jurisdictions, apart from Victoria and Western Australia (although there are a number of state-based differences).

7.2 Statutory contributions and minimum wage

7.2.1 Minimum wages

Basic rates of pay, loadings, penalty rates and other entitlements are set by the national minimum wage and modern awards. Minimum wages, penalties and allowances can be supplemented by enterprise agreements and contracts of employment, but they cannot be undercut.

While there is a single national minimum wage, the actual minimum wage applicable to a particular employee will vary depending upon its industry and occupation, and whether one of the industrial instruments set out above applies.

7.2.2 Superannuation

Federal legislation requires employers to contribute a prescribed minimum level of superannuation for each employee. This is currently set at 9.5 per cent of an employee's ordinary time earnings, generally what the employee earns in normal working hours. This rate is set to rise incrementally each financial year, reaching 12 per cent by the 2025/2026 financial year. There are limited exceptions to this requirement.

Employers that provide less than that statutory minimum are liable to pay a non-deductible charge called the Superannuation Guarantee Charge. There are also limits on the maximum amount of superannuation contributions made for the benefit of an employee that an employer can claim as a tax deduction.

7.3 Work permits

There are a number of temporary and permanent visa options available for people who are considering working in Australia.

The permanent arrangements offer longer term options and include:

- employer-sponsored work visas, which gives the employee access to permanent residency; and
- skilled independent visas, which do not require sponsorship, but are governed by the particular occupation and a number of other requirements.

In all cases there are strict requirements regarding working visas that will need to be closely considered in an application. Obtaining specialist advice from a migration agent is recommended.

Chapter 8: Tax law

Stephanie Daveson, Clayton Utz, Brisbane

8.1 Taxes applicable to individuals

8.1.1 Income tax

Australian residents are taxed on their income and capital gains on a worldwide basis. Non-residents are generally only taxed on their Australian-sourced income, excluding dividends, royalties and interest, which are subject to withholding tax (WHT). Similar treatment applies to temporary residents.

8.1.2 Capital gains tax

Assets acquired after 20 September 1985 are subject to CGT on the occurence of certain events. Examples of such events include the disposal of CGT assets, as well as the ending (loss, destruction, cancellation, surrender, expiry, etc) of CGT assets. Capital gains are offset against any capital losses (current or prior year) and the net capital gain for the year is included in assessable income subject to any available CGT discount.

Capital gains (and losses) of foreign and temporary residents are only recognised for certain Australian assets, including real property, indirect interests in Australian real property, the business assets of an Australian permanent establishment and any options or rights to acquire such assets.

8.1.3 Dividends paid by a company

Under the imputation system of taxation, dividends that are paid to shareholders by an Australian resident company may be franked with an imputation credit that reflects the amount of corporate tax already paid on the company's profits. Individual shareholders who receive franked dividends are entitled to a tax offset equal to the franking credit that reduces or eliminates the tax payable by them on the dividend. Non-resident shareholders are unable to use these credits to offset any tax liability. WHT is imposed at a rate of 30 per cent on the gross amount of the unfranked dividend, but this may be less for double tax treaty countries.

8.2 Taxes applicable to businesses

8.2.1 Income tax

Companies are generally taxed on their income and capital gains at a rate of 30 per cent. A lower rate is available (currently, 27.5 per cent) for small businesses that meet certain requirements. Where a foreign enterprise has a permanent establishment in Australia and a double taxation agreement applies, the foreign enterprise is taxed in relation to the profits of its permanent establishment at the general corporate rate.

Australia's tax consolidation regime allows companies, partnerships and trusts that are 100 per cent Australian-owned to choose to be taxed as a single consolidated entity. Consolidation is available for groups that are wholly owned by foreign parents where there is no single Australian resident holding company (known as multiple entry consolidated groups). Where an election is made, all wholly owned entities must be included in the consolidated group and the head company becomes liable for all group tax liabilities.

8.2.2 Interest withholding tax

Interest withholding tax is imposed on interest paid by an Australian resident as an expense of an Australian business to a non-resident lender. It also applies to interest paid by a non-resident borrower where it is an expense of their Australian branch. A flat rate of ten per cent applies on the gross amount of the interest paid.

8.2.3 Goods and services tax

Goods and services tax (GST) is a broad-based consumption tax imposed at the standard rate of ten per cent on most supplies that are made for consideration and that have a relevant connection with the indirect tax zone (ITZ). It is similar to Value Added Tax (VAT) in other jurisdictions. Supplies include goods, services, information, rights and real property. Special rules extend the application of GST to digital products or other intangible supplies made by foreign suppliers to Australian consumers, as well as to the supply of low-value goods from offshore.

No GST is payable on GST-free supplies, including certain health, food and education supplies, exports and sales of businesses as going concerns. GST is not payable on input taxed supplies, such as those relating to financial services and the sale or leasing of existing residential property. Finally, an entity will make a taxable importation and be liable to pay GST where it imports goods into the ITZ for home consumption.

GST will only be payable on supplies where the entity making the 'taxable supply' is registered or required to be registered for GST purposes. Generally, this applies if the entity's annual turnover for the previous 12 months or projected annual turnover for the next 12 months in relation to supplies that are connected with the ITZ exceeds AU$75,000 (AU$150,000 for non-profit entities). GST liability on a taxable supply generally falls on the supplier. Exceptions include supplies that are reverse charged (including voluntary reverse charging) and supplies made by non-residents through resident agents.

In certain cases, a GST-registered entity that acquires a taxable supply may be entitled to an input tax credit for the GST included in the price of that acquisition. A GST-registered entity may also be entitled to claim an input tax credit where it makes a taxable importation.

8.2.4 Payroll tax

Payroll tax is a state or territory tax that is levied at specified rates by reference to wages and salaries (and other benefits) provided to employees that exceed prescribed threshold amounts in each state or territory. Top rates in each jurisdiction vary and currently range from 4.85 per cent to 6.85 per cent.

Broad rules apply to payments to contractors and the grouping of employers for aggregating wages and salaries.

8.2.5 Fringe benefits tax

Fringe benefits tax (FBT) is imposed on employers on the taxable amount of certain benefits, which is grossed-up under a formula to produce a level of tax that equates with the cash equivalent of the fringe benefit. The FBT rate is currently 47 per cent. Employers are generally entitled to income tax deductions for the cost of providing fringe benefits and FBT paid. The FBT year is from 1 April to 31 March of the following calendar year.

8.3 Other taxes

8.3.1 Taxation of trusts

Trust income normally forms part of the assessable income of the beneficiary to the extent that they have been made 'presently entitled' to such amounts. Where there is some amount to which a beneficiary is not so entitled, that income is taxed at a rate of 45 per cent. Although a trust income tax return is required, distributions of trust income are taxed in the hands of the respective beneficiary at their individual tax rate. The tax laws also have specialised taxing regimes in respect of specialised investment vehicles, such as Managed Investment Trusts and Attribution Managed Investment Trusts.

8.3.2 Taxation of partnerships

Partnerships are subject to pass-through taxation treatment (the shares of partnership profit or loss are taxed at the rate of each respective partner). Capital gains and losses relating to partnership interests and CGT assets of a partnership are made by the partners individually. Certain partnerships, such as the corporate limited partnership, are not subject to pass-through taxation and are instead taxed as companies.

8.3.3 Stamp duty

Stamp duty is charged in all Australian states and territories on the transfer of real property and other types of property. The rates vary by jurisdiction and are applied on a sliding scale to the greater of the consideration paid for the property and the value of the property. As of 1 January 2020, the maximum rate varies from 4.5 per cent to seven per cent, depending on the jurisdiction. Further duty (as of 1 January 2020, at a rate ranging from 0.5 per cent to eight per cent) applies to foreign purchasers of certain property in certain jurisdictions.

8.3.4 Land tax

Land tax is a tax levied annually in all states and territories (other than the Northern Territory) on the unimproved value of taxable property that is above the relevant land tax threshold. Rates (as of 1 January 2020, generally a top rate ranging from 1.1 per cent to 3.7 per cent) and thresholds vary in each jurisdiction. Surcharge land tax (as of 1 January 2020, ranging from 0.75 per cent to 4.25 per cent) can also be imposed on foreign owners of certain land in some jurisdictions. Exemptions and concessions may be available for certain types of land in certain jurisdictions (eg, primary production land).

8.3.5 Other specific taxes

Customs duty is payable at the time goods enter Australia and generally levied on the customs value of those goods as determined in accordance with Australian law.

Excise duty is imposed on certain goods (eg, alcohol, tobacco, fuel and petroleum products) that are produced or manufactured in Australia. If these products are imported into Australia rather than produced or manufactured in Australia, customs duty applies.

Chapter 9: Intellectual property

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9.1 Patents

A standard patent confers on the patentee the exclusive right to exploit commercially the patented invention for a term of 20 years. Australia's criteria of patentability for standard patents is closely aligned with international standards.

Alternatively, a patentee may apply for an innovation patent, which provides protection for eight years. An innovating patent is designed to protect inventions that do not meet the inventive threshold required for standard patents. Following an inquiry into intellectual property, the Australian Government has begun phasing out this type of patent. This means:

- the last day you can file a new innovation patent will be 25 August 2021; and
- existing innovation patents that were filed on or before 25 August 2021 will continue in force until their expiry. This will ensure current rights holders are not disadvantaged.

For both types of patents, the invention must be detailed in a specification (which may be provisional, later followed by a complete specification) describing the invention and concluding with claims that determine the ambit of the monopoly afforded by the patent.

The invention must be novel and amount to a manner of manufacture as that phrase is understood. The invention must also involve either an inventive step (for a standard patent) or an innovative step (for an innovation patent). The specification must be clear and unambiguous, and the claims fully supported by the information disclosed in the specification.

9.2 Trademarks

Australia protects reputation and goodwill in names through passing off law and consumer protection laws that prohibit misleading commercial conduct.

In addition, Australia has a registered trademark system for names, logos, devices, sounds, smells, colours and shapes that distinguish the goods or services of one owner from those of other owners. Registering a trademark provides the owner with the exclusive right to use and commercialise that mark in relation to specified classes of goods and services.

Trademark registration usually lasts for an initial term of ten years and can be renewed on an ongoing basis. If the owner of a registered trademark does not use its mark, it may be removed from the register for non-use.

Australia follows the international system of classification of goods and services. Early trademark registration is desirable for those seeking to enter the Australian market. Australia also has a federal system for registering business names for persons conducting business under a name other than their own name or company name.

9.3 Copyright

Copyright is the exclusive right to reproduce, publish, perform, communicate and adapt original literary (including computer programs), artistic, dramatic and musical works, together with other protected subject matter, such as films and sound recordings. Australia's copyright laws also provide for the protection of moral rights, which give authors the right of attribution, the right to prevent false attribution and the right to have copyrighted works treated with integrity.

Copyright arises automatically on the creation of a work and generally continues for 70 years after the death of the author. Australia is a member of the various international conventions on copyright and so affords reciprocal protection for copyright recognised in other member countries.

The Copyright Act, 1968 (Cth) has been through a number of reforms to address copyright issues arising in the 'internet age' and as a result:

- protects copyright owners from the unauthorised digitisation of their works and unauthorised communication of their works over the internet and other electronic means;
- limits the liability of internet service providers and software manufacturers for copyright infringement by users of their facilities and software; and
- prohibits the making, sale, distribution and use of circumvention devices for the purpose of circumventing a technological protection measure.

Prohibition of unauthorised imports is subject to significant exceptions. The Copyright Act permits the parallel importation of overseas published books and sound recordings, as well as, more recently, electronic literary and music items, and computer software.

9.4 Designs

The Designs Act, 2003 (Cth) provides for the registration and protection, for a period of up to ten years, of any design that is both 'new' and 'distinctive'. A design is the 'overall appearance of a product resulting from one or more visual features of a product', including shape, configuration, pattern and ornamentation.

Registration in Australia requires that the design be novel and not have been publicly used in Australia or published in a document anywhere in the world prior to applying for registration in Australia.

A person infringes a registered design if they deal in certain ways with a product that embodies the design or a substantially similar design. A defence applies for spare parts, allowing third parties to manufacture legitimate spare parts for complex products without infringing the registered design in the complex product.

9.5 Other

9.5.1 Domain names

Various classes of domain names ending in .au may be registered. Domain names ending in .com.au and .com are the most popular addresses for commercial entities operating in Australia. For a .com.au domain name, a substantial and close connection must exist between the commercial entity and that entity's domain name, which can be demonstrated by reference to the trademarks, 'nicknames' or acronyms of an entity, not just its company or business name.

Registration of a .com.au domain name does not create any proprietary rights in that name. Australian courts will, however, recognise rights in domain names where there is a reputation or goodwill in the name.

9.5.2 Trade secrets and confidential information

Both through contract and where information is imparted in confidential circumstances for a limited purpose, effective protection can be provided for technical know-how, customer lists and other confidential information against disclosure or use for an unauthorised purpose.

9.5.3 Plant breeder's rights

The plant breeder's rights scheme allows certain varieties of plant species to be registered, granting the breeder exclusive commercial rights with respect to that variety of plant.

Registration requires that the variety be distinct, and for propagations to be uniform and stable, and gives the breeder a series of exclusive rights, including producing, selling and exporting the plant material. Protection may last for up to 25 years depending on the plant species.

9.5.4 Circuit layouts

Circuit layouts are automatically conferred protection under the Circuit Layouts Act, 1989 (Cth), so there is no requirement to register the layout in order to be granted the exclusive right to copy, commercially exploit in Australia or make an integrated circuit of the layout. Circuit layouts may be protected for a term of up to 20 years.

Chapter 10: Financing

Alberto Colla, MinterEllison, Melbourne

10.1 Licensing requirements for banks

10.1.1 Background

The principal licensing obligations for banking in Australian arise under the Banking Act, 1959 (Cth), National Consumer Credit Protection Act, 2009 (Cth) (NCCP) and Corporations Act. A bank seeking to provide customers with the full ambit of banking services will have licensing requirements and associated obligations under each piece of legislation.

The obligations will vary depending on who is receiving the banking service (ie, retail or wholesale client) and what type of banking service is offered (eg, credit and home loans, deposit or investments products, payment products or products to manage risk, such as derivatives).

10.1.2 Banking business: authorised deposit-taking institution licence

An entity must be authorised as an authorised deposit-taking institution (ADI) by the Australian Prudential Regulation Authority (APRA) before it can carry out banking business in Australia. A 'banking business' includes the taking of money on deposit, the making of advances of money or any other financial activities prescribed under the Banking Act. It is an offence to conduct banking business without a proper authority.

Only corporations can obtain an ADI licence. APRA will not consider applications from partnerships, associations or other types of unincorporated entities. APRA expects that all applicants will be able to comply with the various prudential standards from the commencement of its banking operations. Applicants must satisfy the following: capital requirements, shareholding ownership rules, governance standards, adequate risk management and internal control systems, compliance mechanisms, information and accounting systems, and have external and internal audit arrangements.

Foreign Banks which are authorised to carry on a banking business in an overseas jurisdiction can apply to APRA to conduct a banking business through an Australian branch. Deposits in foreign ADIs do not receive the benefit of Australia's financial claims scheme and foreign ADIs are usually restricted to conditions relating to the opening of a deposit account (requiring a minimum balance) that in practice effectively restrict them to the wholesale market.

Foreign banks merely opening a representative office in Australia (not a full branch) are also regulated under the Banking Act and are required to obtain the written consent of APRA. Consent is required for foreign banks to use the word 'bank' or its equivalent as part of the bank's corporate name in connection with maintaining a representative office.

10.1.3 Australian financial services licence

Any entity intending to run a financial services business in Australia is required to hold an Australian financial services licence (AFSL) unless an exemption applies. Most Australian banks will hold an AFSL. Those who hold an AFSL are subject to regulation by ASIC.

Under the Corporations Act, financial services include providing advice in relation to financial products, dealing in a financial product, making a market for a financial product, operating a registered managed investment scheme, providing a custodial or depository service and providing traditional trustee company services.

Financial products broadly fall into three categories:

1. products through which a person makes an investment;
2. products through which a person manages a risk; and
3. non-cash payment products.

Banking services that are financial products include: derivatives, debentures, foreign exchange contracts and contracts of insurance (see further section 764A of the Corporations Act).

Importantly, consumer credit is not regulated under the Corporations Act.

An AFSL identifies whether the holder is authorised to provide services to retail and/or wholesale clients. There are additional protections applicable to retail clients (eg, provision of a Financial Services Guide) which do not apply to wholesale clients. Wholesale customers are customers like larger corporations, but can include high-net-worth individials (HNWIs) with an assumed level of business sophistication. The AFSL will also identify the particular products or services that the holder is authorised to provide. This may mean, for example, that when a financial institution engages in a new type of business, it must seek a variation to its licence to include new areas of business not previously covered by its AFSL.

10.1.4 Australian credit licence

Since 1 July 2010, a national licensing scheme has applied to entities that engage in credit activities (including the provision of leases) in relation to consumers under the NCCP. Most of the specific requirements are contained in the National Credit Code (schedule 1 to the Act) (NCC). ASIC is responsible for administering the NCCP.

Generally, the NCC applies to credit that is provided to a natural person or strata corporation and is wholly or predominantly for personal, household or domestic purposes, or residential property investment (see section 5 of the NCC for a full definition). Common examples of regulated products are home loans, credit cards and personal loans. Loans for business purposes are not regulated under the NCCP. Australian financiers who lend to consumers must hold an Australian credit licence and are subject to the responsible lending obligations under the NCCP. Responsible lending requires the licensee to make reasonable enquiries about the consumer's requirements and objectives, and to take reasonable steps to verify the consumer's financial situation to ensure that a loan is not unsuitable.

A bank engaged in consumer credit activities would need to hold both an AFSL and an Australian credit licence.

10.1.5 Compliance with the Anti-Money Laundering and Counter Terrorism Financing Act

The purpose of the Anti-Money Laundering and Counter Terrorism Financing Act (the 'AML/CTF' Act) regime is to identify and track money that is either the proceeds of criminal behaviour or that is to be used for the funding of terrorist activities. The current AML/CTF Act, 2006 (Cth) and the AML/CTF Rules Instrument, 2007 (No 1) (Cth) was passed by Parliament in 2006 and replaced the earlier regime, known as the Financial Transactions Reports Act, which dated back to 1988.

An organisation may be caught by the AML/CTF regime if it provides a 'designated service' that falls within one of three broad categories: financial services, bullion services or gambling services. Banking services, such as the provision of deposit accounts, loans and remittance services, are included in the definition of designated services. If an entity provides a 'designated service', then it will be considered a 'reporting entity' under the AML/CTF and will have to register with the Australian Transaction Reports and Analysis Centre. Reporting entities must have an AML/CTF Compliance Programme and, among other obligations, are expected to verify the identity of each customer (ie, Know Your Customer requirements), conduct ongoing monitoring obligations and observe mandatory reporting obligations (triggered by cash transactions above a specified threshold, and international funds transfer and suspicious matters).

10.1.6 Unfair contract terms for small business and consumer lending

The ASIC Act, 2001 (Cth) contains a number of basic protections for consumers and small businesses in relation to the provision of financial products and credit. These include protections from unfair contract terms in standard form contracts. ASIC is the relevant regulator for financial products and services offered to consumers and small businesses. Following the 2018 Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, there has been significant activity by ASIC in the banking sector to ensure that banks are not imposing unfair contract terms on their consumers and small businesses.

Chapter 11: Privacy laws and data protection

Alberto Colla, MinterEllison, Melbourne

The Privacy Act, 1988 (Cth) is the primary means of privacy protection in Australia. It applies to the handling of personal information and also has specific requirements for handling credit and tax file number information. Compliance with the Privacy Act is regulated by the Australian Information Commissioner (the 'Commissioner') and its office, the Office of the Australian Information Commissioner (OAIC).

Australian privacy laws are principles-based. The Privacy Act contains 13 Australian Privacy Principles (APPs) that set out how both private sector organisations and public sector agencies must collect, use, disclose and store personal information.

The APPs also give individuals certain information privacy rights, including:

- a right to access the personal information an entity holds about them;
- a right to correct that information; and
- a right to make a complaint and have it dealt with.

There are restrictions on using personal information for direct marketing purposes and other laws will apply if direct electronic marketing (eg, emails and texts) or telemarketing is being conducted. While personal information may be disclosed overseas, certain steps must first be taken and entities generally remain accountable for the handling of the information by the overseas recipient. Employers' handling of personal information about their current or former employees is exempt from the Privacy Act.

The Privacy Act gives the Commissioner functions and powers, including the power to receive and investigate privacy complaints, make determinations (including payment of compensation), conduct own motion investigations, seek enforceable undertakings from an entity and apply to the court for civil penalties.

The Privacy Act also includes a notifiable data breach scheme, which requires regulated entities to notify eligible data breaches (ie, where a person is likely to suffer serious harm from a privacy data breach) to the Commissioner and affected individuals. Entities must also assess suspected eligible data breaches.

11.1 Consumer data right

In 2019 the Australian Government began implementing new laws that create a data right for consumers (individuals and businesses) in Australia. The purpose of the right is to:

- give consumers greater control over access to, and direct sharing of, their consumer data; and
- increase competition in a sector by making it easier for consumers to compare product offerings.

The consumer data right regime currently applies to the banking sector and will be implemented on a sector-by-sector basis with the energy sector to follow.

Chapter 12: Competition law

Alberto Colla, MinterEllison, Melbourne

The Australian Competition and Consumer Act, 2010 (Cth) (CCA) (formerly known as the Trade Practices Act) regulates competition and consumer protection law in Australia.

The competition provisions of the CCA are based on antitrust legislation in the US and are not dissimilar to the antitrust provisions of the European Community's Treaty of Rome.

The CCA prohibits:

- cartels;
- resale price maintenance;
- anti-competitive concerted practices;
- misuse of market power;
- exclusive dealing;
- anti-competitive mergers; and
- a range of unfair business practices, including when dealing with consumers and small businesses.

It also imposes obligations on businesses designed to protect consumers, provides an access regime for essential facilities, and provides a specific access and competition regime for the telecommunications industry.

The ACCC is responsible for administering and enforcing the CCA. It has the power to authorise, on public benefit grounds, conduct that may otherwise breach the CCA.

There are significant consequences for contraventions of the CCA, including potential imprisonment, fines, compensation, corrective action and other orders.

12.1 Cartels and RPM

The CCA prohibits anti-competitive behaviour, such as agreements between competitors to:

- fix, maintain or control prices;
- split up a market or customers;
- restrict or limit supply, production, capacity or acquisition;
- rig bids; or
- impose a minimum resale price or induce resellers not to sell products below a specified price.

12.2 Concerted practices and other anti-competitive agreements

The CCA also prohibits 'concerted practices', which include coordination between corporations that may otherwise fall short of an agreement, arrangement or understanding that has the purpose, effect or likely effect of substantially lessening competition in a market.

The CCA also prohibits agreements, arrangements or understandings that have the purpose, effect or likely effect of substantially lessening competition in a market.

12.3 Misuse of market power

It is illegal for a corporation with a substantial degree of market power to engage in conduct that has the purpose, effect or likely effect of substantially lessening competition.

12.4 Exclusive dealing

Various forms of exclusive dealing (including restrictions on acquiring or supplying) are illegal if they have the purpose, effect or likely effect of substantially lessening competition in a market.

12.5 M&A

The CCA prohibits the acquisition of shares or assets of a company if the acquisition is likely to have the effect of substantially lessening competition in a market in Australia.

The acquisition of a foreign company by another foreign company may be subject to the CCA if, as a consequence, a controlling interest in a company in Australia is acquired.

The ACCC undertakes reviews of M&As that raise (or may raise) competition concerns.

Chapter 13: Dispute resolution

Alberto Colla, MinterEllison, Melbourne

13.1 Structure of the courts

Under Australia's Constitution and the doctrine of 'separation of powers', the judiciary is independent from the executive and legislative arms of government.

The High Court stands atop both the federal and state courts in Australia. It has jurisdiction over constitutional matters, international law cases and all final appeals from the lower courts.

The Federal Court of Australia has jurisdiction over civil matters arising under federal laws, as well as criminal cases involving federal crimes. There are federal courts located in all states and territories. Taxation, consumer law, bankruptcy, industrial relations and corporation law are examples of the types of matters heard in the federal jurisdiction. The Federal Circuit Court of Australia sits at the bottom of the federal court hierarchy, hearing less complex disputes involving federal laws.

The state court systems are similar across all states and territories. There is generally a superior court (the Supreme Court), an intermediate court (known as the District Court in NSW, and the County Court in Victoria) and a lower court (known as the Local Court in NSW, and the Magistrates' Court in Victoria). The majority of civil and criminal offences in Australia are state offences, and the state courts hear the vast majority of cases. Courts atop the state court hierarchy hear cases with large potential financial penalties and custodial sentences, while lower courts hear smaller civil matters, less serious indictable offences and summary offences.

13.2 Use of arbitration

International commercial arbitration in Australia is governed by the International Arbitration Act, 1974 (Cth), which is based on the United Nations Commission on International Trade Law (UNCITRAL) Model Law. This provides for various matters, including the staying of court proceedings capable of settlement by arbitration and the enforcement of awards under various arbitration conventions.

By the operation of this act, arbitration is very much in use in Australia. Courts are required to refer parties to arbitration when presented with an unresolved matter covered by an arbitration agreement, and arbitration agreements are often interpreted approvingly by the courts. Australian courts have also held that arbitration awards are consensual and private, therefore not subject to challenge on the basis of constitutional invalidity.

Domestic arbitration is also frequent and consistent across states and territories, with uniform legislation across each domestic jurisdiction.

13.3 Other forms of dispute resolution

Alternative dispute resolution (ADR) is extremely common in Australia. Courts are considered a last resort and parties are often required to engage in ADR mechanisms before they may proceed with litigation in court.

The most common ADR process is mediation. This typically involves a meeting between two parties in a disagreement, moderated by a third-party mediator. The mediator has no authority to impose a settlement, and the process is strictly voluntary. However, by identifying issues and assessing options, mediation is highly successful in helping parties reach a compromise and arrive at a settlement.

The ADR process is broader than mediation alone; it extends to expert appraisals, private judgments and online dispute resolution. ADR is cheaper and faster than litigation, involves flexible settlements, enables the private resolution of disputes and can leave both parties highly satisfied.

China

Chapter 1: Introduction

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1.1 General legal framework

The legal system of the People's Republic of China (PRC or China; for the purpose of this guidebook, referring only to mainland China) is a civil law system influenced by both German law as well as the former Soviet Union's legal system. The sources of law mainly include the Constitution of the PRC; national laws enacted by the National People's Congress (NPC) and its Standing Committee; administrative regulations promulgated by the State Council; and regulations and rules promulgated by the ministries and local legislative bodies. Legal practice in the PRC has distinctive regional patterns at the provincial level; major cities and special economic zones, as local legislative bodies, enjoy a certain degree of local legislative power.

Although China does not acknowledge binding case precedents, judicial practice still draws on the experience of common law in crafting decisions. The Supreme People's Court (SPC) began releasing 'guiding cases' in 2011 and, to date, the number has risen to over 100 cases. While not a formal source of law, 'guiding cases' are a form of judicial interpretation used to harmonise judicial standards and adjudication. To further decrease discrepancies resulting from similar cases, the SPC issued Implementing Measures for Establishing the Mechanism Resolving Law Application Differences on 11 October 2019, according to which all courts must apply to the SPC for resolutions if they find that any pending case may conflict with the SPC's effective judgments.

1.2 Recent legal developments

After 40 years of high-speed development since the last century's economic reform, China has entered into a period of high-quality development. To keep pace with social and economic changes, the PRC has continuously reformed its legal system. Since its accession to the World Trade Organization (WTO), China has built a comprehensive and complex legal system. By the end of 2011, the PRC had adopted its Constitution, enacted 236 laws, and promulgated about 690 administrative rules and 8,500 local regulations. Since 2012, the PRC has made great efforts to revise and harmonise its current laws.

The most ambitious achievement in the PRC's legislative history is the passing of its first Civil Code on 28 May 2020. The Civil Code is now the most extensive piece of legislation in the PRC and is the first to be named a 'code'. It consists of seven parts, including the general provisions, real rights, contracts, personality rights, marriage and family, inheritance, and tort liability. It will be effective from 1 January 2021 and will supersede any existing laws.

For international investors, the most direct and significant change is the Foreign Investment Law of the PRC, effective from 1 January 2020, superseding three foreign investment laws dating back to the original adoption in years from 1979 to 1988 and revised from time to time. The unification of the three laws into one will facilitate foreign investment into China.

As China is in the process of shifting from a world factory to an innovative power, it has been strengthening intellectual property protection to safeguard both foreign and domestic creators. The E-Commerce Law of the PRC, effective on 1 January 2019, prescribed obligations to e-commerce platforms to protect intellectual property, and the newly revised Trademark Law of the PRC came into force in late 2019. The revision of the Patent Law of the PRC is also ongoing.

In addition, the Standing Committee of the NPC adopted the revised Securities Law of the PRC, effective on 1 March 2020. Aimed at establishing a multi-tier capital market system with more stringent supervision and risk-control, the revised law promotes the registration system of securities issuance, increases penalties for violating rules and regulations, and enhances protection for investors.

This handbook briefly covers China's business environment, legal framework and business operations in the following chapters.

Chapter 2: Business environment

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Since the initiation of economic reforms in the late 1970s, China has experienced an economic growth averaging 9.4 per cent annually, which is far higher than the world's economic growth rate during the same period. China became the world's second-largest economy in 2010, accounting for about 16 per cent of the world economy, and is now a top trade and foreign direct investment (FDI) inflow country.

A comprehensive industrial system has been established. In recent years, China has been seeking economic growth pattern transformation from the traditional investment-driven industries to technology and innovation-driven and environmentally friendly industries. The government has promulgated relevant documents, such as the Guidance Catalogue of Industrial Structure Adjustment by the National Development and Reform Commission (NDRC) on 30 October 2019, and the Catalogue of Encouraged Industries for Foreign Investment by the NDRC and Ministry of Commerce of the PRC (MOFCOM) on 30 June 2019, to encourage investment in new industries. Meanwhile, market size and diversity across the country also offer diverse investment opportunities.

Laws and policies are constantly evolving to keep up with the rapid economic development of the past four decades, recording or guiding the changes and developments in the business field. China's centrally controlled political system has enabled the NPC and central government to promulgate legislation that is universally applied across the whole nation. On the other hand, the ministries and the local congresses and governments may issue industry or locality-specific legislative documents or policies with more guidance to bridge the gap and reduce ambiguity in laws. It is thus important for investors to keep track of changes in laws and their subordinate regulations and rules, and understand the practical differences in different localities.

The business environment has been continuously improving, especially in recent years. According to the *Global Business Environment Report 2020*, released by the World Bank, China's business environment in general has reached 77.9 per cent of the world's best level, ranking 31st in the world and climbing up 15 places compared with the previous year. According to this report, China is, for the second year in a row, among the top ten economies in the world with the most notable improvements in its business environment as a result of pushing forward the reform agenda. This chapter presents a snapshot of China's business environment by summarising the relevant indicators the World Bank uses to evaluate the ease of doing business in an economy.

2.1 Starting a business

China implements a unified negative list of market entry. In areas other than those listed on the negative list, entry is equally open to all kinds of market entities. For foreign investors, a negative list of foreign investment is also applicable and the principle of the national treatment for foreign-invested enterprises (FIEs) is adopted.

Except for a few businesses that should obtain a licence in advance as required by law, investors can go directly to register the business entity with the State Administration for Market Regulation (SAMR) or its local branches. The SAMR is now actively promoting the use of an online 'one-stop' application procedure, that is, completing all formalities required for starting a business via an online centralised platform, including obtaining the business licence, the company chops (seal/stamp) and taxation registration. According to the central government, the timeline for the SAMR to deal with formalities for starting a business should be shortened to within five working days as of the end of 2019. Many local governments have promised a shorter timeline, for instance, the local branches of the SAMR in Beijing and Shanghai have promised that all formalities will be completed within one day if the application materials are in order.

2.2 Enforcing contracts

Investors can enforce a contract via litigation at court or arbitration (if arbitration is chosen by the parties). China's courts adopt the two-instance trial system, and judgments and orders of the second instance court are final and enforceable in general, except that, under exceptional circumstances, the parties can apply for a retrial of the case. Summary procedure is also available for simple cases. The court's decisions are published online with limited exceptions of, for instance, divorces cases and cases involving state secrets. Arbitration is also an effective and well-recognised way to resolve disputes. Courts generally recognise and enforce effective arbitration awards, including foreign arbitration awards, because China is a party to the Convention on the Recognition and Enforcement of Foreign Arbitration Awards (the 'New York Convention').

2.3 Registering property

Land in China is owned by the state or, in rural areas, by collective organisations. A private party can obtain the land use right and the ownership of houses built on the land. The land use right and house ownership can and should be registered with the real estate administration authority so that the land use right and house ownership are formally established. In the same way, the mortgage on the land use right or house ownership should be registered. The registration is carried out using the centralised, electronic and computer-based registration system managed by the real estate administration authority of each city. The rights holder and interested party may access the information maintained in the registration system.

2.4 Obtaining credit

Commercial banks consist of large-scale state-owned banks, medium-sized joint-stock banks, small-scale urban commercial banks and rural credit cooperatives. All commercial entities have access to financing from a bank, subject to the bank's review of the borrower's credit. A commercial loan provided by a bank is mainly priced by reference to the loan prime rate (LPR). Generally, banks are willing to accept the borrower's real estate and movable property as collateral. Laws also permit the use of certain kinds of rights as collateral, such as shares or equity interests in companies, patents, copyrighted content, trademarks, accounts receivable, bonds, deposit certificates, warehouse receipts and bills of lading. Generally, the perfection of a mortgage and pledge is accomplished by registration with the relevant registration authorities in charge; and the perfection of a pledge over a tangible movable property is accomplished through the transfer of possession of the property by the pledgor to the pledgee. The secured party enjoys the priority of being repaid from the proceeds of the disposal of the collateral.

2.5 Obtaining electricity

Generally, obtaining electricity requires submitting a request for electricity demand, an application for a signing contract and power connection construction. In Shanghai, the local government has promised that the process of power supply for low-voltage projects will take ten days. In Guangzhou, for low-voltage non-residential users, it will take no more than three days to complete the process if the construction of external lines is not required, and no more than eight days if the construction of external lines is required.

2.6 Dealing with construction permits

China has established a comprehensive system covering the whole process from the granting of a land use right and issuance of a construction permit to the completion, acceptance and registration of real property. The government makes an effort to streamline the process and requires a reduction of the time required to within 120 working days, including by simplifying the requirements for low-risk construction projects, reducing the time to receive water and drainage connections, and promoting the integration of multiple verifications and joint acceptance. In Shanghai, the local government has implemented an online and offline 'one-stop centre' process for industrial projects with an area of less than 10,000 square metres in order to reduce the approval process to within 24 days.

2.7 Trading across borders

Enterprises may carry out independent cross-border trade (goods and technology) after filing with the commercial authority and registering with customs. The import and export of goods and technologies are subject to a list of prohibited or restricted goods and technologies issued by the state. Customs are piloting a 'two-step declaration' customs clearance model by which the enterprise may take delivery of goods after a summary declaration upon the consent of customs, and complete the entire declaration within a specified time.

The general trend for cross-border technology trade is that conditions for technical cooperation are primarily determined by the parties involved through consultation in accordance with the principle of fairness. Notably, some relevant regulations have been amended. For instance, the statutory provisions in relation to guarantee obligations by the transferor and entitlement to the improvement of intellectual property rights were removed from the Regulations on the Administration of Technology Import and Export (promulgated by the State Council on 10 December 2001 and last amended on 2 March 2019), which used to be a subject of consultation between the transferor (licensor) and transferee (licensee).

2.8 Protecting minority investors

For a limited liability company, laws provide for the protection of the rights and interests of minority shareholders in certain circumstances. For instance, the Company Law (promulgated by the Standing Committee of the NPC on 29 December 1993 and last amended on 26 October 2018) provides that if a company has been profitable for five consecutive years and meets the conditions for profit distribution but fails to make dividends for five consecutive years, the shareholder who votes against such a shareholders' resolution has the right to request that the company purchases its equity at a reasonable price. The Company Law also provides that the shareholder may launch litigation in the case of damage to the shareholder's interests caused by misbehaving directors or senior managers, or in the case of damage to the company's interests. In addition, protective provisions that are prevalent in international markets can also be commonly seen in China's investment cases, especially those with private equity funds, for example, veto rights, the supermajority voting requirement, pre-emptive rights, redemption rights, liquidation preferences, and tag-along and drag-along rights.

For a public company, laws and regulator's rules provide some additional protections to minority shareholders, such as cumulative voting; restrictions on the amount of and time for controlling shareholders to sell stock; and a more stringent approval procedure for the company to provide security for the shareholders or *de facto* controller of the company. Chinese companies have the option to list publicly in domestic and/or overseas stock markets. For those that are listed overseas, directly or indirectly, the interests of minority shareholders are protected by local applicable rules.

2.9 Improving the business environment

The Chinese government has made significant efforts to improve the business environment in recent years. To this end, in addition to the promulgation of the new Foreign Investment Law in 2019, a series of regulations have been issued. The State Council issued the Regulations on Optimizing the

Business Environment on 22 October 2019. Subsequently, the Ministry of Finance, SAMR, State Intellectual Property Office, Ministry of Natural Resources and other ministries/commissions have issued circulars on the implementation of the Regulations on Optimizing the Business Environment. Major cities, such as Beijing, Guangzhou, Shanghai and Shenzhen, have also issued local regulations on optimising the business environment. All of these have created a positive influence on the investment convenience for investors.

Chapter 3: Business and corporate structures

Liu Ning, JunHe, Shanghai

3.1 Structures for doing business in China and relevant laws

3.1.1 Structures for doing business

Companies and partnerships

Companies and partnerships are two major ways for foreign investors to structure a business in China. Companies are independent legal persons, whose liability shall be limited to the companies' assets. Partnerships do not operate as independent legal persons; investors or founders shall bear unlimited liability if the assets of partnerships are insufficient to pay off the debts. Most FIEs take the form of companies, and partnerships are more often seen and used in foreign investment in the venture capital and private equity fields.

Limited liability company and companies limited by shares

Companies in the PRC include limited liability companies and companies limited by shares. Compared with limited liability companies, there are stricter requirements for forming and operating companies limited by shares in terms of corporate governance, public disclosure and so on. Most foreign investors choose the form of limited liability companies for new investment. Businesses aiming at a public listing in a stock exchange in the PRC may consider choosing the form of a company limited by shares from the beginning, as it is the only acceptable form of organisation for a public listing in the PRC.

3.1.2 Legal requirements under relevant PRC law

The major law governing PRC companies is the PRC Company Law, which was initially promulgated by the Standing Committee of the NPC in 1993 and subsequently amended in 1999, 2004, 2005, 2013 and 2018.

General requirements for a limited liability company

Pursuant to the Company Law, a limited liability company (the most commonly used form by foreign investors) shall have less than 50 shareholders, and its registered capital shall be the amount of capital contribution subscribed by all shareholders registered with the company registration authority. Capital contributions may be in cash or in-kind (eg, intellectual property, land use rights and other non-cash properties that can be valued and transferred in accordance with the law). Except certain special industry and business as specifically required under relevant laws, there is no requirement for a minimum amount of capital contribution.

Unless otherwise provided in the articles of association, the shareholders are entitled to profit sharing in accordance with the ratio of their capital contribution. A shareholder proposing to transfer its equity interests to a non-shareholder shall obtain the consent of more than half of the other shareholders. The legal representative of the company who represents the company in civil activities shall be either the chairman of the board of directors/executive director or the general manager of the company. In addition, the legal representative shall be registered with the company registration authority, and all such information is available to the public in China through a public search.

Governance structure of a limited liability company

The governance structure of a limited liability company under the PRC Company Law consists of: (1) the shareholders' meeting; (2) the board of directors or executive director; (3) the board of supervisors or the supervisor(s); and (4) the managerial staff, including a general manager and other board-appointed officers, such as a deputy general manager and a chief financial officer.

The shareholders' meeting is the highest authority of the company. The group decides the most important matters of the company. The board of directors is the executive organ of the shareholders' meeting, which shall have three to 13 board members (in the case of smaller companies, the board of directors can be replaced with one executive director). The board of supervisors, which exercises supervisory functions over the company, shall have at least three members (in the case of smaller companies, the board of supervisors can be replaced with one or two supervisors). The general manager is responsible to the board of directors/executive director. The general manager exercises his/her rights and duties pursuant to the Company Law and the articles of association of the company.

One-person limited liability company

The limited liability company includes a special category called a one-person limited liability company. A one-person limited liability company only has one shareholder instead of a shareholders' meeting, and the shareholder can be either a natural person or a legal person. A natural person can only invest in one one-person liability company. If the shareholder of a one-person limited liability is unable to prove that the company's assets are independent of the shareholder's personal assets, the shareholder shall bear joint liability for the company's debt.

3.2 Statistics on newly established foreign investment enterprises

Pursuant to the official statistics of the National Bureau of Statistics of the PRC, from January 2019 to December 2019, the newly approved FIEs in China totalled 40,888 (enterprises in the area of banking, insurance and security not included), down by 32.5 per cent year-on-year. Actual use of foreign investment reached $138.1bn, up by 2.4 per cent year-on-year; among which 5,591 FIEs are invested in by investors from Belt and Road countries, up by 24.8 per cent year-on-year.

3.3 Free trade zones

Free trade zones (FTZs) in China are a specific class of special economic zones where goods can be landed, handled and re-exported without the intervention of customs authorities. China's opening-up policy has driven the establishment of FTZs in major cities and regions over the past several years. The first FTZ was launched in Shanghai in 2013 as a milestone in doing business in China. To date, FTZs have been launched in 18 cities/regions in China: Chongqing, Fujian, Guangdong, Guangxi, Hainan, Hebei, Henan, Heilongjiang, Hubei, Jiangsu, Liaoning, Shandong, Shanghai, Shanxi, Sichuan, Tianjin, Yunnan and Zhejiang.

The common goal of FTZs is to implement new models and innovative and preferential policies to improve the business environment, attract investment and offer geographical advantages for trade, administrative services, flow of capital, openness of transportation, taxation and so on. Each FTZ may have its own development priorities, for example, among the six new FTZs launched in August 2019, the Guangxi FTZ seeks to tap cooperation potential with Association of Southeast Asian Nations (ASEAN) members, build a land-sea corridor for international trade and develop border areas. The Shandong FTZ, launched at the same time, regards institutional reform as its priority. It aims to carry out reforms on 16 administrative service items and release more than 20 guidelines on optimising administrative services to be provided by the local government. With the Foreign Investment Law coming into force on 1 January 2020, FTZs in China are gearing up for the implementation of more institutional reforms and innovative measures. Foreign investors may consider investing in the FTZs, taking into account their locations, policies and advantages.

3.4 Legal risks and challenges

3.4.1 Requirement for licences or permits

Besides a business licence, if an FIE is engaged in a certain specific business sector, it may need to apply for specific licences or permits from the particular government authority that supervises that particular sector. Most of these licences and permits are the same as those of domestic enterprises. For example, an FIE that intends to engage in the sale of pharmaceuticals shall obtain an operating permit from the relevant drug administration bureau. If an FIE intends to engage in the value-added telecommunication business, it shall obtain an operating permit from the relevant industry and information technology bureau. The time for obtaining licences and permits may vary due to the different requirements of different government authorities.

In recent years China has gradually promoted decentralisation and the transformation of government functions. As a result of such reform, many licences or permits that were in the past obtained before registration with the market supervision authority for a business licence have either been cancelled or changed, so that they are obtained after the issuance of the business licence. The central and local governments publish a list of permits or licences that shall be obtained before registration for business licences; permits or licences not included in such a list can be obtained after the issuance of the business licence and before relevant business is carried out by FIEs.

3.4.2 Foreign Investment Law

The foreign investment regime in China is undergoing significant changes. Pursuant to the Foreign Investment Law of the PRC, the organisation form, structure and operating rules of FIEs are subject to the provisions of the Company Law, the Partnership Enterprise Law and other applicable laws. FIEs established in accordance with the three old foreign investment laws before the FIE came into effect may keep their original organisational forms for five years after 1 January 2020; that is, existing FIEs established in accordance with the three old foreign investment laws shall take action to change their organisation forms within five years and shall operate in accordance with PRC Company Law or other applicable laws from 1 January 2020.

3.4.3 Compliance with environmental laws

In recent years the PRC government has increasingly emphasised environment protection. This requires foreign investors to pay more attention to compliance with environmental laws, especially with respect to the establishment of manufacturing enterprises.

3.4.4 Labour costs

Labour costs in China continue to rise, especially in the form of wages and welfare across urban areas, which is another factor that needs to be taken into account by foreign investors.

Chapter 4: Takeovers (friendly M&A)

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4.1 Takeovers of non-listed companies

4.1.1 Regulatory framework for the acquisition of non-listed companies

There is various legislation governing M&A in China, which, to a certain extent, makes it challenging for foreign investors that do not have much experience in foreign investment in China via M&A.

Generally speaking, in terms of non-listed companies, both the target and acquiring companies are required to comply with, among other things, the primary laws and regulations, including the Company Law of the PRC and the new Foreign Investment Law of the PRC.

More specifically, foreign investors may also need to follow the detailed requirements contained in the Provisions on Merger and Acquisition of Domestic Enterprises by Foreign Investors (the 'M&A Rules'), which was first released by the State Administration for Industry and Commerce and nine other governmental authorities in 2006 and was last revised in 2009. The M&A Rules have been important rules for M&A in China by foreign investors for many years. The M&A Rules require, among other things, that: (1) the purchase price be determined based on the valuation of the target by a qualified Chinese appraisal firm; (2) domestic enterprises or individuals' acquisition of affiliated companies through controlled overseas companies be approved by the MOFCOM; and (3) an acquisition be filed with the MOFCOM if such an acquisition will cause a change of control over a domestic company owning any renowned trademark or China's time-honoured brands.

The promulgation of the Foreign Investment Law has aroused fierce discussions in the market over the validity of the M&A Rules, partly because certain provisions of the M&A Rules may conflict with the new Foreign Investment Law. That being said, as of the end of February 2020, the M&A Rules are still in effect, without being invalidated.

4.1.2 M&A statistics for non-listed companies

Based on the statistics sourced from MOFCOM, M&As in China by foreign investors became more and more active in 2015. Particularly, in 2015, 1,466 new FIEs were established in China by way of M&A, up 14.4 per cent year-on-year, with the actual use of foreign investment amounting to $17.77bn, up 137.1 per cent year-on-year. The share of M&A in the total amount of actual foreign investment increased from 6.3 per cent in 2014 to 14.1 per cent in 2015.

In addition, from January to November 2016, the actual use of foreign investment contributed by foreign investor's M&As maintained steady growth. In particular, 1,466 new FIEs were established in China through M&A, with the actual use of foreign investment amounting to RMB 123.5bn, up 15.6 per cent year-on-year, accounting for 4.5 per cent and 16.9 per cent of the total number of newly established FIEs and the total amount of actual use of foreign investment, respectively.

4.1.3 Typical methods of acquisitions for non-listed companies

Under PRC laws, typically, a foreign investor could take over a domestic company by either: (1) equity acquisition by which a foreign investor will purchase equities in the target from its original shareholder(s); or (2) asset acquisition, by which a foreign investor may set up a new FIE in China to purchase the target's assets, or purchase the target's assets first and then invest such assets in the establishment of a new FIE to operate such assets.

A typical M&A transaction involves, inter alia, target search and approach, negotiations with the target, valuation, deal structuring, due diligence, closing and post-acquisition integration. Taking equity acquisition as an example, the acquisition of a domestic company by a foreign investor typically and primarily involves, among other things, the following steps:

- reaching a term sheet with the target company and its shareholder(s) on the key commercial terms;
- conducting due diligence investigations (financial, legal, compliance, intellectual property, human resources, etc) into the target company;

- preparing and executing an equity purchase agreement, an investment agreement/ shareholders agreement, the amended and restated articles of association of the target company, and other transaction documents (if applicable);
- upon the satisfaction of all other conditions precedent, the target company applying to various governmental authorities for changing relevant registration/filing information so as to properly register/record the foreign investor as a shareholder of the target company; and
- the foreign investor paying transaction consideration, the payment timeline of which may be adjusted based on the deal structure.

4.1.4 Other considerations in the acquisition of a PRC non-listed company

China has a sophisticated regulatory regime for M&A by foreign investors. Apart from the primary legislation mentioned above (ie, the Company Law, the Foreign Investment Law and the M&A Rules), there are other considerations to consider regarding M&A transactions in China, such as those illustrated, but not limited to, the below.

Merger control review

Pursuant to the Anti-Monopoly Law of the PRC, if an M&A transaction constitutes the 'concentration of undertakings' as provided in the Anti-Monopoly Law, and if such concentration has reached the threshold of notification set forth by the State Council of China, then such an M&A transaction will be subject to a merger control review, and the parties to such concentration shall make an anti-monopoly notification to the competent anti-monopoly authority; otherwise, such concentration may not be implemented. Where the parties fail to seek the clearance of a merger control review, they may be penalised by the anti-monopoly authority, such as being ordered to cease the concentration and being fined.

National security review

China has established a security review system to conduct a security review of foreign investment that impacts or may impact national security. A national security review may come into play if foreign investors are trying to acquire:

- domestic enterprises that have a bearing on national defence security; or
- domestic enterprises that are engaged in key industries concerning national security (eg, important agricultural products, important energy and resources, and key technologies), and the acquisitions of which may enable the foreign investors to acquire an effective control over such enterprises.

If a proposed takeover is likely to fall into the scope of a national security review, the foreign investor may make the national security review notification on a voluntary basis. Failing to do so may expose the deal to uncertainty because the authority in charge has the power to initiate the national security review procedures at its discretion or based on complaints made by any third parties, without regard to whether the deal has been closed.

Special procedures for the acquisition of state-owned enterprises

Another factor that foreign investors should take into account is whether the target company is considered as a state-owned enterprise (SOE). Under PRC laws, the acquisition of a SOE is subject to special procedures, which may lengthen the time required for such an acquisition or cause uncertainty. These special procedures include but are not limited to:

- governmental approval: where the proposed acquisition upon closing would result in the state no longer having control of the target SOE, the parties shall seek prior approval from the competent People's government;
- asset appraisal: in general terms, the consideration for the acquired equities in a SOE should not be lower than the price appraised by a qualified Chinese appraisal firm; and
- acquisition through property right exchanges: PRC laws generally require that the sale of equities in a SOE should be conducted in public through a property right exchange, which is a quasi-government agency.

Data privacy and cybersecurity

Following the release of an array of new laws, regulations and rules in the field of data privacy and cybersecurity, data protection has become one of the primary considerations for M&A deals in the past few years. PRC laws have imposed various requirements on cross-border transfers of data, use and storage of consumers' personal information and so on. Hence, potential exposure in respect of data privacy and cybersecurity are important due diligence matters in M&A, especially when the M&A transactions take place in internet-based industries.

Compliance risk

For M&A transactions in China, increasing emphasis has been placed by multinational corporations and US companies on potential compliance risks, in part due to the increasingly stringent enforcement of the US Foreign Corrupt Practices Act. As certain long-established business practices in China may not be improved within a short period of time, the compliance risk in undertaking M&A transactions in China may remain high. Against this backdrop, foreign acquirers should consider special anti-bribery and anti-corruption due diligence for M&A in China.

4.2 Takeovers of listed companies

4.2.1 Regulatory framework for the acquisition of a listed company

In contrast to the global economic downturn, the A-share securities market's performance remains strong in China and has been increasingly attracting foreign investors from all over the world who are keenly interested in investing in Chinese listed companies. However, as China's capital market, in particular the A-share securities market, is not currently fully open, the acquisition of a listed company by a foreign investor is subject to requirements of special laws and regulations, in addition to legislation that is generally applicable to M&A in China. These include:

- regulations governing QFII/RQFII:
  - Administrative Measures for the Domestic Securities Investment by Qualified Foreign Institutional Investors (QFII), as jointly promulgated by the China Securities and Regulatory Commission (CSRC), the State Administration of Foreign Exchange (SAFE) and the People's Bank of China (PBOC) on 1 September 2006 ('Measures on QFII'); and
  - Measures for the Pilot Program of Securities Investment in China by RMB Qualified Foreign Institutional Investors (RQFII), as jointly promulgated by the CSRC, PBOC and SAFE on 1 March 2013 ('Measures on RQFII');
- legislation on securities regulation:
  - Measures for the Administration of the Takeover of Listed Companies, as promulgated by the CSRC on 23 October 2014, and its subsequent implementation rules ('Measures on Takeover of Listed Companies'); and
  - Administrative Measures on the Strategic Investment in Listed Companies by Foreign Investors, as revised and promulgated by MOFCOM, CSRC, SAFE and other ministries on 28 October 2015 ('Measures on Strategic Investment'); and
- a series of rules and measures in connection with Northbound Trading Link of Shanghai-Hong Kong Stock Connect and Shenzhen-Hong Kong Stock Connect as respectively promulgated by the CSRC, Shanghai Stock Exchange (SSE) and Shenzhen Stock Exchange (SZSE).

4.4.2 Typical acquisition methods for listed companies

Under the PRC legal regime, a foreign investor may elect either method as set out below to acquire the shares of a PRC listed company.

Apply to be licensed as a QFII/RQFII or trade A-shares through an existing QFII/RQFII

Any foreign investor that meets certain criteria as provided in the Measures on QFII (eg, financial capacity, qualified and experienced experts, and well-rounded internal control) can apply for a QFII licence and thereafter can use the RMB settled from foreign currency to invest in RMB financial instruments (including trading A-shares listed on SSE or SZSE) within the quota as approved by CSRC on a case-by-case basis. If a foreign investor does not apply for a QFII licence, as an alternative, it can entrust any existing QFII to invest in an A-share listed company.

Similarly, a foreign investor can also apply for an RQFII licence in accordance with Measures on RQFII, and such an RQFII can use RMB capital sourced from abroad to invest in A-share-listed companies within the quota as approved by SAFE.

Participating in the acquisition of a listed company as a strategic investor

The Measures on Strategic Investment stipulate that where a foreign investor meets several thresholds as outlined thereunder (eg, possession of overseas assets exceeding $100m or managing overseas assets worth more than $500m), it can acquire the shares of an A-share-listed company as a qualified strategic investor.

Under the current legal regime, and in typical practice, a qualified strategic investor may conduct a strategic investment in an A-share-listed company by:

- participating in the listed company's private placement;
- transferring shares of the listed company by agreement;
- making a tender offer; or
- making an indirect acquisition through other intermediary vehicles.

Making an investment in A-share-listed companies via the Northbound Trading Link of Shanghai-Hong Kong Stock Connect and Shenzhen-Hong Kong Stock Connect

Foreign investors may engage a Hong Kong broker and apply to the SSE or SZSE to transact shares of A-share-listed companies through a securities trading service company formed by the Stock Exchange of Hong Kong Limited in Shanghai or Shenzhen. Further, SSE and SZSE have adopted different standards on the A-shares available for trading to foreign investors.

4.2.3 Other considerations in the acquisition of a PRC-listed company by a foreign investor

Apart from the universal concerns arising out of a foreign investor's M&A transactions in China, which have been addressed in the foregoing (eg, market entry for foreign investors, merger control review and national security review), there are additional considerations for a foreign investor to weigh up in the acquisition of a PRC-listed company, including, among other things:

Exemption of tender offer

According to the Takeover of Listed Companies, if the acquirer elects to proceed with the acquisition at the point when the shares in which they are interested reach 30 per cent of the issued shares of the listed company, the acquirer shall issue a general or partial offer to the shareholders of the listed company in accordance with the law; otherwise, the acquirer shall apply to the CSRC for exemption from issuing a tender offer. In order to protect the legitimate rights and interests of all investors, only a few particular scenarios can give rise to the possibility for the acquirer to obtain such an exemption for a tender offer from CSRC, which shall be deliberately leveraged by the acquirer.

Horizontal competition and connected transactions

Pursuant to the Measures on Takeover of Listed Companies, in connection with the investment by a foreign investor in an A-share-listed company, such an investor shall specify in the disclosure documents (1) that it has prepared and announced whether there is horizontal competition or potential horizontal competition between the business of the investor, and any of its party acting in concert, controlling shareholder and actual controller, and (2) the business of the listed company, and whether there is an ongoing connected transaction. If there will be any horizontal competition or ongoing connected transaction, relevant arrangements shall be made to avoid horizontal competition between the investor and related parties in order to maintain the independence of the listed company.

Chapter 5: Foreign investment

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According to statistics published by MOFCOM, foreign investment in China has grown steadily in recent years. From 1979 to 2019, China received a total of $2.2874tn in foreign investment and 1,001,377 FIEs were established. Further, against a background of slowing global economic growth, sluggish cross-border investment and intensified competition, foreign investment in China in 2019 maintained steady growth of $138.14bn, an increase of 2.4 per cent over the same period in 2018. The industries with high growth rates of foreign investment are information transmission, software and information technology services, leasing and commercial services, pharmaceutical manufacturing, electrical machinery and equipment manufacturing, instrument and meter manufacturing, and scientific research and technology services.[1]

5.1 History of the foreign investment regime in China

5.1.1 Establishment of the foreign investment regime

China began to implement its policy of reform and opening up in 1978. Attracting foreign investment and learning from advanced foreign industries became China's national strategy. Consequently, the NPC enacted the Sino-Foreign Equity Joint Venture Enterprise Law of the PRC[2] (the 'EJV Law') in 1979 and the Implementing Regulations for the EJV Law[3] in 1983. In 1986, 1988, 1990 and 1995, the Wholly Foreign-Owned Enterprise Law of the PRC[4] (the 'WFOE Law'), the Sino-Foreign Cooperative Joint Venture Enterprise Law of the PRC[5] (the 'CJV Law'), the Implementing Rules for the WFOE Law,[6] and the Implementing Rules for the CJV Law[7] were also promulgated, respectively. The promulgation of these four laws and their implementing regulations (collectively the 'FIE Laws') marked the establishment of the foreign investment regime in China.

5.1.2 Reform of the foreign investment regime

In the decades that followed promulgation of the FIE Laws, with the change of China's domestic and international presence it became increasingly difficult for the FIE Laws to meet China's expanding reform and opening up needs. As stated in section 3.4.2, in 2019, the NPC passed the Foreign Investment Law to replace the FIE Laws, and made significant changes to the foreign investment regime. Subsequently, the State Council enacted the Implementing Regulations for the 'Foreign Investment Law'[8] ('Implementing Regulations'). The FIE Laws have fulfilled their purpose for nearly 40 years, but have been replaced and are no longer applicable.

5.2 Types of foreign investment

Under the new foreign investment regime, foreign investment in China is taking the following forms: (1) newly established FIEs: foreign investors establish FIEs solely or jointly with other investors; (2) M&A: foreign investors acquire shares, equity, property shares, or other similar rights or interests in domestic enterprises; (3) new projects: foreign investors invest in new projects solely or jointly with other investors; and (4) other forms of investment: foreign investors make other types of investment permitted by laws, administrative regulations or provisions of the State Council.[9]

5.3 Features of the Foreign Investment Law

The Foreign Investment Law and its Implementing Regulations comprise the fundamental laws and regulations for foreign investors doing business in China.[10] Foreign investment promotion, protection and administration are the key principles of the Foreign Investment Law and its Implementing Regulations.

5.3.1 Foreign investment promotion

The key principles for foreign investment legislation in China are to actively expand opening up, promote foreign investment and create a first-class international business environment. China's key policies to promote foreign investment include 'equal treatment to both foreign and domestic investors', 'improvements to the transparency of foreign investment policies' and 'preferential treatment to foreign investment in accordance with the law'.

Equal treatment to foreign and domestic investors

Under China's new foreign investment regime, government policies to support the development of enterprises apply equally to domestic enterprises and FIEs in accordance with the law. These policies include, but are not limited to, government funding arrangements, land supply, tax deductions, qualifications and licences, standard setting, project applications and human resource policies.[11] In particular, FIEs may participate in government procurement through fair competition in accordance with the law. Products produced and services provided by FIEs in China will be treated equally in the process of government procurement.[12]

Improvements to the transparency of foreign investment policies

One of the key purposes of China's foreign investment regime reform is to create an open, transparent, predictable and fair investment environment. For example, when formulating regulatory documents, competent authorities will solicit the opinions of FIEs to improve the predictability and transparency of foreign investment policies. When formulating standards, including national and industrial standards, FIEs have the right to participate equally in accordance with the law. The government and its departments shall formulate foreign investment guidelines and provide services to foreign investors and FIEs.[13]

Provinces and municipalities such as Beijing, Fujian, Guangdong, Guangxi, Guizhou, Jiangsu, Jiangxi, Shanghai, Tianjin and Yunnan have established comprehensive service entities and supporting websites to promote foreign investment. Taking the online platform 'Invest Shanghai'[14] as an

14 'Invest Shanghai' is the investment service platform of Shanghai.

example, the website displays Shanghai's investment environment, investment policies, industrial distribution and various available investment promotion services.

Preferential treatment to foreign investment in accordance with the law

To promote foreign investment and further opening up, in accordance with the needs of the national economy and social development, China encourages foreign investors to invest in specific industries, fields and regions, and offers preferential treatment according to applicable laws and regulations for doing so. The preferential treatment includes, but is not limited to, the following:

Establishment of specific regions (including 18 FTZs) with more vigorous opening up policies

Among the preferential opening up policies, for pilot policies implemented in certain special economic regions, once such pilot policies are deemed feasible, they may be promoted in other regions or nationwide.[15] For example, the value-added telecommunication service industry used to be a restrictive industry. Before 2014, foreign investors in the value-added telecommunication service industry could not hold more than 50 per cent of the shares. Since 2014, Shanghai FTZ has relaxed the restrictions on the shareholding of foreign investors in some value-added telecommunication services, including storage and transfer services, call centre services, domestic multi-party communication services and internet access services for internet users.[16] This relaxation of the shareholding requirement by foreign investors was extended to all pilot FTZs in 2018.[17] Later on in 2019, the shareholding restriction on the storage and transfer services, call centre services and domestic multi-party communication services were relaxed nationwide.[18]

Formulation of the Catalogue of Industries for Encouraging Foreign Investment

The Catalogue of Industries for Encouraging Foreign Investment (the 'Encouraging FI Catalogue') is one of China's most important mechanisms for promoting foreign investment. Foreign investment projects listed in the Encouraging FI Catalogue may enjoy preferential treatment in areas such as tax in accordance with laws, administrative regulations or the provisions of the State Council. For example, from 1 January 2011 to 31 December 2020, enterprises engaged in encouraged industries in Western China may enjoy a reduced enterprise income tax rate of 15 per cent.[19] Also, for foreign investment within the scope of the Encouraging FI Catalogue, the tariff exemption policy shall apply to the self-use equipment imported within the total investment amount.[20]

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15 See Art 13 of the Foreign Investment Law and Art 10 of the Implementing Regulations.

16 See Art 2 of the *Opinions on Further Opening up Value-Added Telecommunication Business to Foreign Investments in China (Shanghai) Pilot FTZ* promulgated by the Ministry of Industry and Information Technology and Shanghai Municipal Government on 6 January 2014 and effective from the same date.

17 See the *Special Administrative Measures for the Market Entry of Foreign Investment in Pilot FTZ (Negative List) (2018 Version)*, which was jointly released by the NDRC and MOFCOM on 30 June 2018 and became effective on 30 July 2018.

18 See the *Special Administrative Measures for the Market Entry of Foreign Investment (Negative List) (2019 Version)*, which was released by the NDRC and MOFCOM on 30 June 2019 and became effective on 30 July 2019.

19 See Preferential Enterprise Income Tax for Encouraged Industries in Western China promulgated by the State Tax Administration on 16 May 2018.

20 See Art 7 of the Notice on Further Deepening Reform and Properly Handling Foreign-invested Projects to Fight the Epidemic promulgated by NDRC on 9 March 2020.

5.3.2 *Foreign investment protection*

The legitimate rights and interests of foreign investors and FIEs in China will be protected through a series of measures, the most important of which are discussed below.

Arrangements to allow free transfer of technology

The Chinese government and its officials may not compel foreign investors and FIEs to transfer technology through administrative licensing, inspection, punishment or any other administrative actions[21] to eliminate any perceived improper influence of the government on commercial arrangements between Chinese and foreign parties. In addition, Chinese and foreign parties now enjoy more freedom to negotiate technology cooperation. For example, the Regulations of the PRC on the Administration over Technology Import and Export promulgated by the State Council on 8 January 2011 stipulate that a technology import agreement is prohibited from restricting the transferee from improving the technology provided by the transferor or using the improved technology and so on.[22] The Decision of the State Council on Revising Certain Pieces of Administrative Regulations (2019) issued by the State Council on 2 March 2019 removed such a prohibition.

Government requirements to fulfil its contractual obligations

To better protect foreign investors, local governments and their departments must fulfil policy commitments and perform the contracts concluded with foreign investors and FIEs pursuant to the laws. Local governments and their departments may not breach contracts on the ground of administrative division adjustment, change in government, organisation or job function, or replacement of responsible persons, among others. Policy commitments made by local governments and their departments are written commitments made pursuant to the statutory authority on the support policies, preferential treatment and convenience applicable to the investment of foreign investors and FIEs in the region.[23]

No expropriation except in special circumstances and fair compensation

The government may not expropriate a foreign investor's investment. Under special circumstances in which a foreign investor's investment is expropriated pursuant to law due to public interest needs, such an expropriation must be conducted according to statutory procedures. In addition, the foreign investor must be compensated in a timely, fair and reasonable manner.[24]

Protection of trade secrets

The government and its officials must keep confidential the trade secrets of foreign investors and FIEs that come to their knowledge during the performance of duties, and may not divulge or illegally provide such trade secrets to third parties.[25]

21 See Art 24 of the Implementing Regulations.

22 See Art 29 of the Regulations of the PRC on the Administration over Technology Import and Export.

23 See Art 25 of the Foreign Investment Law and the Art 27 of the Implementing Regulations.

24 See Art 20 of the Foreign Investment Law.

25 See Art 23 of the Foreign Investment Law.

Free repatriation of lawful income outside of China

Foreign investors may, according to applicable laws, freely remit their capital contributions, profits, capital gains, income from asset disposal, intellectual property royalties, lawfully acquired compensation, indemnity or liquidation income and other types of lawfully earned income into or outside of China, in RMB or any foreign currency. These policies are intended to alleviate some investors' concerns about foreign exchange controls and capital requirement regulations in China.[26]

5.3.3 Foreign investment administration

Depending on its form and features, the foreign investment, it may be subject to a series of administrative measures, including but not limited to: (1) the foreign investment negative list; (2) foreign investment information reporting; (3) national security review; (4) approval by or record-filing with the NDRC; (5) antitrust review; and (6) industry-specific approval requirements for certain industries. The foreign investment negative list, foreign investment information reporting and national security review are exanded upon below.

Foreign investment negative list

For the first time in 2013, China adopted a pilot negative list approach to foreign investment in the Shanghai FTZ. After the negative list was tested and adjusted in the Shanghai FTZ, the Special Administrative Measures for the Market Entry of Foreign Investment (Negative List) (2018 Version)[27] was released and implemented nationwide. The negative list includes prohibited and restricted industries. Foreign investors are not entitled to invest in any prohibited industry. For restricted industries, foreign investors must meet certain conditions prescribed in the negative list. For industries not listed in the negative list, foreign investors are treated equally to domestic investors and enjoy national treatment prior to and after the investment.

There are two negative lists now in effect: the Special Administrative Measures for the Market Entry of Foreign Investment (Negative List) (2019 Version) (the 'National Negative List') and the Special Administrative Measures for the Market Entry of Foreign Investment in Pilot FTZs (Negative List) (2019 Version)[28] (the 'FTZ Negative List'). The National Negative List applies to FIEs established nationwide (excluding FTZs). The FTZ Negative List applies to FIEs established in FTZs.

Compared with the National Negative List, the FTZ Negative List is less restrictive. There are fewer prohibited and restricted industries. The National Negative List includes 48 prohibited and restricted industries. The FTZ Negative List includes only 37 industries. For example, foreign investment in fishing for aquatic products in China's waters and inland waters is prohibited by the National Negative List, but it is not prohibited by the FTZ Negative List. The restrictions imposed on restricted industries are also more relaxed in the FTZ Negative List. For example, the National Negative List prohibits foreign investment in artistic performance groups. The FTZ Negative List only requires that the investment in artistic performance groups be controlled by the Chinese party.

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26 See Art 21 of the Foreign Investment Law.

27 The Special Administrative Measures for the Market Entry of Foreign Investment (Negative List) (2018 Version) was jointly released by the NDRC and MOFCOM on 28 June 2018 and became effective on 28 July 2018.

28 The FTZ Negative List was released by the NDRC and MOFCOM on 30 June 2019 and became effective on 30 July 2019.

Foreign investment information reporting system

The foreign investment information reporting system has been formally in place since 1 January 2020. Under the information reporting system, foreign investors or FIEs must submit investment information to MOFCOM or its provincial counterpart based on the principle of necessity. This replaced the previous approval or filing procedures with MOFCOM or its provincial counterpart.

According to the Measures for Foreign Investment Information Reporting,[29] foreign investors or FIEs must submit investment information to MOFCOM or its provincial counterpart by providing an initial report, change report, deregistration report or annual report, depending on the form of foreign investment. The investment information sought includes information about the enterprise information, the investors and their actual controllers, investment transactions, enterprise operations, and enterprise assets and liabilities. For enterprises subject to special administrative measures, the applicable industry licence must also be submitted.

National security review system

Foreign investment that affects or is likely to affect national security is subject to a national security review.[30] A national security review of foreign investment focuses on the security review related to M&A. Where a merger or acquisition causes or is likely to cause a significant impact on national security, the foreign investors may be required to terminate the transaction or take other effective measures to eliminate the influence of the transaction on national security.[31] For more details regarding the national security review system, please refer to section 4.1.4 b.

It is also worth noting that the rules on national security review of foreign investment in FTZs differ slightly from national rules. In FTZs, foreign investment in 'important culture' and 'important information technology products and services' is also subject to a national security review. In addition, the scope of a national security review in FTZs also includes foreign investment in the forms of new projects and a subscription of convertible bonds.[32]

5.4 Adjustments for existing foreign investment enterprises according to the Foreign Investment Law

Before the Foreign Investment Law was implemented, in terms of organisation form and corporate governance structure, the special provisions of the FIE Laws prevailed for FIEs. Only where the FIE Laws were silent did the Company Law[33] and other laws apply to FIEs. However, since the Foreign Investment Law no longer prescribes the organisation form and corporate governance structure of FIEs, as mentioned in section 3.4.2, FIEs established before the

29 The Measures for Foreign Investment Information Reporting was released by MOFCOM and SAMR on 30 December 2019 and became effective on 1 January 2020.

30 See Art 35 of the Foreign Investment Law.

31 See Art 4 of the Notice of the General Office of the State Council on Launching the Security Review System for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors (released by the General Office of the State Council on 3 February 2011 and effective on 3 March 2011).

32 See Art 1 of the Notice of the General Office of the State Council on Printing and Distributing the Trial Measures for the National Security Review of Foreign Investment in Pilot Free Trade Zones (released by the General Office of the State Council on 8 April 2015 and effective on 8 May 2015).

33 The Company Law of the PRC was revised by the Standing Committee of the NPC on 26 October 2018.

Foreign Investment Law was implemented must adjust their organisation forms and corporate governance structures to comply with the Company Law, the Partnership Enterprise Law of the PRC[34] and other applicable laws[35] within five years of the implementation of the Foreign Investment Law (the 'Transition Period').[36] After the Transition Period, the Administration for Market Regulation, the agency that administers company registrations formerly known as the Administration of Industry and Commerce or the AIC, will not process FIE registration matters and will make this public.

With respect to the organisation form, FIEs established as limited liability companies or partnerships are not required to register a change of organisation forms, and FIEs without a legal personality may apply to be restructured into partnerships during the Transition Period.[37]

With respect to the corporate governance structure, equity joint ventures (EJVs) must make corresponding adjustments, which may involve equity transfer rules and profit distribution rules, among others. To illustrate some of the adjustments required under the new foreign investment regime, the adjustments required for EJVs that were established before the Foreign Investment Law was implemented are discussed below.

5.4.1 Corporate governance structures

The now-abolished EJV Law provided different corporate governance rules than those contained in the Company Law. For example, under the EJV Law, EJVs did not have shareholders' meetings. The highest authority of an EJV was the board of directors. Under the Company Law, the highest authority of a limited liability company (including an EJV) is the shareholders' meeting. Therefore, EJVs established before the Foreign Investment Law was implemented must incorporate a procedure for holding shareholders' meetings, and shareholders' meetings must be the highest authority of the company. The corresponding rules of procedure and voting mechanisms must also be formulated.

5.4.2 Equity transfer rules

Further, under the EJV Law, to transfer equity interest in an EJV to a third party, the transferring party must obtain the consent of the other party to the EJV. Under the Company Law, which now applies to EJVs, unless otherwise agreed by the shareholders, a party must only obtain the consent of a shareholder holding more than 50 per cent of the voting rights to transfer its equity interest to a third party. If any other shareholder does not consent to the transfer but refuses to purchase the equity interest to be transferred, the objecting shareholder will be deemed to agree to the proposed transfer.

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34 The Partnership Enterprise Law of the PRC was revised and passed by the Standing Committee of the NPC on 27 August 2006 and implemented on 1 June 2007.

35 See Art 31 of the Foreign Investment Law.

36 See Art 42 of the Foreign Investment Law.

37 See the Notice of the State Administration of Market Regulation on Implementation of the Foreign Investment Law for Proper Handling of Foreign Investment Enterprise Registration (released by State Administration of Market Regulation on 28 December 2019).

5.4.3 Profit distribution

Finally, under the EJV Law, the parties to the EJV must share profits in proportion to their registered capital contributions. By contrast, under the Company Law, limited liability companies may distribute profits in the manner as agreed by all shareholders. Therefore, FIEs in the form of limited liability companies may adjust their profit distribution method based on their agreement.

5.5 Conclusion

The expansion of the opening up and promotion of foreign investment dominate China's current foreign investment legislation. The promulgation and implementation of foreign investment laws and regulations, such as the Foreign Investment Law and its Implementing Regulations, demonstrate China's desire to create a fair, convenient and open business environment. Under the Foreign Investment Law, foreign investors will be treated equally to domestic investors, and their investment will be better protected in China. Foreign investors will also have opportunities to invest in more industries and regions. With the further opening up of China, foreign investors should proactively assess the Foreign Investment Law's impact, and keep a close eye on the supporting legislation, regulations, local administrative approvals and even 'window guidance' of relevant bureaus in charge.

Chapter 6: Legislation and practice of China's bankruptcy regime

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6.1 Statutory framework of China's bankruptcy regime

China's bankruptcy system mainly consists of laws, relevant judicial interpretations and normative documents formulated by the courts.

6.1.1 The Bankruptcy Law

The Enterprise Bankruptcy Law of the PRC (the 'Bankruptcy Law'), issued by the Standing Committee of the NPC and effective as of 1 June 2007, is the main legislation that governs mainland China's bankruptcy regime. The Bankruptcy Law applies to all legal entities in China, including state-owned, private and foreign-invested companies in the form of limited liability companies or joint-stock limited companies. The Bankruptcy Law does not apply to individuals.

6.1.2 Judicial interpretations and normative documents of the courts

The judicial interpretations of the SPC on the Bankruptcy Law mainly include Provisions on Appointing Administrators for Hearing Enterprise Bankruptcy Cases and Provisions on Determining Administrators' Compensation for Hearing Enterprise Bankruptcy Cases effective in 2007, as well as Provisions (I), (II) and (III) on Several Issues Concerning Application of the Bankruptcy Law effective in 2011, 2013 and 2019, respectively.

Some local high courts and intermediate courts have also formulated guidelines applicable to their jurisdictions, such as Guidelines for Trials of Bankruptcy Cases (Trial) formulated by Shanghai High People's Court on 31 August 2018 and Guidelines for Trials of Reorganization Cases (Trial) by Shenzhen Intermediate People's Court on 25 March 2019. In addition, some normative documents of the SPC, such as Minutes of the National Court's Work Meeting on Bankruptcy Trials and Minutes of the Conference on Civil and Commercial Trials Heard by Courts in China issued in March 2018 and September 2019 respectively, also play an important role in guiding China's bankruptcy practice.

6.2 Bankruptcy procedures in China

Bankruptcy procedures in China include liquidation, reorganisation and settlement. Liquidation is a straightforward process of the disposal of debtor's property in a short space of time, and the debtor shall be deregistered after the procedure. Reorganisation and settlement may regenerate a company, but with a different emphasis and applying different situations.

6.2.1 Commencement of bankruptcy procedures

The statutory circumstances triggering bankruptcy procedures are: (1) the debtor is unable to pay debts due and its assets are insufficient to pay off debts; (2) there is clear lack of ability for the debtor to pay off debts; or (3) there is a possibility of the debtor losing its ability to pay off debts. Under the first or second circumstance, the debtor may initiate a proceeding of either liquidation, reorganisation or settlement, but under the third circumstance, the debtor may only apply for a reorganisation proceeding. Where a debtor is unable to repay debts due, the creditor may also apply for reorganisation or liquidation of the debtor.

If a company is found not to have sufficient assets to pay off debts during liquidation of a voluntary dissolution or is dissolved before the completion of liquidation, the liquidation committee shall apply to the court for bankruptcy liquidation.

6.2.2 Control of bankruptcy procedures

Bankruptcy procedures are judicial proceedings subject to the direction and supervision of the court. In a liquidation or settlement procedure, the administrator takes over the debtor, while in a reorganisation procedure, upon the application of the debtor and approval of the court, the debtor may manage its own assets and operate its business under the supervision of the administrator. The administrator is appointed by and reports to the court, and performs its duties in accordance with law under the supervision of the creditors' meeting and creditor committee. Creditors may exercise their rights via the creditors' meeting or creditor committee.

6.2.3 Special regimes for financial institutions

The bankruptcy of commercial banks, securities companies, insurance companies and other financial institutions has special features under the Bankruptcy Law. Where either of the statutory circumstances for bankruptcy occurs to a financial institution, the financial supervision and administration authority of the State Council may choose to apply the takeover and custody procedures or apply to the court for reorganisation or liquidation.

After the effectiveness of the Bankruptcy Law, with the government's focus on the comprehensive management of high-risk financial companies, some securities companies withdrew from the market through liquidation and several trust companies regenerated through reorganisation.

6.2.4 Cross-border bankruptcy: recognition and enforcement of foreign court judgments

The Bankruptcy Law has set forth the principle of cross-border bankruptcy by providing that: (1) the bankruptcy proceeding initiated pursuant to the Bankruptcy Law shall be binding on the debtor's property outside China; and (2) for the bankruptcy proceedings conducted in foreign courts involving debtor's property located within the territory of China, the Chinese court shall review the valid judgment or ruling of the foreign court and decide whether to recognise and enforce it in accordance with international treaties concluded or acceded to by China, or on the basis of the principle of reciprocity.

In practice, courts in some foreign countries and regions have already given recognition and assistance to the enforcement of judgments of bankruptcy cases made by China's courts. However, so far, there are very few cases where Chinese courts have recognised and enforced the judgments or rulings of bankruptcy cases made by foreign courts. Given the increasing presence of Chinese investment globally, cross-border bankruptcy has been a hot topic in academic and practical discussions in recent years.

6.3 Overview of bankruptcy practice

6.3.1 A growing number of bankruptcy cases

After the Bankruptcy Law came into force in 2007, the number of bankruptcy cases did not increase for several years. In fact, it retrogressed. However, since 2015 the number of cases accepted and concluded by the courts has risen rapidly, which might be linked to the cleaning up of 'zombie enterprises' and the policy of 'promoting structural reforms to build a modern economic system' by the Chinese government. A series of influential cases have emerged, of which the reorganisation case of Bohai Steel Group, involving a debt in total of RMB 280bn (approximately $40bn), is so far the largest bankruptcy case in China.

According to the public database including work reports of the SPC for the last ten years, the number of bankruptcy cases concluded by China's courts has increased rapidly from between 2,000–4,000 cases before 2015 to 16,000 cases by 2018.

6.3.2 *Establishment of bankruptcy tribunals and courts*

Guided by the SPC, since 2016 some local intermediate and high courts have successively set up bankruptcy tribunals to handle bankruptcy cases. The number of bankruptcy tribunals nationwide has increased from five in early 2016 to 73 by the end of 2016, and further to 97 by 2017. In January 2019 Shenzhen Intermediate People's Court took the lead in setting up the first special bankruptcy court in China, and since then more bankruptcy courts have been established in Beijing, Chongqing, Hangzhou, Guangzhou, Shanghai, Tianjin and Wenzhou. The establishment of bankruptcy tribunals and courts has helped to improve the international credibility and influence of China's bankruptcy trials.

6.3.3 *Construction of e-bankruptcy*

The SPC is also committed to disclosing information on bankruptcy cases through an e-bankruptcy channel. This means that the courts use the internet to facilitate bankruptcy procedures. In 2016 the SPC set up the National Enterprise Bankruptcy Information Disclosure Platform, whereby the trial process information on bankruptcy cases, including announcements, legal documents and debtor information, is published in a unified manner, and the creditors may convene creditors' meetings and voting through the Platform. In addition, the online auction of property is also widely adopted in bankruptcy procedures. When hearing the bankruptcy case of Jadeite Airlines, the Shenzhen Intermediate People's Court auctioned two aircraft engines through the online auction platform. Foreign companies from the US and Israel participated in the auction via the platform.

6.4 Development trends for bankruptcy practice

It is to be expected that the number of bankruptcy cases will continue to rise and that the bankruptcy regimes in China expand. The current Bankruptcy Law has been implemented for more than 12 years and has lagged behind growing bankruptcy practice in the country. In 2018 the Standing Committee of the NPC added a revision of the Bankruptcy Law into its legislative plan. Currently, the revision work is in progress and has not been completed. It is worth noting that the mechanism of bankruptcy for individuals is being explored and it may be formally legislated, either separately or by incorporation into the revised Bankruptcy Law.

Chapter 7: Employment law

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7.1 Major laws and regulations

China's modern employment regulatory regime was developed in the 1980s, reflecting historic changes to the employment market. Centred on contractual employment relationships, the regulatory regime is comprehensive, mature, complex and location-dependent. The NPC and its standing committee adopt employment legislation prescribing nationally basic principles and rules for employment issues. Administrative agencies under the central government promulgate detailed administrative regulations and departmental rules implementing employment legislation. To accommodate local conditions, legislative bodies and administrative agencies at local levels promulgate their own regulations and rules.

7.2 Key issues in employment law practice

7.2.1 Regional differences

There are regional differences in the execution and performance of employment contracts, settlement of work-related injuries, standard of social insurance payments and approaches to disputes. For example, minimum wage is higher in developed cities and provinces. A comparison chart of minimum wages for four developed cities and cities is below.

City/Province	Beijing	Shanghai	Jiangsu	Guangdong
2019 minimum wages (RMB)	2,200	2,480	1,620–2020	1,410–2,200

Regional differences are also reflected in the conditions for signing an open-ended term employment contract. In Beijing and most local jurisdictions, an employer must renew employment for the employee with an open-ended term contract when the second fixed-term contract expires. On the other hand, the employee may choose to end the employment relationship or enter into another fixed-term contract. While in Shanghai, the employer has the choice of renewal or termination of the employment relationship after the second fixed-term contract expires.

7.2.2 Dismissal and termination of employment contracts by employers

China has relatively strict protections against dismissal, which is conceptually different from termination. As set out in Articles 36 and 39–41 of the Labor Contract Law,[38] an employer cannot dismiss an employee without mutual consent or without statutory grounds for dismissal. Some of the statutory grounds provided by the Labor Contract Law are material breach of company rules and serious dereliction causing substantial loss to the employer. As for termination, according to Article 44 of the Labor Contract Law, termination only occurs upon expiration of the employment contract or satisfaction of termination conditions provided in the laws and regulations.

38 Labor Contract Law of the PRC, effective on 1 January 2008 and revised by the NPC Standing Committee on 28 December 2012.

7.2.3 Expatriate employees

Expatriates can fill posts in China with special requirements that have no available domestic candidates. Before obtaining work and residence permits, an expatriate employee must enter into an employment contract with the employer. Only the employer may submit applications for relevant permits for the expatriate employee.

Subject to compulsory Chinese laws and regulations, employers and expatriate employees may negotiate the terms of wages, working hours, rest and vacation, and health and safety protections. Employers, however, must pay social insurance for expatriate employees in China. In the case where an expatriate employee is a citizen of a country that has entered into a bilateral or multilateral treaty with China on social insurance, the provisions of the treaty prevail.

7.3 Recent trends

The procedure for employment dispute resolution in China includes negotiation, mediation, arbitration and litigation. Note that arbitration is a prerequisite for employment dispute litigation. In recent years, employers and employees have been increasingly willing to choose ADR methods. According to data published by the Ministry of Human Resources and Social Security, nationwide mediation organisations for employment disputes in 2019 mediated 1,070,000 cases, almost all of which were closed. The average rate for successful mediation in recent years is above 65 per cent.

Major claims in employment dispute cases revolve around remuneration, employment relationship recognition, work-related injury insurance and so on. Remuneration claims account for over 45 per cent of employment dispute cases. Many of these claims occur in more developed cities and provinces with larger populations of migrant workers (eg, Beijung, Guangdong, Jiangsu and Shanghai). Data suggests that more claims are pursued by employees working in developed regions.

7.4 Conclusion

As new technology – like the Internet Plus model, which integrates mobile internet, cloud networking, big data and the Internet of Things – develop and facilitate the emergence of new types of work under the sharing economy, future society and employment relationships will change. In the future, employment legislation will need to protect the rights of employees while adapting to changes in the marketplace. Employment law is expected to achieve a balance between the rights and obligations of employers and employees. We also expect the SPC and the Ministry of Human Resources and Social Security to work more closely to resolve regional differences in the field.

Chapter 8: Tax law

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8.1 Tax overview

Chinese tax law stems from five sources: legislation passed by the NPC (or its standing committee), regulations passed by the State Council, bilateral tax treaties agreed between China and other countries, circulars and announcements made by the State Administration of Taxation (SAT) and judicial interpretations issued by the SPC.

Legislation is passed by the NPC; it is then supplemented by regulations passed by the State Council, such as implementation regulations. The SAT and other state organs may then produce circulars and announcements regarding practice and procedure. These publications have the force of law. In 2019 over 160 such documents were produced. Most tax disputes are resolved through negotiations with the relevant tax authority or by using the relevant tax authority's own internal review mechanism. While a judicial remedy does exist for taxpayers who are dissatisfied with the SAT's decisions, tax litigation in Chinese courts is rare. As such, judicial guidance is sparse.

In addition to domestic sources of law, China also has a network of over 100 bilateral tax treaties governing taxation methods and, in some cases, the maximum rates to be applied to cross-border transactions. In cases of conflict between these sources, Chinese law is clear that relevant treaty provisions should prevail. This network is due to be amended by the provisions of the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting, but while China has signed the Multilateral Convention, it has yet to ratify it into domestic law.

8.1.1 Corporate income tax and other taxes affecting enterprises (non-exhaustive)

In the early 1990s China passed a series of laws wherein the worldwide profits of domestically resident enterprises were subject to corporate income tax (CIT) in China. The last major overhaul of CIT took place in 2008 with the passing of the Enterprise Income Tax Law. Since that date, both China-registered enterprises and overseas enterprises resident in China have been taxed equally on their worldwide corporate income and at a standard rate of 25 per cent (see 8.2 below for exceptions) with tax credits given for tax paid overseas. This is in striking contrast with the legislation in some other Asian countries, such as Hong Kong and Singapore, where foreign-sourced profits are not subject to tax. While the Chinese approach to taxation of worldwide income is unusual, its approach to taxation of domestically sourced income follows the international standard, as both foreign resident companies and Chinese resident companies are subject to tax.

The determinative factor in the assessment of whether an enterprise is subject to CIT on its worldwide income in China is whether the enterprise is regarded as resident in China. Resident enterprises are defined as those enterprises that are either incorporated in China and also those foreign-registered enterprises that have their place of effective management in China. The place of effective management is regarded as the place where the implementing substantive and comprehensive management and control over the production and business operations, staff, accounts and property and so on of an enterprise takes place. Consequently, an enterprise registered in a foreign jurisdiction may be regarded as resident in China if, for example, the directors are resident in China and key decisions relating to the management and control of the enterprise take place within China. In such cases, a foreign-registered enterprise will be required to adhere to all the relevant provisions of domestic Chinese tax law and pay tax on its worldwide income in China.

Capital gains tax

No separate CGT regime exists. Capital gains are instead rolled into the operating profits and taxed using normal CIT principles.

Dividends

A tax credit is available if the Chinese enterprise either holds directly or indirectly at least 20 per cent of shares in the underlying profit-making overseas enterprise, provided relevant criteria are met. The concept of indirect holding is limited to five tiers. Such dividends are regarded as corporate income. Domestic dividends are exempt from CIT.

Withholding tax

Outbound China-sourced income, such as dividends, interest, rental income, royalties and gains from the sale or transfer of shares in a China-resident enterprise, are subject to WHT at ten per cent. This figure may be lowered by a tax treaty. A temporary WHT deferral is available for dividends distributed to foreign investors that are reinvested into China, provided relevant criteria are met. In addition to WHT, VAT is also levied on some types of income.

8.1.2 Individual income tax

Chinese residents are subject to tax on their worldwide income. Non-residents are only taxed on their China-sourced income. An exemption on overseas income exists for non-domiciled Chinese residents who have not been present in China for more than 183 days for six consecutive tax years, commonly referred to as the ‘six-year rule’. If an individual is absent for more than 30 consecutive days in a calendar year, then the six year counter is reset to zero.

8.1.3 VAT

The Chinese VAT system for larger enterprises follows the international norm, with enterprises being able to offset their input and output VAT. In general, the VAT rate for most goods is currently 13 per cent and the VAT rate for most services is six per cent.

8.1.4 Other taxes (non-exhaustive)

LAND VALUE APPRECIATION TAX AND REAL ESTATE TAX

Land value appreciation tax is applied every time an individual or enterprise realises a gain from the sale of a land use right, building or premises and its associated structures. The gain is taxed on a four-band progressive rate from 30 per cent to 60 per cent. Real estate tax applies to land and buildings at either 1.2 per cent of the original value less a regional allowance or 12 per cent of the annual rental income.

CONSUMPTION TAX

Manufacturers or importers of certain types of consumable or luxury goods, such as alcoholic beverages, tobacco, cars and motorcycles, must pay consumption tax at rates ranging from one per cent to 56 per cent. Certain goods are taxed at a fixed amount based on quantity.

DEED TAX

The transferee or assignee of land use rights or real properties is subject to deed tax at a rate of between three per cent and five per cent, even where such a transfer is a gift or an exchange.

8.2 Preferential tax policies

Preferential tax policies are mostly aimed at technology enterprises or small enterprises. This is a non-exhaustive list:

- New/hi-tech enterprises may be eligible for a reduced CIT rate of 15 per cent, and key software enterprises or key integrated circuit design enterprises may be eligible for a reduced CIT rate of ten per cent. In both cases, the enterprise must be assessed and meet certain criteria. In addition, certain integrated circuit enterprises may also qualify for a tax free initial period of two or five years followed by CIT applied at 50 per cent of the normal rate for an additional three or five years, respectively.
- In the Shanghai FTZ, a number of preferential policies exist. Most notably, machinery and equipment imported by manufacturing enterprises and manufacturing service enterprises are tax exempt, although limited specific exceptions do exist. A number of preferential policies also exist in other FTZs and in parts of China, such as in Pingtan, Zinjiang and Zhuhai, but are due to expire in December 2020 unless formally extended.
- From 1 January 2019 to 31 December 2021, small and thin-profit enterprises with an annual taxable income of RMB 1m or less will be subject to a preferential CIT rate of five per cent. If such enterprises have a taxable income between RMB 1m and RMB 3m then, in addition to the above, income in excess of RMB 1m will be subject to a CIT rate of ten per cent.
- A super deduction of 75 per cent[39] for qualifying R&D expenditure incurred by qualifying high-tech and technology service enterprises applies until the end of 2020.

39 A super deduction of 75 per cent (ie, a deduction of 100 per cent of the value with an additional deduction of 75 per cent of the value, an aggregate deduction of 175 per cent)

8.3 Legal risks and challenges

Enterprises incorporated outside China should carefully assess where their key decision makers are situated and where key decisions are made. If the SAT determines that a foreign incorporated enterprise has its place of effective management in China, then that enterprise will be taxed in China on its worldwide income.

For several decades, tax authorities around the world have found that the established practice of creating specific or targeted tax rules has led to enterprises creating evermore complex and innovative tax schemes, creating systemic problems in global taxation, particularly regarding base erosion and profit shifting. In response, many countries have adopted a flexible General Anti-Avoidance Regulation or General Anti-Abuse Regulation (GAAR) to counter such schemes. Although CIT in China has long been subject to a GAAR, 2019 saw the introduction of a GAAR for IIT purposes. Enterprises and individuals should be aware that regardless of whether their transactions are lawful in form, should the SAT determine that the main purpose of the transaction was to reduce, exempt or defer tax payments, then the SAT may exercise its power to make adjustments to the tax payable. GAAR by its intended nature is flexible, thereby making its application hard to predict. As a consequence, enterprises should approach their tax planning activities in China with care.

Chapter 9: Intellectual property protection

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9.1 Primary features of intellectual property protection

In 2017 the NPC introduced legislation to strengthen the protection of intellectual property rights in China. According to Article 123 of the General Rules of the Civil Law of the PRC (promulgated on 15 March 2017), exclusive rights are granted to owners of the following types of intellectual property rights: works, patents (including invention, utility model and design), trademarks, geographical indications, trade secrets, IC layout designs, new plant varieties and other objects protected by law.

After thorough consideration of national conditions and legal standards, China adopted a ‘dual-track system’ of intellectual property rights protection, which consists of administrative protection and judicial protection, supplemented by arbitration and mediation.

Administrative protection provides an efficient, simple and inexpensive approach to intellectual property rights protection, by seeking the assistance of administrative authorities to address issues of infringement and counterfeiting. Judicial protection of intellectual property rights protection is provided by courts at all levels, whose function is to safeguard lawful intellectual property rights and interests through civil, administrative and criminal adjudication.

9.2 Improvements to intellectual property rights laws and regulations

China is continuously reviewing and updating its intellectual property laws. These updates include the Patent Law of the PRC (promulgated on 12 March 1984, last amended on 27 December 2008); the

Trademark Law of the PRC (promulgated on 23 August 1982, last amended on 23 April 2019); the Copyright Law of the PRC (promulgated on 7 September 1990, last amended on 26 February 2010); and the Anti-Unfair Competition Law of the PRC (promulgated on 2 September 1993, last amended on 23 April 2019. All of these updates were promulgated by the Standing Committee of the NPC.

China is accelerating the development of a punitive damages scheme under its intellectual property rights laws and regulations. For example, the Trademark Law now prohibits malicious applications to register trademarks and trademark hoarding. The Anti-Unfair Competition Law strengthens protections available to trade secrets owners. A draft amendment to the Patent Law that increases the penalties for patent infringement is being reviewed by the Standing Committee of the NPC.

9.3 Administrative protection of intellectual property rights

9.3.1 Intellectual property rights applications and authorisations

In recent years the number of intellectual property rights applications and authorisations in China has grown rapidly. In 2019 over 1.4 million new applications to register invention patents were accepted, and over 450,000 patents were granted. In the same year, over 7.8 million applications to register trademarks were accepted, and 6.4 million trademarks were registered.

To process such a significant volume of applications, the application review time has been shortened substantially, which indicates that the authorisation process has become more efficient and convenient.

9.3.2 Administrative protection of intellectual property rights

To fulfil China's commitment to strengthening the administrative protection of intellectual property rights, the National Intellectual Property Administration (NIPA) has enhanced intellectual property rights protection in e-commerce by actively investigating and penalising e-commerce patent infringement and counterfeit goods. Similarly, the National Copyright Administration, along with three other government agencies, has led a special task force, which focuses on the infringement of copyright of online short videos, and has enhanced efforts to combat copyright infringement and piracy. The General Administration of Customs has also strengthened intellectual property rights protection at China's customs borders, and restricted the import and export of counterfeit and low-quality goods.

9.4 Judicial protection of intellectual property rights

9.4.1 Establishment of specialised intellectual property rights courts

In China, cases related to patents, new varieties of plants, layout-design of ICs, technical secrets, computer software, monopoly and well-known trademarks are subject to a centralised jurisdiction. To accommodate the centralised jurisdiction of intellectual property disputes, China established three independent intellectual property courts in Beijing, Guangzhou and Shanghai in 2014 and 21 intellectual property trial departments in intermediate people's courts around the country to hear disputes concerning these types of intellectual property rights in 2017.

Further, in 2019 the SPC established an intellectual property court to hear nationwide appeals of cases involving patents and other technical expertise. China also established three independent internet courts in Beijing, Guangzhou and Hangzhou in 2017 and 2018 to hear online copyright disputes and other related online disputes. China also developed a new online trial mechanism to adjudicate intellectual property rights disputes. China is dedicated to improving the judicial protection of intellectual property rights and to protecting new types of intellectual property rights stemming from technological innovation.

9.4.2 Enhanced judicial protection of intellectual property rights

In recent years, the number of intellectual property cases accepted by Chinese courts has increased significantly. Concurrently, PRC courts have adopted a precedents system in rendering judgments and have taken measures to improve the quality of litigation proceedings in intellectual property rights cases. By penalising intellectual property rights violations, the courts better safeguard the legitimate interests of intellectual property rights owners and increasingly deter intellectual property rights violations.

9.5 Alternative dispute resolution development of intellectual property rights protection

China is also actively exploring applying ADR in intellectual property rights protection. By introducing arbitration into intellectual property rights dispute settlements, the number of arbitration cases involving intellectual property rights, especially intellectual property rights contractual disputes, has grown significantly. In 2019 the China Patent Protection Association released the Standard of Mediation on intellectual property rights Disputes, which provides an alternative way to solve disputes through mediation presided over by the people's mediation committee. As an innovative development of ADR, it is promising that it will play an increasingly essential supplementary role in intellectual property rights protection in future.

9.6 New trends and potential risks concerning intellectual property rights protection

In recent years China has optimised and integrated administrative functions for intellectual property rights protection at the national level. To allow a comprehensive enforcement of intellectual property laws, China established the SAMR to facilitate supervision over patent and trademark infringement and counterfeiting. China also restructured the NIPA in 2018, integrating the Patent Re-examination Board and Trademark Review and Adjudication Board, which further improves the administrative protection rendered over intellectual property rights. The establishment of special intellectual property rights courts is also improving the quality and efficiency of intellectual property rights proceedings in China. These measures have been taken to ensure that IPR protection and management in China is and continues to be more efficient and effective in practice.

Given the continuous review of and amendments to intellectual property laws and enhancements to the judicial protection of intellectual property rights, intellectual property rights owners should stay apprised of changes in applicable law and the appropriate forum for seeking intellectual property rights recognition and protection.

Chapter 10: Financing

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10.1 Banking and finance

10.1.1 Introduction

Financial regulatory framework

Under the current financial regulatory framework in China, the financial market is subject to the supervision of: (1) the Financial Stability and Development Commission of the State Council; (2) the PBOC; (3) the China Banking and Insurance Regulatory Commission (CBIRC) (which is a merged entity of the China Banking Regulatory Commission and the China Insurance Regulatory Commission as of 2018); and (4) the CSRC. This group is collectively known as the 'One Committee, One Bank and Two Commissions'.

The Financial Stability and Development Commission of the State Council, established in 2017, is mainly responsible for promulgating macroeconomic policies and maintaining economic stability. The PBOC, acting as the central bank of China, focuses on formulating and implementing monetary policies (including the interest rates of deposits and loans), and one of its most important subdivisions, SAFE, is mainly responsible for foreign exchange control. The CBIRC is the direct regulator of both the banking industry and insurance industry. The CSRC is the direct regulator of the securities and futures industry.

Criteria for financial business

Currently, there are around 15 types of financial institutions in China subject to the supervision of the CBRIC. For these intuitions, the industry entry criteria are very strict, and most such institutions must obtain a financial licence before conducting financial business.

Main bank financing regulations

The commercial loan is the most important business of banks. As the most fundamental regulation and guideline for regulating loan financing, the General Rules for Loans, implemented by the PBOC and published on 1 August 1996, set out the basic rules for loan transactions, that is, loan types, tenor and interest, the respective obligations and rights of the lenders and borrowers, the relevant supervisions and penalties, and so on.

In 2009 and 2010 CBRIC promulgated three measures and one guideline to regulate the four main types of commercial loans in China's market: the Interim Measures on the Management of Working Capital Loans; the Interim measures on the Management of Personal Loans; the Interim Measures on the Management of Fixed Assets Loans; and the Guidelines on Project Financing Business. All four are regarded as an important supplement to and implementing rules of the General Rules for Loans.

Loan interest rate

Since the 1990s all financial institutions in China's loan market have determined their interest rate by floating up or down certain proportions of the benchmark interest rate announced by the PBOC (the 'PBOC base rate').

In the second half of 2019 the PBOC issued [2019] Notices 15 and 30, aiming to reform and improve the LPR mechanism debuted in October 2013. The notices stipulated that the facility interest rate must be quoted by reference to the LPR, which is calculated on the basis of the LPR quotations submitted by 18 quotation banks on the 20th of each month.

Security

In China, security types are mainly stipulated in the PRC Property Law, the Security Law and its corresponding judicial interpretation, and relevant department rules and regulations.

A basic principle for all security arrangements in China is that only such a type of security that is explicitly stipulated in PRC laws will be recognised and effectively performed.

Another important feature of the security laws in China is that the security contract will come into effect when it is duly signed, but the security right will only be created upon the completion of certain perfection formalities (ie, approval, registration and filing) with relevant government authorities.

FX matters

Cross-border bank financing transactions are highly supervised and controlled by SAFE in China. Such cross-border transactions can be mainly divided into: (1) cross-border debt financing; and (2) cross-border guarantee. Conducting any such transactions shall be subject to strict regulations and formalities (including registration, filing and reporting) by SAFE, CBIRC and other authorities.

10.1.2 Financial market in China

Financing scale

In recent years China's financing scale has increased at an annual growth rate of around ten per cent. Although the growth rate has slowed down as a result of the government's financial deleveraging policy, the trend of the financing scale is growing steadily. According to data published by the PBOC, the social financing scale was RMB 256.36tn at the end of January 2020, an increase of 10.7 per cent.

Cost of financing

Starting from 4.15 per cent on 20 August 2019, China's one-year loan LPR decreased to 4.05 per cent on 20 February 2020. The five-year LPR edged down by ten basis points (bps) as well to 4.75 per cent on 20 February 2020 from 4.85 per cent on 20 August 2019. In response to the difficulties and high costs of financing, the Chinese government has reduced the required reserve ratios four times and applied a series of measures to ease funding shortages faced by small and micro enterprises.

10.1.3 Regional difference in practice

In China, when the central government authority issues an administrative regulation, local government authorities will usually issue corresponding implementing rules to provide details on the implementation and operation of these administrative regulations. Such local implementing rules are stipulated within the regime of the administrative regulation at the central level, but will differ in detail, as each will take into consideration their respective local practice and situation.

The complicated policy-making mechanism in China requires that the foreign investor or financial institutions pay attention not only to the central regulations but also local policies and practice when carrying on financial transactions in China.

10.1.4 Challenges with opportunities

Professionalism and internalisation

With China's 'Going Out' policy, more and more Chinese companies are investing abroad. Overseas or cross-border M&A financial transactions, therefore, occur frequently. PRC domestic banks play an important role in these financial transactions. However, because of a lack of practice, PRC domestic banks still need to gain more international financing experience and become more professional in the financing industry.

Marketisation of the interest rate

As a result of the aforementioned LPR reform, the majority of financial institutions in China's market now face a dilemma: on the one hand, they have no clue as to how to quote a proper interest rate, and on the other, they have strong doubts about how the final LPR formed on the basis of quotations could reflect their actual funding costs and the loan price. This dilemma casts a shadow over the future of the LPR.

Seeking innovation is the best way to escape the existing situation. Financial institutions urge the establishment via Fintech of a scientific pricing mode; however, perfecting the provisions related to the market interest rate (eg, adding a market disruption definition and a flexible pricing adjustment mechanism) could be a choice.

A more open and international financial market

Since 2017 the Chinese government has issued a series of regulations and policies to ease restrictions for foreign enterprises in finance. In particular, in June 2019 the Financial Committee of China's State Council published 11 measures to further promote the opening up of the financial market.

With the continuous economic growth and the government's efforts, the Chinese financial market is moving towards a more open and international market with more consistent rules. It is foreseeable that the Chinese government will implement more policies for the opening up and internationalisation of the financial market.

10.2 Equity financing

There are two main methods for a company to raise funds using equity financing: seeking a private equity investment or conducting an initial public offering (IPO). This section outlines the two financing tools.

10.2.1 Private equity investment

A booming market of private equity investment

China has emerged as one of the largest equity investment markets; its importance is globally recognised. According to data released by the Asset Management Association of China (AMAC), by the end of November 2019 China had more than 14,000 equity investment institutions, managing assets with a total value in excess of RMB 11tn (approximately \$1.6tn).[40]

Typical structures of foreign investor's private equity deals

To become involved in China's private equity market, foreign investors typically use two structures: (1) FDI, whereby a foreign investor directly invests into a PRC target company in exchange for equity interest or shares; and (2) setting up a foreign-funded investment platform in China and using the foreign-funded investment platform to invest in a PRC target company. The regulatory framework for FDI has been discussed in other chapters and thus does not require elaboration here.

With respect to foreign-funded investment platforms, there are currently three types of platform that can be set up by a foreign investor: a qualified foreign limited partnership (QFLP), a foreign-funded investment company or a foreign-funded startup investment enterprise.

Qualified foreign limited partnership

A QFLP refers to a private equity investment fund that a foreign investor subscribes to for its capital commitment as a limited partner. A QFLP is generally established in the form of a limited partnership, involving one or more foreign investors as its limited partners. The general partner of such a fund may be either a domestic or foreign resident. A QFLP's fund manager may be a foreign-funded equity investment management enterprise incorporated in China, provided it has been registered with AMAC as a private equity fund manager, for which a PRC legal counsel's due diligence report and legal opinion are required to be submitted to AMAC for filing.

40 The exchange rate between the US dollar and RMB is around 6.9.

In China many local municipality governments have enacted and implemented rules governing thresholds for foreign investors of a QFLP, as well as established, compliance requirements on any preferential tax treatment entitled to the QFLP.

To set up a QFLP, the foreign investor must meet a threshold in terms of financial capacity, industrial experience, existing investment projects and personnel qualifications. For example, if a foreign investor elects to set up a QFLP in Shanghai, it shall self-own capital of at least $500m or manage funds or assets of no less than $1bn; the total subscribed capital commitment to a QFLP shall be no less than $15m; and any sole limited partner's capital contribution to a QFLP shall be no less than $1m.

Investment company

A foreign investor is allowed to set up an investment company, provided that it can meet the entry criteria to be an eligible promoter of such a company. An investment company can discretionarily use RMB sourced from the settlement of its capital fund in foreign currency to make an equity investment in a domestic company.

It is noteworthy that SAFE issued a new circular in October 2019, according to which a non-investment FIE is permitted to legally make an equity investment in a domestic company with its capital funds under several compliance requirements. As such, the difference between an investment company and a non-investment FIE has been narrowed.

Startup investment enterprise

Foreign-funded investment enterprises incorporated for the purpose of engaging in an investment of startup enterprises and providing management services to the same will be categorised as a startup investment enterprise. Compared with the QFLP, the investment of a startup investment enterprise is subject to a smaller scope, namely a high-tech enterprise that has not been listed on a stock exchange.

10.2.3 Initial public offering in China

Overview of China's initial public offering market

China's IPO market is undergoing rapid and steady growth. Statistically speaking, a total of 373 Chinese companies completed their IPOs in 2019, raising RMB 514.705bn (approximately $74.59bn) in total, which works out as a yearly growth of 16.20 per cent and 23.67 per cent, respectively.

Introduction to China's stock markets and regulation framework

In development since the 1990s, China's stock market has formed a multi-level capital market system, which includes: (1) the 'floor market', consisting of the main board (the 'Main Board'), the Small and Medium-sized Enterprise Board (the 'SME Board'), the Growth Enterprise Market (GEM) and the SSE Science and Technology Innovation Board (the 'STAR Board'), which was newly launched in June 2019; and (2) the 'over-the-counter market', comprised of the National Equities Exchange and Quotations and various regional equity trading markets.

Among these markets, the Main Board has the strictest listing thresholds on the issuer in terms of its operating period, capital size, profits (eg, the accumulative net profits for the last three fiscal years exceeds RMB 30m, approximately equivalent to $4.35m), market value and other aspects, and thus many big players choose to be listed on the Main Board, while the enterprises listed on the SME Board, GEM and the National Equities Exchange Quotations have a relatively smaller scale and are less profitable. In addition, the unprecedented listing rules of the STAR Board allow an overseas company with a 'variable interest entities' structure to list its stock or issue its depository receipts on the STAR Board, provided that such an issuer has fulfilled certain financial indications and compliance requirements. Therefore, the STAR Board may become more open and compatible to multinational high-tech companies.

Regulatory framework of IPOs

China has promulgated numerous laws governing the issue and trading of shares, as well as the disclosure of information of an issuer, which includes various guidelines from the security regulatory authority and stock exchanges. The CSRC is the highest supervisory and regulatory institution for securities in the PRC, responsible for the formulation of policies relating to securities; drafting of securities laws and regulations; and supervision of the securities markets, market intermediaries and participants; as well as the supervision and regulation of securities transactions.

The primary laws, regulations and rules that lay the cornerstones of the current regulatory framework for IPO in China (including the STAR Board) are set out below:

- PRC Securities Law (2019 Revision) issued by the Standing Committee of the NPC on 28 December 2019 (the 'New Securities Law'), which became effective on 1 March 2020 and regulates, among other things, the issue and trading of securities, takeovers by listed companies, securities exchanges, securities companies, and the duties and responsibilities of the PRC State Council's securities regulatory authorities;
- Measures for the Administration of the Initial Public Offerings and Listing of Stocks, promulgated by CSRC with the latest version revised on 6 June 2018;
- Measures for the Administration of the Registration of IPO Stocks on the Science and Technology Innovation Board (for Trial Implementation), promulgated by CSRC on 1 March 2019;
- Listing Rules of the SSE, promulgated by the SSE, with the latest version revised on 30 April 2019, and Listing Rules of the SZSE, promulgated by the SZSE, with the latest version revised on 30 April 2019; and
- Listing Rules of the Science and Technology Innovation Board, promulgated by the SSE, with the latest version revised on 1 March 2019.

Focus on issues in connection with the reform of China's IPO system

After several years of amendments and deliberations, the long-awaited New Securities Law recently came into effect on 1 March 2020. The New Securities Law showcased vast changes and reforming measures, including: (1) adopting a registration-based IPO system to replace the existing approval system; (2) imposing more severe punishments for violations (eg, financial fraud and insider trading); and (3) enhancing information disclosure and protection for retail investors.

Prior to the promulgation of the New Securities Law, the public issuance of securities had to be reported to the CSRC for case-by-case approval, and now the New Securities Law has officially abolished such an administrative approval system. Instead, a registration system will be used under a prescribed timeframe. However, as the detailed rules and guidance for such a registration system have not yet been published, there are many uncertainties concerning the implementation of the registration system and the linkage between the new legislation and old legislation during the interim period.

Chapter 11: Privacy laws and data protection

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11.1 General legal framework

11.1.1 Applicable laws and regulations

There is no single comprehensive privacy or data protection law in China. At present, the principal personal data protection legislation in China is the Cybersecurity Law of the PRC (CSL), which became effective on 1 June 2017. It sets out general data protection requirements for all network operators regarding personal data collection, use and sharing. When a foreign investment company owns or manages networks (including websites, internet platforms, local area networks and industrial control systems), or provides a network service within the territory of China, it is identified as a network operator and the CSL applies. Further, companies providing services to Chinese citizens/users via offshore entities, especially those involving data cross-border transfer, may also be subject to personal data protection rules established by the CSL.

To refine and supplement the general requirements in the CSL, the regulatory departments and national standard-formulating agencies have enacted a number of regulations and normative documents, including Provisions on the Cyber Protection of Children's Personal Information; Administrative Measures on Data Security (Draft for Comments); Measures for Security Assessment for Cross-border Transfer of Personal Information (Draft for Comments); Regulations for the Security Protection of Critical Information Infrastructure (Draft for Comments); and GB/T 35273-2017 Information Security Technology – Personal Information Security Specification (the 'Standard'). Although the Standard is not compulsory, it has been widely recognised as guidance for good practice by both the competent authorities and companies. The Standard is designed to regulate personal data controllers' behaviour in collecting, storing, using, sharing, transferring or publicly disclosing information, or at other stages of data processing.

Some general regulations, such as the Criminal Law, the General Rules of the Civil Law and the Tort Liability Law, also have an impact on privacy and data protection in China. In addition, data protection requirements also exist in certain sector-specific legislation, especially the sectors of banking and finance, medical and health, e-commerce, telecommunications and so on.

11.1.2 Competent authorities

China has no single authority responsible for enforcing provisions relating to data protection. Under the CSL regime, the main competent authorities are the Cyberspace Administration of China (CAC), Ministry of Public Security, Ministry of Industry and Information Technology and SAMR. Certain sector-specific regulators, such as the PBOC and National Health Council, are also authorised to implement and enforce relevant sector-specific legislation.

11.1.3 Data protection obligations of network operators

Foreign companies, as network operators or data controllers, shall bear the data protection obligations during their operations in China, including but not limited to:

- abiding by the ‘lawful, justifiable and necessary’ principles to collect and use personal data;
- obtaining prior consent from the relevant data subjects when sharing or disclosing the collected personal data to a third party (including their affiliates);
- responding promptly to requests from data subjects to provide access to, rectify or delete their personal data;
- taking technical and other necessary measures to ensure the security of the collected data, and to establish and improve the system for data protection;
- taking immediate remedies and reporting to the competent authority and affected data subjects in case of actual or threatened disclosure, damage or loss of data collected; and
- appointing network security officer(s) to protect the security of the network, and, if necessary, appointing a data protection officer or setting up a data protection department.

11.2 Trends and development

The implementation of the CSL and its supporting measures show that Chinese legislators are gradually consolidating the laws to protect national cyberspace sovereignty and network security. The illegal processing of personal data and privacy policies has been the central concern for data protection regulators.

In 2019 the CAC, Ministry of Industry and Information Technology, Ministry of Public Security and SAMR jointly carried out their one-year ‘special campaign’ against apps unlawfully collecting and using personal data. The authorities aim to enhance the supervision and punishment of unlawful collection and use of personal data, requiring industrial associates to assess their privacy policies, as well as the collection and use of personal data by, in particular, apps that have a large user base and are frequently used in daily life.

According to published statistics in September 2019, more than 8,000 complaints have been accepted by the authorised working group of the campaign. The group has conducted security assessments of over 400 frequently used apps and sent out rectification suggestions to more than 100 app-operating entities.

Furthermore, in order to regulate the collection and use of user information by mobile apps, the CAC and SAMR launched the Implementation Rules on Security Certification for Mobile Internet Applications in March 2019, which encourages apps operators voluntarily to apply for app security certification.

11.3 Key compliance risks for foreign companies

11.3.1 Consent of the data subject

In general, if a foreign company wishes to collect, use or transfer personal data from data subjects (eg, registered users of an app) during operation, prior consent is required from the data subjects, just as it is for domestic companies.

Pursuant to Article 41 of the CSL, foreign companies (as network operators) shall abide by 'lawful, justifiable and necessary' principles to collect and use personal data by announcing their rules for collection and use, expressly notifying the subject of the purpose, methods and scope of such collection and use, and obtaining consent from the subject of such personal data. If the collected personal data includes sensitive personal data (eg, phone numbers, ID number and address), pursuant to section 5.5 of the Standard, foreign companies shall obtain explicit consent, meaning the specific and unambiguous expression of will freely made by fully informed data subjects.

In contrast to the CSL, section 5.4 of the Standard further provides certain exceptions to the requirements to obtain consent, including national security, public health and security necessary for executing or performing contracts, among others. Nonetheless, it is important to note that the Standard is not an enforceable legal document but a set of recommendations and guidelines. Therefore, it is recommended to obtain consent from the data subject whenever possible.

11.3.2 Sharing and disclosure of personal data

According to the Standard, when foreign companies intend to share or disclose the collected personal data to a third party (including their affiliates), they shall obtain prior consent from the relevant subjects. To meet the consent requirements, foreign companies shall inform subjects, usually in the form of a privacy policy, of the purposes of the sharing, disclosure or transfer of the personal data, the scope of the transferred data and the data recipient. There is an exception when the personal data to be shared or transferred has been processed for de-identification purposes and the data recipient is unable to reidentify the data subjects.

Pursuant to section 8.2 of the Standard, foreign companies are also recommended to:

- assess the personal data security impact in advance, and take effective measures to protect data subjects according to the assessment findings;

- maintain accurate records of the particulars of sharing and transferring personal data, including the date on which the data is shared or transferred, amount of data shared or transferred, purposes for sharing or transferring the data, and basic information of data recipients, and keep these records safe; and
- help data subjects to understand the particulars of the data recipients' storage and use of their personal data and learn about the rights of data subjects, such as accessing, modifying and deleting their own personal data and cancelling their own account.

11.3.3 Cross-border data transfer restrictions under the CSL

It is common practice for multinational companies to deploy unified and connected IT systems and office networks to realise global centralised management. When foreign companies transfer certain personal data or operation data collected within China to overseas affiliates or cooperative partners, the cross-border data transfer regulatory requirements apply.

Pursuant to Article 3 of Measures for Security Assessment for Cross-border Transfer of Personal Information (Draft for Comments), published by the CAC on 13 June 2019, before the cross-border transfer of personal data, foreign companies shall bear the data protection obligations below, including but not limited to:

- obtaining prior consent from the data subjects and informing them of the purposes of the sharing, disclosure or transfer of the personal data, the scope of the transferred data and the data recipient;
- conducting a security assessment for the cross-border transfer of personal data, and filing the assessment results with the local CAC office;
- executing data transfer agreements with overseas data recipients;
- maintaining a log of all cross-border transfers of personal data for at least five years; and
- submitting an annual report to the CAC on the status of cross-border transfers and the performance of data transfer agreements.

Note that, as outlined in sector-specific regulation, certain sensitive personal data, such as personal biometric information and credit information, can only be stored or processed within the territory of China. In principle, it is prohibited for such sensitive personal data to be transferred to overseas entities.

11.3.4 Data security standard

The CSL implements a multi-level protection system for cybersecure network protection, which classifies networks into five grades and progressively imposes higher security requirements for each grade.

Foreign companies, as network operators, are responsible for taking technical and other necessary measures to ensure the security of data they collect and to prevent the data from being accidentally disclosed or destroyed. Companies shall evaluate and determine the grades of their operating networks, and companies with networks of Grade 2 or higher shall file such networks with the local public security bureau.

If a foreign company entrusts a third party to process personal data on its behalf, it shall ensure that such a processor provides an adequate level of protection to the personal data involved, as provided in section 8.1 of the Standard.

11.4 Conclusion

With the strict enforcement of the CSL, cybersecurity and data protection has become a priority of corporate compliance review. Although many multinational companies have established comprehensive data protection management systems based on a European or American standard, it is highly recommended to examine the above compliance risks and localise the management system to meet Chinese regulatory requirements.

Chapter 12: Competition law

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12.1 Legal framework of China's competition law

A competition law system is a synthesis of various laws and regulations that regulate the competition of market entities. It takes the competition relationship in market activities and the competition management relationship between managers and operators as the regulative object and, in the main, is intended to maintain the normal competition order, with anti-monopoly and anti-unfair competition as the core content.

12.1.1 Laws and administrative regulations

In addition to the Antitrust Law (released on 30 August 2007) and Law of the PRC Against Unfair Competition (revised on 23 April 2019), there are also other provisions in relation to competition regulation among other laws in the current Chinese competition legal system, such as the Pricing Law (released on 29 December 1997), Law on the Protection of Rights and Interests of Consumers (revised on 25 October 2013), E-commerce Law (released on 31 August 2019) and Advertising Law (revised on 26 October 2018).

Administrative regulations also make up an important part of the competition legal system, such as the Interim Provisions on the Prohibition of Monopoly Agreements; the Interim Provisions on the Abuse of Dominant Position in the Market; the Interim Provisions on Stopping Abuse of Administrative Power; and the Interim Provisions on Restricting Competition, which was promulgated by SAMR and came into effect on 1 September 2019. Others include the Regulation on Prohibiting Infringement upon Trade Secrets (1998); Certain Regulations on Prohibiting Unfair Competition Activity Concerning Imitating Specific Names, Packaging or Decoration of Well-known Commodities (1995); Interim Provisions on Prohibition of Commercial Bribery (1996); and Interim Provisions on

Prohibiting Bid-Rigging (1998), which were issued by the former State Administration for Industry and Commerce; and Provisions on the Merger and Acquisition of Domestic Enterprises by Foreign Investors, which was released in 2009 by MOFCOM.

12.1.2 Judicial and other interpretations

In China judicial interpretations have a unique function as an important component of the legal system. The most important judicial interpretations about competition law include the Provisions on Several Issues concerning the Application of Law in the Trial of Monopoly Civil Disputes (2012); Several Issues Concerning the Applicable Laws in the Trial of Unfair Competition Civil Cases Interpretation (2007) issued by the SPC; and Answers to Several Questions in the Trial of Unfair Competition Cases (Trial) (1998), issued by the Beijing Higher People's Court. In addition, the provisions on competition in the international conventions to which China is a party also play a significant role in China's competition legal system. In addition, some competition policies issued by relevant government agencies are also worthy of attention, that is, various policies and measures adopted by the government to promote and protect competition.

12.2 Competition enforcement practices in 2019

In April 2018 the SAMR was officially founded and became the main enforcement agency of competition law. According to the Law of the PRC Against Unfair Competition, some other administrative organisations, such as NIPA and CBIRC, also have corresponding anti-unfair competition enforcement power in their respective fields.

The competition law enforcement agencies are divided across central and provincial levels. In 2019 the general authorisation system was established, that is, the SAMR is responsible for investigating and dealing with cases that are inter-provincial, extremely complicated or have a significant influence on the country, and that need to be investigated by SAMR directly. Provincial enforcement agencies can investigate monopoly acts within their own administrative regions.

A total of 38 cases of monopoly behaviour were investigated and handled by the national market supervision system in 2019. At present, SAMR announces on its official website 17 cases concerning monopoly agreements and abuse of market dominant position. A total of 432 cases of concentrations of undertakings have been concluded. Among them, there are five cases with conditional approval. A total of 17 non-legally notified cases were punished. As for administrative monopoly, the SAMR announced a total of 16 typical cases in 2018.

China currently regulates seven types of unfair competition behaviours: commercial confusion acts; commercial bribery; false publicity; infringement of trade secrets; unfair prize-attached sales; damage to commercial reputation; and new types of unfair competition in the internet field. In July 2019 the SAMR launched anti-unfair competition enforcement actions in key areas across the country from August to December, focusing on investigating counterfeiting, commercial confusion, commercial bribery, false publicity, commercial defamation and other acts of unfair competition. As of 25 October 2019, a total of 2,173 cases of unfair competition were investigated and dealt with nationwide, with a value of RMB 101m.

12.3 Competition judicial practice in 2019

According to the statistics of the Judgment Documents Network, in 2019 courts of all levels across the country concluded 41 antitrust civil lawsuits. From judicial practice, we can see that it is very difficult for the plaintiff to prove the dominant position of the defendant in the relevant market in most cases. As of March 2020, according to Chinese law database pkulaw.com, courts of all levels across the country concluded 1,027 unfair competition disputes in 2019, mainly involving commercial bribery, infringement of trade secrets and counterfeiting.

Currently, the SPC hears appeals in intellectual property cases heard by intellectual property courts and intermediate people's courts. The SPC applied the so-called 'Leap Appeal System' for the first time in an antitrust lawsuit in September 2019.

12.4 Competition policy trends and hint for companies

At present China is one of the world's three major competition law enforcement regions. Competition law enforcement is becoming more stringent and commonplace. When it comes to competition law enforcement and judicial practice, it's forseeable that international cooperation will continue to improve at pace with economic globalisation. Much emphasis will be placed on internet-related competition violations and cases where competition law overlaps with intellectual property.

The Regulation on the Optimization of the Business Environment (2020) promulgated by the State Council has underlined that law enforcement efforts against monopoly and unfair competition shall be stepped up so as to create a market environment for fair competition. It can be expected that the vigorous promotion of the fair competition review system will improve the business environment significantly.

Chapter 13: Dispute Resolution

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Similar to other legal systems around the world, mediation, arbitration and litigation are the three main mechanisms for resolving international commercial disputes in the PRC. According to a work report released by the SPC in 2019, more than 3 million commercial disputes were concluded at the stage of first instance trial in 2018.[41] Meanwhile, arbitration institutions in China also saw an increase in the number of cases handled in 2018. For example, the China International Economic and Trade Arbitration Commission presided over 2,962 cases in 2018, whereas the Beijing Arbitration Commission/Beijing International Arbitration Center oversaw 4,872 arbitration cases at the end of that year.[42, 43] As such, it is of little doubt that a large number of commercial disputes in China are now resolved with litigation and arbitration proceedings.

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41 ChinaCourt, *Report on the Work of the SPC* (full text) www.chinacourt.org/article/detail/2019/03/id/3791943.shtml accessed 13 May 2020.

42 China International Economic and Trade Arbitration Commission, *CIETAC 2018 Work Report* and *2019 Work Plan* www.cietac.org/index.php?m=Article&a=show&id=15803 accessed 13 May 2020.

43 Beijing International Arbitration Centre, *2018 Annual Report* www.bjac.org.cn/news/view?id=3375 accessed 13 May 2020.

13.1 Commercial litigation

Judicial litigation has always been one of the most effective methods in China for resolving international commercial disputes. To avoid irreparable harm, and to ensure effective legal enforcements after prevailing in a lawsuit, disputing parties in China often prefer judicial litigation because of the various preservation measures (ie, interim/provisional measures and/or injunctive relief) available against an adverse party. Adopting a 'second instance ruling being final' doctrine, the selection of the appropriate jurisdiction/forum for commercial litigation often depends on the amount of controversy and geographical locations in the case.

As such, this type of litigation system might sometimes result in prolonged/protracted trial time. However, in contrast with arbitration-like proceedings, an extensive review by the appellate court (second instance) may provide more legal certainty and clarification.

In recent years the number of foreign-related cases resolved via litigation in China has increased drastically, which in turn has resulted in corresponding legal reforms initiated by both the legislative body and the judicial system.[44] As a result, in April 2011 the Applicable Laws on Foreign-Related Civil and Commercial Relations came into effect.

At the same time, the judicial system has greatly increased the number of courts authorised to handle these foreign-related cases. More specifically, before 2011 the 'first instance' jurisdiction of foreign-related commercial disputes was exclusively limited to provincial intermediate people's courts and courts of identical jurisdictional level. Only recently, pursuant to a notice issued by the SPC that came into effect on 1 January 2018, all intermediate and basic courts can now hear foreign-related civil and commercial cases.

With the ever-increasing number of international commercial disputes, in January 2018 the Chinese government issued the Opinion Concerning the Establishment of the Belt and Road International Commercial Dispute Resolution Mechanism and Institutions, in which three recommendations for resolving cross-border commercial disputes were put forward: first, the SPC will establish China International Commercial Courts (CICC); second, the SPC will lead in establishing the International Commercial Expert Committee; third, the establishment of diversified dispute resolution mechanisms, which effectively integrate litigation, mediation and arbitration so as to create a convenient, expeditious and low-cost 'one stop' centre for dispute resolution, will be promoted. Subsequently, the First and Second International Commercial Courts were established in Shenzhen and Xi'an, respectively. Cases tried by the CICC shall be heard by a collegial panel consisting of three or more judges. The CICC practices the 'first instance being

44 'Since the second half year of 2013, the number of international cases in civil or commercial matters has increased dramatically', according to Chen Yifan, 'Big Data analytic based on international civil or commercial cases', *Legal System and Society*, January 2018 (part one).

final' doctrine. All judgments and rulings made by the CICC are final and binding on the parties with legal effect.[45] By the end of 2019, CICC had accepted 13 cases.[46]

13.2 Commercial arbitration

Many foreign enterprises prefer arbitration as a way of dispute resolution. By the end of 2018, there were 255 arbitration institutions in China.[47] The total number of cases accepted by the China International Economic and Trade Arbitration Commission in 2019 was 3,333 (a year-on-year growth of 12.53 per cent), of which 617 were foreign-related, with parties coming from 72 countries and regions. An increasing number of parties are selecting international conventions and various national laws as substantive reference in arbitration, such as the UN Convention on Contracts for the International Sale of Goods, Australian law and Italian law.[48] In addition, since China is a member of the New York Convention, at least in theory, a party with an arbitral award rendered in China may petition for recognition and enforcement in any other member countries of the Convention.

In accordance with China's arbitration law and civil procedure law, as well as relevant judicial interpretations, the standard of review of a domestic arbitral award differs from a foreign arbitral award. The people's courts set forth different grounds and conditions for the non-enforcement or cancellation of domestic and overseas arbitration awards. As a result, the court generally follows a stricter standard when reviewing a domestic arbitration award; however, it focuses mainly on procedural matters/issues with overseas arbitral awards.

13.3 Mediation and alternative dispute resolution

Compared with arbitration proceedings, the process of mediation is considered by many as more flexible, confidential and effective. It is sometimes much easier for parties involved in a commercial dispute to come to terms simply because of the less stressful atmosphere and flexibility provided in a mediation process.

Under relevant laws and regulations of the PRC, mediation is also common practice. Currently, however, judicial authorities in China only recognise mediation agreements issued by the people's courts, arbitration institutions and People's Mediation Committees. A mediation agreement reached under the supervision of the People's Mediation Committee shall be enforced only after a confirmation made by the court. However, with respect to a settlement agreement resulting from a mediation proceeding abroad, there is no existing law addressing the process of application and/or enforcement of remedy as of yet.

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45 Provisions of the SPC on Several Issues Regarding the Establishment of CICC (Fa Shi [2018] No 11):
Art 5 s: 'Cases tried by the International Commercial Court shall be heard by a collegial panel consisting of three or more judges.'
Art 15: 'A judgment or ruling made by the International Commercial Court is a legally effective judgment or ruling. A conciliation statement made by the International Commercial Court shall have the same legal effect as of a judgment after its receipt signed by the parties.'

46 CICC Court, 'The First International Commercial Court of the SPC Concluded the First Five Cases Efficiently' http://cicc.court.gov.cn/html/1/218/149/156/1545.html?from=groupmessage accessed 13 May 2020.

47 'According to the statistics of the Ministry of Justice, there were 255 arbitration committees with more than 60000 staff by the end of 2018', Ministry of Justice of the PCR, the Ministry of justice declares the Reform and Development Goals of arbitration in the new era www.moj.gov.cn/Department/content/2019-04/02/612_231935.html accessed 13 May 2020.

48 China International Economic and Trade Arbitration Commission, *CIETAC 2019 Work Report,* www.cietac.org/index.php?m=Article&a=show&id=16447 accessed 13 May 2020.

Another recent phenomenon in the realm of mediation is that China's judicial authorities have intentionally expanded the scope of subject matter in mediation. On 16 October 2017 the SPC and the Ministry of Justice issued the Opinions on the Pilot Work of Mediation by Lawyers, allowing one or more lawyers, under the colour of mediators, to assist relevant parties in reaching an agreement through voluntary negotiation in 11 provinces and cities.[49] In addition, the establishment of an ad hoc arbitration system in various pilot FTZs is also under active discussion and preparation.[50]

13.4 New trends and challenges

With ever-increasing globalisation, dispute resolutions such as litigation, arbitration and mediation have advantages and disadvantages. Most importantly, the modern legal profession recognises these proceedings to be mutually beneficial, seamlessly integrating with each other. For example, the idea and principle of mediation is effectively combined into both litigation and arbitration proceedings in China.

In order legally to promote holistic approach integrating the various dispute resolutions on a singular platform, in 2018 Justice Luo Dongchuan from the SPC stressed the idea of creating a 'one-stop' international commercial dispute resolution mechanism. With support from CICC and the International Expert Committee, this mechanism is expected to become one of the first 'one-stop' platforms integrating litigation, mediation and arbitration in a coherent and systematic format.[51] With such elevated expectations, some questions still remain as to how effectively to identify competent arbitration and mediation institutions and how to transfer cases effectively among the various institutions, as well as how to allocate relevant expenses among the parties while ensuring the purpose of the 'one-stop' mechanism. These issues indeed demand cautious deliberation, as we continuously acquaint ourselves with professional experiences, as well as the implementation of new laws and policies.

Chapter 14: Development and practice of wealth management legal business

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With the continuous development of the Chinese economy, the affluent class in China has grown rapidly in the past few decades. As of 2018 the number of HNWIs with personal investable assets of more than RMB 10m (about $1.43m) nationwide reached 1.97 million, and the overall size of investable assets held by individuals across the country reached RMB 190tn (about $27.2tn).[52] The affluent class is paying more attention to the safety of its wealth. Wealth management for private

49 Opinions on the pilot work of lawyers' mediation by the Ministry of Justice of the SPC.

50 Wen Xiantao, 'UN Convention on International Settlement Agreements Resulting from Mediation and Commercial Mediation in China', China Law Review, No 1 (2019).

51 CICC Court, '"Integration-based Resolutions": China's solution to international commercial dispute' http://cicc.court.gov.cn/html/1/218/149/156/1117.html accessed 13 May 2020.

52 *Private Wealth Report 2019* of China Merchants Bank – Bain & Company.

client legal services, especially for HNWIs, has become an emerging area of legal services in China in recent years.

14.1 Main legal applications of wealth management services

A client's wealth management business involves comprehensive needs, such as marriage, inheritance, tax planning, immigration, family business governance and succession, involving multiple departmental laws, including non-litigation and litigation businesses, and domestic and foreign legal relationships recognising typical integrated legal practices. The main substantive laws are outlined below:

14.1.1 Application of the Marriage Law

The marriage risks of HNWIs directly affect their wealth security. Lawyers need to provide services based on client needs, such as drafting legal documents, including marital asset agreements, divorce agreements and marital asset division agreements, as well as representing clients in divorce proceedings. Therefore, the Marriage Law of the PRC[53] and related judicial interpretations are important laws applicable to the wealth management business.

14.1.2 Application of the Succession Law

In recent years more HNWIs have entrusted lawyers to take into consideration comprehensive factors with respect to the inheritance arrangements of wealth, before or even after life. Inheritance is done mainly through statutory succession, testamentary succession and legacy. The above arrangements and legal documents need to comply with the Succession Law of the PRC,[54] the judicial interpretation and the guiding cases of the SPC.

14.1.3 Application of the Company Law

The family wealth management business is always accompanied by issues such as the standardisation of family business governance and the delegation of business management rights. Clients usually entrust lawyers to design a complete plan for the inheritance of family businesses to optimise the governance structure of family businesses and plan the inheritance arrangements of equity ownership and operating rights. The validity of the aforementioned legal documents relates to the application of legal provisions, such as the Company Law[55] of the PRC and related judicial interpretations.

14.1.4 Application of the Trust Law

The Trust Law of the PRC[56] was promulgated and taken into effect in 2001. The trust system in China has yet to be improved. However, due to the unique advantages of trusts in wealth management and inheritance arrangements, more clients have begun to engage with lawyers to set up family asset trusts to arrange wealth.

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53 Promulgated and implemented on 10 September 1980, amended on 28 April 2001.

54 Promulgated on 10 April 1985, implemented on 1 October 1985.

55 Promulgated on 29 December 1993, fourth amendment on 26 October 2018.

56 Promulgated on 28 April 2001, implemented on 1 October 2001.

14.1.5 Application of tax laws

In any wealth plan, the tax issues of clients, families and family businesses are involved. If clients or family members have already emmigrated, overseas tax issues will also be involved. Chinese clients have begun to entrust lawyers to provide planning solutions for tax risks of family members or assets in accordance with domestic and overseas tax laws.

In addition to the above laws that are important for wealth management, there are other laws, such as the Insurance Law of the PRC[57] and the application of the Law of the PRC on Choice of Law for Foreign-Related Civil Relationships.[58] When serving clients in China, lawyers often need to help clients achieve their wealth management goals with laws of different disciplines in non-litigation plan formulation, as well as legal representation in litigation.

14.2 Development of China's wealth management services and demand status

In recent decades the scale of China's economic and social wealth has grown rapidly. In 2019, China's share of global wealth reached 17.7 per cent, and China has the second-largest number of HNWIs in the world. The per capita income level and wealth of Chinese residents have increased significantly, and the accumulation of family assets has also brought about the rapid development of the wealth management industry. Chinese HNWIs have begun to pay attention to the long-term allocation of assets and the prevention of legal risks. Currently, more clients are actively commissioning lawyers for overall wealth management and planning, spawning the novel legal service field of wealth management.

14.3 Regional differences in China's wealth management services

As of the end of 2018, the number of HNWIs in 23 provinces and cities in China exceeded 20,000. Among them, HNWIs in provinces like Beijing, Guangdong, Jiangsu, Shanghai and Zhejiang account for about 43 per cent of the national total HNWIs;[59] therefore, judging from the distribution of wealth throughout China, the proportion of HNWIs in first-tier cities is relatively high, and their corresponding wealth management demands have also increased. At the same time, with the continuous development of second and third-tier cities, demand for wealth management legal services in those regions has gradually increased as well. However, holistically speaking, wealth management services and clients are mainly concentrated in first-tier cities with developed

57 Promulgated on 30 June 1995, amended for the third time on 24 April 2015.

58 Promulgated on 28 October 2010, and implemented on 1 April 2011.

59 *Private Wealth Report 2019* of China Merchants Bank – Bain & Company.

economies. Lawyers and wealth management agencies in this business are also mainly concentrated in large cities with developed economies.

14.4 Challenges in wealth management services

14.4.1 Inadequate risk awareness of HNWIs

Although family wealth security and inheritance have become a necessity for HNWIs, due to insufficient publicity and education around the legal risks of assets, clients have paid more attention to investment than security planning, and lack the inclination to entrust lawyers to prevent risks.

14.4.2 Insufficient experience of wealth management professionals and service agencies

Although China's economy is well developed, the corresponding legal framework to meet the needs of HNWIs in respect of private wealth management has yet to mature. Compared with the wealth management industry in Western developed countries, mainland China's wealth management services still have problems, lagging behind the clients' need in terms of cultivating professionals and the experience of legal practices, which at the same time indicates the huge demand gap for wealth management legal services in the market and the vast space for it to develop.

14.4.3 A systematic service pattern of wealth management is needed

HNWIs have diverse asset types and relatively complex familial structures. They face global asset allocation requirements and the challenges of family business inheritance. Wealth management institutions are required to provide a professional service and to coordinate law, tax, finance, immigration, education and other fields to form a systematic service pattern. Generally speaking, China's wealth management industry has not yet formed a systematic and collaborative service model. The main reasons for this include a lack of detail in the laws about wealth management, insufficient experience of professional institutions and practitioners in this field, non-existent systematic industry service standards and the immaturity of the localised legal service model.

14.4.4 Global cooperation ecology is needed

At present, China's wealth management industry has not yet established a global cooperation system. It is difficult to achieve clients' globally integrated wealth management and risk prevention goals. International professional cooperation is in urgent need of development.

From a holistic perspective, the size of China's wealth management market is considerable, and demand is increasing. In future, there will be a vast space for development of China's wealth management legal services, and the entire industry needs to promote the development of services in a coordinated way and pay more attention to international legal service cooperation.

Chapter 15: Environmental policy and law

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When making environmental decisions, Chinese policy and law makers adopt the following two analysis dimensions: sustainable development, and utilitarianism and cost-benefit analysis. So how does environmental policy and law in the PRC unfold from those two dimensions? What is the impact on enterprise?

15.1 Sustainable development

Although China's economic aggregate ranks second in the world in terms of gross domestic product (GDP), China is still declared as a developing country because its per capita GDP is only about $10,000, and, according to UN standards, many people are still subsisting on very low-level income. Although the number of people in this category makes up just 0.6 per cent of the total population, which is far lower than many developed countries, development is still China's top priority. At present, the annual growth rate of China's GDP will not, nor can it be, lower than six per cent.

China has proposed a policy of high-quality development. Focusing on this policy, China has put forward the policy orientation that 'both gold mountain and silver mountain is needed, and green water and green mountain is needed too, and green mountains and lucid waters are indeed mountains of gold and silver'.

The Constitution of the PRC was amended in 2018 and includes 'ecological civilization', paralleled with 'material civilization', and 'beautiful China' paralleled with 'prosperous and powerful China'. It lists 'ecological civilization construction' into the scope of functions and powers of the State Council which is given equal importance to 'economic affairs, urban and rural development'.

Article 6 of the new Environmental Protection Law of the PRC stipulates that '[t]he local people's governments at all levels shall be responsible for the environmental quality within their respective administrative regions'.

For this reason, in 2015 Central Committee of the Communist Party of China (CPC) launched circular inspections of environmental protection across various provinces. During the inspections, special report telephone numbers and email addresses for environmental supervision and inspection were set up. Public accountability and punishment was applied by the Central Environmental Protection Supervision Group to address the problem of weak supervision of environmental protection.

The Secretary of the Gansu Provincial Party Committee of the CPC and the Secretary of the Shanxi Provincial Party Committee of the CPC were held accountable for their criminal responsibility because they had not followed the central environmental policy and even acted in opposition to it. The former was responsible for ecological damage in the Qilian Mountains National Nature Reserve. The latter illegally approved the construction of a large group of villas in the hinterland of

Qinling Mountains. Tens of thousands of other leaders (Chinese middle and senior cadres) at or above the county level, including provincial governors, ministers, county heads and directors, have also been held accountable. The clear signal is that local leaders must focus not only on the economy and development but also on environmental protection.

In addition to the Central Environmental Protection Inspectorate, China has implemented local air and water environmental quality rankings. Lower-ranked local government leaders will be held accountable for any breach of quality levels. The forms of accountability include admonitions, administrative sanctions and party discipline (eg, firing party members and dismissing positions), and criminal responsibility. To this end, the Provisions of the CPC Central Committee and the State Council on the Supervision over the Work of Ecological and Environmental Protection and Measures for the Accountability of Party and Government Leaders for Damage to the Ecological Environment (for Trial Implementation) and so on were specifically issued, and the Regulation of the CPC on Disciplinary Actions, the Regulation on the Selection and Appointment of CPC and Government Leaders and other intra-party regulations were amended.

In the past ten years China has continuously reduced the production capacity of industries such as cement, glass, steel and paper-making; eliminated small-scale and high-energy-consuming industries; proposed to save space for the development environment for high-end services, finance, bio-medicine, the electronic information industry, the aerospace industry, education, culture and tourism, renewable new energy, ecological environmental protection, modern agriculture and animal husbandry, and food; has continuously adjusted and optimised the industrial structure; and has issued a series of environmental supervision policies and laws, and enforced them strictly.

Despite this, China’s environmental policies and laws will not and cannot be separated from the reality of development.

Taking the air environment quality standard as an example, which is also a unified standard in China and the US, for the index of carcinogen PM2.5, the first-class (good) standard in the US is below 12, but the first-class (excellent) standard in China is below 35 (unit: micrograms/cubic metre, the same below). The standards of American Grade 3 (unhealthy for sensitive people) and Grade 4 (unhealthy) are 35–55 and 55–150 respectively, but China’s second-level (good) and Grade 3 (slight pollution) are 35–75 and 75–115, respectively. Therefore, it can be concluded that the grading system in the US is more stringent. When the PM2.5 indicator in China is Grade 2 (good), the US may conclude that it has already reached a moderate pollution level, namely Grade 4 (unhealthy) level.

Obviously, China is pursuing the Sustainable Development Goals and has adopted a progressive environmental protection development strategy. It may take another ten years, but the environmental quality standard in China will gradually increase to be in line with developed countries.

15.2 Utilitarianism and cost-benefit analysis

China has been vigorously pursuing ecological environmental protection policies and laws since 2012 based on the pragmatic notion of ‘gains cannot make up for losses’. President Xi Jinping has often been quoted saying ‘good ecology represents the prosperity of civilization; bad ecology represents the decay of civilisation’.

In the final two decades of the 20th century, China's accelerated desertification, water pollution and water shortage caused by high consumption, and the danger of climate change on the Qinghai-Tibet Plateau caused by greenhouse gases, were major events directly impacting the survival and revival of Chinese civilization.

Since 2012 China has focused on solving the very prominent problem of the low cost of pollution and consequent low illegal cost. To address this, in addition to amending the Environmental Protection Law, five supporting implementation measures have been introduced, which have greatly improved environmental supervision and law enforcement, given the ecological environment law enforcement. The relevant departments now have powers to enforce measures such as a daily penalty, freeze and seizure, limited production and shutdown, disclosure of environmental information and administrative detention.

Such measures include the Measures for the Implementation by Competent Environmental Protection Departments of Consecutive Daily Penalties; Measures for the Implementation of Sealing-up and Impounding by Competent Environmental Protection Departments; Measures for the Implementation by Competent Environmental Protection Departments of Limiting and Halting Production for Remediation; Measures for the Disclosure of Environmental Information by Enterprises and Public Institutions; and Interim Measures for the Transfer by Administrative Departments of Cases of Environmental Violations for which the Penalty of Administrative Detention May Be Applied. These measures are unprecedented. At the same time, the Atmospheric Pollution Prevention and Control Law of the PRC; the Water Pollution Prevention and Control Law of the PRC; and the Law of PRC on the Prevention and Control of Environment Pollution Caused by Solid Waste were amended. The Soil Pollution Prevention and Control Law of the PRC was formulated. The sum of penalties was increased greatly and penalty items were added, such as the maximum sum of RMB 5m for each administrative violation. The sum of daily penalties is currently more than RMB 200m.

From January to November 2018 the total number of cases implemented nationwide was 36,302. Among them, 691 cases were continuously punished on a daily basis, 33.94 per cent less than the same period last year (1,046), and fines amounted to RMB 985m, a decrease of 8.41 per cent compared with the same period last year (RMB 1.075bn). 6,196 cases of production limitation and suspension, a decrease of 20.99 per cent compared with the same period last year (7,842); 7,145 administrative detentions were transferred, a decrease of 8.71 per cent compared with the same period last year (7,827); and 2,367 suspected environmental pollution crimes were transferred, a decrease of 6.18 per cent compared with the same period last year (2,523).

In 2013, the Interpretation of the SPC and the Supreme People's Procuratorate on Several Issues concerning the Application of Law in the Handling of Criminal Cases of Environmental Pollution was issued. The IALCCEP was revised in 2016.

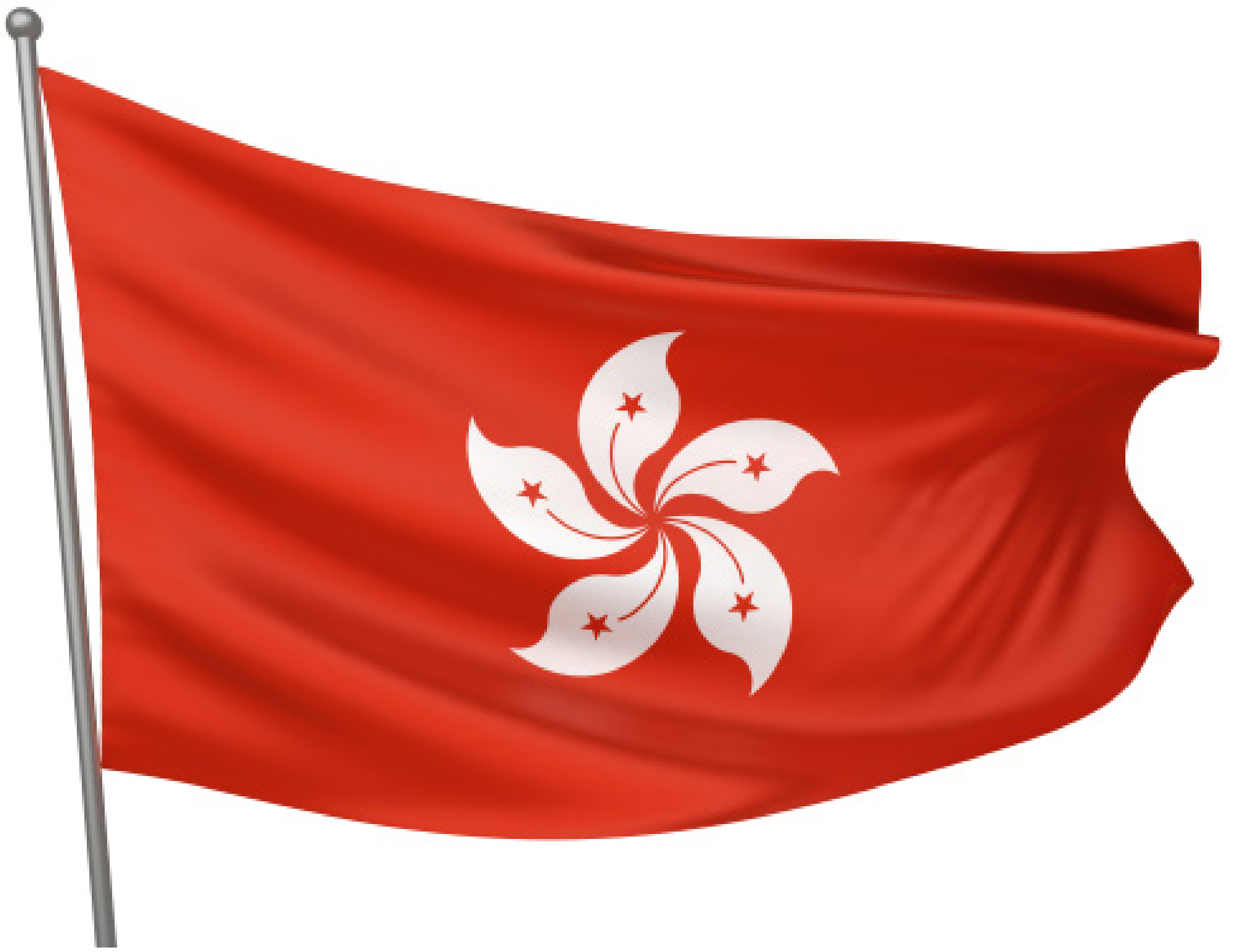
Before 2013 the average annual number of criminal cases of environmental pollution was between 20–30; however, the number of such cases in 2013 was 1,300, four times the total cases before 2013. The number of criminal cases has increased by about 30 per cent each year. According to statistics, in 2017 and 2018 the court's newly accepted criminal cases of environmental pollution were 2,344 and 2,409, and closed criminal cases of environmental pollution were 2,258 and 2,204, respectively.

According to data released by the Supreme People's Procuratorate on 14 February 2019, 26,527 people were arrested for the crime of destroying the protection of the environment and resources. From 2015-2017, 91,131 people were prosecuted for crimes against the environment. In 2018, 15,095 people were arrested and 42,195 people were prosecuted for crimes against the environment.

Environmental pollution crimes include the crime of quantity. The Interpretation of the SPC and the Supreme People's Procuratorate on Several Issues concerning the Application of Law in the Handling of Criminal Cases of Environmental Pollution stipulates that if the environmental pollution causes the loss of public or private property of more than RMB 300,000, criminal responsibility shall be investigated, and if the amount exceeds RMB 1m, the punishment shall be increased. China has issued a series of ecological environmental damage assessment guidelines or methods, such as the Recommended Methods for Authentication and Assessment of Environmental Damage (Edition II) (formerly formulated by the Ministry of Environmental Protection in 2014); Technical Guidelines for Identification and Assessment of Eco-environmental Damage, Soil and Groundwater(Established by the Ministry of Ecology and Environment in 2018); and Regulations on the Classification of Environmental Damage Judicial Authentication (jointly formulated by the Ministry of Justice and the Ministry of Ecology and Environment in 2019) for use in determining the loss amount. Currently there are about 200 environmental damage judicial authentication agencies in China, divided into seven major environmental judicial authentication practice categories, such as identification of wildlife damage caused by ecological pollution, wetland ecosystem damage caused by ecological pollution and urban ecosystem damage caused by ecological pollution.

In 2020 the Supreme People's Procuratorate of the PRC announced a criminal case with supplementary civil claims related to the protection of endangered wild fauna. The defendent was accused of killing and selling 11 pangolins and pangolin products. In this case, the prosecutor hired Wu Shibao, a professor at the School of Life Sciences of South China Normal University and a member of the pangolin expert group of the International Union for Conservation of Nature Species Survival Committee. The professor issued a quantified expert opinion on the damage to the ecological environment in this case. Professor Wu used the Methods of Value Assessment on Wild Animals and Their Products, Catalogue of Terrestrial Wild Animals Standard Value Standards to assess the ecological loss. As a result, the defendant was not only sentenced but also paid fines of RMB 880,000.

Hong Kong SAR



Chapter 1: Introduction

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An international financial centre, Hong Kong is no longer only or primarily a gateway for foreign capital inflow into mainland China. Of course, in 2019 Hong Kong continued to facilitate international investment in the mainland, much like it did in the early years after the transfer of sovereignty to the PRC in 1997. Indeed, at the end of 2018 Hong Kong's outward direct investment to mainland China accounted for more than 40 per cent of the city's total direct investment outflow, making it the most important investment destination for Hong Kong. At the same time, the mainland was Hong Kong's second-largest source of investment, with a share of 26.8 per cent of Hong Kong's inward direct investment.

However, the Hong Kong Special Administrative Region (HKSAR) has in recent years increasingly become an international centre for business, commerce and services in its own right, while reaffirming its position as a global hub for finance, trade and dispute resolution. Over the past decade Hong Kong has consistently achieved top rankings in the World Bank's annual *Doing Business* report. As recently as October 2019 the city moved up from fourth place to rank third among 190 economies in the *Doing Business 2020* report. Hong Kong was, in early 2020, the world's freest economy and – with services sectors making up more than 90 per cent of GDP – also the world's most services-orientated economy.

Hong Kong's success as an international business centre is, in part, due to the 'one country, two systems' principle enshrined in the Basic Law, which is the constitutional document for Hong Kong that guarantees the 'high degree of autonomy' of the HKSAR and recognises the concept of 'Hong Kong people administering Hong Kong'. This principle of 'one country, two systems', in turn, lays the foundation for much of the legal and economic systems on which Hong Kong's commercial fortunes rests. In this spirit, the Basic Law contains, among others, the following major provisions:

- 'The HKSAR has a high degree of autonomy, and enjoys executive, legislative and independent judicial power, including that of final adjudication.'
- 'The socialist system and policies shall not be practised in the HKSAR, and the previous capitalist system and way of life shall remain unchanged for 50 years.'
- 'The laws previously in force in Hong Kong, that is, the common law, rules of equity, ordinances, subordinate legislation and customary law shall be maintained, except for any that contravene the Basic Law and subject to any amendment by the legislature of the HKSAR.'
- 'The HKSAR shall protect the right of private ownership of property in accordance with law.'
- 'The HKSAR remains a free port, a separate customs territory and an international financial centre… There shall be free flow of capital.'
- 'The HKSAR shall pursue the policy of free trade and safeguard the free movement of goods, intangible assets and capital.'

- ‘The HKSAR may on its own… maintain and develop relations and conclude and implement agreements with foreign states and regions and relevant international organizations in the appropriate fields, including the economic, trade, financial and monetary… fields.’

These provisions provide a constitutional footing to the preservation of Hong Kong’s common law system under the supervision of an independent judiciary, while also conferring to the SAR the power to negotiate and conclude trade and investment agreements independently of the mainland. Thanks to the ‘one country, two systems’ formula, Hong Kong has maintained its close investment and trade ties with mainland China, and at the same time has been able to nurture a business-friendly legal and regulatory environment that has led major global corporations and financial institutions to set up regional headquarters and offices in the city.

Against this backdrop, the following 13 chapters will provide an overview of various aspects of Hong Kong’s legal system, each of which is relevant in one way or another to the conduct of business in Hong Kong. In short, the following topics will be addressed:

- Chapter 2 summarises different components of Hong Kong’s business environment. In addition to highlighting initiatives that illustrate the close ties between the SAR and the mainland, the chapter provides an introduction to Hong Kong’s legal and financial infrastructure and tax regime.
- Chapter 3 outlines common forms of business and corporate structures in Hong Kong. Limited companies, unincorporated businesses and different types of business collaboration are discussed under separate headings.
- Chapter 4 concerns the M&A regime in Hong Kong, with a focus on share transfers involving private companies. Relevant legal issues are explained, followed by an overview of the due diligence exercise and the core documentation involved in the sale of a company or business.
- Chapter 5 addresses foreign investment in Hong Kong and considers two specific sectors which, by way of exception to the city’s free market economy policy, are subject to certain restrictions on investment.
- Focusing on corporate insolvency, Chapter 6 summarises winding-up procedures under Hong Kong law, as well as available statutory methods for effecting a corporate rescue. It concludes by examining Hong Kong’s cross-border insolvency regime.
- Chapter 7 discusses legal aspects of employment, industrial relations, and work health and safety in Hong Kong, including, among other things, the law relating to employment rights and contracts, as well as the termination of employment.
- Chapter 8 introduces Hong Kong’s taxation regime. To this end, the chapter first outlines different types of tax, before briefly addressing tax disputes and anti-avoidance under Hong Kong tax law.
- Intellectual property is the subject of Chapter 9, which provides a general overview of the scope of protection of the main categories of intellectual property rights in Hong Kong.

- Chapter 10 provides a general outline of the law relating to Hong Kong's financial landscape, covering the legal and regulatory framework for bank lending and the taking of security, as well as legal aspects of the city's debt and equity capital markets.
- Chapter 11 contains a summary of privacy laws and data protection in Hong Kong. A description of the regulatory framework and the data protection principles is accompanied by discussions relating to third-party processing, direct marketing and cross-border transfers of data. The chapter concludes by mentioning a recent proposal for statutory changes.
- Chapter 12, on competition law in Hong Kong, provides a general overview of the competition law regime, followed by an explanation of the First and Second Conduct Rules and the merger rule.
- To conclude the walkthrough of Hong Kong's legal environment for business, Chapter 13 deals with dispute resolution, with separate sections to address litigation before the Hong Kong courts, Hong Kong seated arbitration and mediation.

Chapter 2: Business environment

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This chapter explains the business environment in Hong Kong. Hong Kong has a market-orientated and free economy. Due to its unique history, combined with its status as a SAR of the PRC, Hong Kong has established itself as a respected international financial centre that also serves as a key gateway to the rapidly developing mainland China market. With well-established legal and financial infrastructures in place and a favourable tax regime, Hong Kong is considered a prime location for businesses to thrive.

2.1 Hong Kong's free economy

2.1.1 Overview

Hong Kong has long been recognised as one of the freest and most competitive economies in the world. Hong Kong's economy was consistently rated the freest in the world from 1995 to 2019 on the Index of Economic Freedom published by the Heritage Foundation.[1]

1 See www.heritage.org/index/country/hongkong?version=562 accessed 13 May 2020.

Hong Kong is ranked the second-most competitive economy out of 63 economies according to the *World Competitive Yearbook 2019*, published by the International Institute for Management Development.[2]

2.1.2 Free flow of capital, free port and free trade

The freedom and openness of Hong Kong's economy is supported by the adoption of positive non-interventionist economic policies as enshrined under the Basic Law of Hong Kong. In particular, Hong Kong has no foreign exchange control policies. A policy of free trade is adopted with safeguards over the free movement of goods, intangible assets and capital. Hong Kong also maintains its status as a free port. There are no trade barriers or tariffs on the import and export of goods. Hong Kong's free economy provides room and flexibility for businesses to prosper.

2.2 Gateway to mainland China

Businesses in Hong Kong are also able to access trade and investment opportunities in mainland China, taking advantage of Hong Kong's geographical location and favourable policy treatment by the central government.

2.2.1 CEPA

Hong Kong businesses enjoy preferential treatment on the trading of goods, provision of services and investment in the PRC under the mainland and Hong Kong Closer Economic Partnership Arrangement (CEPA).

Under CEPA, all goods of Hong Kong origin enjoy a zero tariff upon being imported into mainland China.

With effect from 1 June 2020, the entry of Hong Kong service providers and professionals into the mainland China market was further liberalised pursuant to an amendment to CEPA. This amendment provides an opportunity for Hong Kong service providers to further expand their business presence in mainland China.

Hong Kong investors that fulfil the requirements under CEPA also enjoy preferential treatment regarding investment in non-service sectors, as well as further investment protection.

2.2.2 Connectivity of financial and capital markets

The Hong Kong and mainland China capital markets enjoy a high degree of connectivity, with large volumes of trades. This connectivity is enshrined in various policy initiatives, principally the Shanghai-Hong Kong Stock Connect, the Shenzhen-Hong Kong Stock Connect and the Bond Connect. These initiatives allow international investors to tap into the mainland China stock and bond markets by trading and clearing through the Stock Exchange of Hong Kong Limited (HKEX).

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2 See www.imd.org/wcc/world-competitiveness-center-rankings/world-competitiveness-ranking-2019 accessed 13 May 2020.

In addition, Hong Kong is a significant offshore RMB hub. Most of the world's RMB payment transactions are processed through Hong Kong.[3] Hong Kong had the highest daily turnover of RMB foreign exchange and interest rate derivatives among offshore markets as of April 2019.[4]

2.2.3 National initiatives

With the implementation of the Outline Development Plan for the Guangdong-Hong Kong-Macao Greater Bay Area, the central government is committed to providing support to strengthen Hong Kong's status as an international financial, transportation and trade centre, global offshore RMB hub, and international asset management and risk management centre. Hong Kong also plays a significant role in the Belt and Road Initiative. Hong Kong's participation in the national initiatives will provide more opportunities for cross-border business cooperation.

2.3 International outlook

Hong Kong is a highly internationalised trade and financial hub that allows businesses to capture opportunities worldwide.

Hong Kong has established trade and economic relationships with developed economies around the world. Hong Kong has entered into free trade agreements with, among others, the ASEAN, Member States of the European Free Trade Association, Australia and New Zealand. It has also entered into investment promotion and protection agreements, and comprehensive double taxation agreements with multiple jurisdictions around the world.

Hong Kong is also a popular destination for foreign investment, ranking third and fourth in terms of FDI inflow and outflow, respectively, according to the UN Conference on Trade and Development (UNCTAD) *World Investment Report 2019*.[5]

Hong Kong is also a well-recognised international financial centre, ranking third in the world according to the Global Financial Centres Index.[6] It also has active participation in multiple regional and international financial organisations, including the WTO, Asia-Pacific Economic Cooperation, Pacific Economic Cooperation Council, Asian Infrastructure Investment Bank and Asian Development Bank.

2.4 Well-established legal and financial infrastructures

2.4.1 Legal system

Hong Kong maintains a separate legal system from mainland China. Hong Kong adopts the common law system and has an independent judiciary with the power of final adjudication. Since the handover

3 According to Brand Hong Kong's International Financial Centre Fact Sheet, as of 2019 about 75 per cent of the global offshore RMB payments are processed via Hong Kong: see www.brandhk.gov.hk/uploads/brandhk/files/factsheets/Hong_Kong_Themes/International%20financial%20centre_E_April%202020.pdf accessed 29 May 2020.

4 According to the Triennial Central Bank Survey of Foreign Exchange and Over-the-Counter Derivatives Markets in 2019, conducted by the Bank for International Settlements.

5 See https://unctad.org/en/PublicationsLibrary/wir2019_en.pdf accessed 13 May 2020.

6 See the Global Financial Centres Index 26 published in September 2019 www.longfinance.net/programmes/financial-centre-futures/global-financial-centres-index/gfci-26-explore-data/gfci-26-rank accessed 13 May 2020.

in 1997, Hong Kong has developed its own jurisprudence under the framework of the Basic Law in accordance with common law principles and with the benefit of international insights brought by the eminent judges from other common law jurisdictions appointed to Hong Kong's highest court. The mature and well-developed legal system in Hong Kong, which contains strong safeguards for private property rights and enjoys the support of a deep pool of local and foreign legal talent, serves as the backbone for Hong Kong's success as an international financial centre.

Hong Kong has developed its reputation as an international dispute resolution centre, with respected mediation and arbitration services. With the Arbitration Ordinance (Cap 609) providing a legal framework and institutions such as the Hong Kong International Arbitration Centre (HKIAC) in place, businesses have the alternative to resolve commercial disputes in a speedy and confidential manner via arbitration in Hong Kong. For an overview of Hong Kong's dispute resolution framework, see Chapter 13 (Dispute resolution).

2.4.2 Financial infrastructure

Hong Kong has a vibrant financial market. HKEX is one of the largest and most respected stock exchanges in the world. HKEX has been a popular destination for fundraising by businesses. The Hong Kong IPO market ranked first globally in terms of IPO funds raised in 2019. With new changes to the Listing Rules to allow for the listing of 'new economy' companies with a weighted voting rights structure and pre-revenue biotechnology companies, as well as secondary listing, the Hong Kong stock market is expected to become an even more diverse channel for fundraising.

The Linked Exchange Rate System pegs the Hong Kong dollar to the US dollar and provides stability to Hong Kong's monetary and financial market.

The financial sector prospers in Hong Kong with the support of a talented local workforce, with over 6.8 per cent of the population employed in the sector directly, contributing 19.7 per cent of Hong Kong's GDP as of 2018.[7]

2.5 Favourable tax regime

Hong Kong has adopted a territorial-based profits tax regime. Profits with a source in Hong Kong are taxable. With effect from the year of assessment 2018/19, a two-tiered profits tax rate was introduced. Profits tax rates for corporations and unincorporated businesses are 8.25 per cent and 7.5 per cent, respectively, on assessable profits up to HK$2m, and 16.5 per cent and 15 per cent, respectively, on any part of assessable profits exceeding HK$2m.

There is no CGT or WHT on dividends in Hong Kong.

7 See www.brandhk.gov.hk/uploads/brandhk/files/factsheets/Hong_Kong_Themes/International%20financial%20centre_E_April%202020.pdf accessed 29 May 2020.

Chapter 3: Business and corporate structures

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This chapter highlights the common forms of business and corporate structures in Hong Kong.[8]

The most common form of business structure in Hong Kong is the limited company. Other forms of structure, such as limited partnerships, are also available, but are less commonly used. Non-entity-based structures, such as unincorporated businesses and other forms of business collaboration without separate legal personality, are also possible.

3.1 Limited company

The characteristics of and requirements regarding a limited company are set out under the Companies Ordinance (Cap 622) (CO 622).

3.1.1 Incorporating a limited company

A common way for businesses to establish a local presence in Hong Kong is by incorporating a Hong Kong limited company. Hong Kong limited companies have the following features and requirements:

- Hong Kong companies can structure their capital in a highly flexible manner. There is no requirement as to the size of the issued capital or the nominal value of the shares. Share capital may be denominated in a currency other than Hong Kong dollars.
- The constitutional document of a Hong Kong company is its articles of association, which prescribes the internal regulation of the company. The articles of association can be tailored, but must include certain mandatory articles that set out the company's name, the liability of its members, initial share capital and shareholders in accordance with CO 622. For a private company, the articles of association must also restrict the transfer of shares in the company, limit the number of its shareholders to 50 and prohibit invitations to the public to subscribe for shares or debentures in it. The articles of association must be filed with the Companies Registry and will be a matter of public record.
- A Hong Kong company must have at least one shareholder. Shareholders of Hong Kong companies may be individuals or corporations. There is no requirement for the shareholder to be a Hong Kong identity card holder or be resident in Hong Kong. Hong Kong companies must keep an up-to-date register of members and significant controllers (ie, people with significant influence or control over the company, including indirect stakeholders). These registers are not a matter of public record.

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8 For the avoidance of doubt, it is noted that the forms and structures discussed in this chapter are not exhaustive.

- A Hong Kong company must have at least one director. A body corporate may be appointed as a director, but at least one director must be a natural person. There is no nationality or residency restriction on directors. The company must keep an up-to-date register of directors.
- A Hong Kong company must appoint a company secretary. The company secretary may be an individual ordinarily resident in Hong Kong or a body corporate (eg, a company secretarial service provider) having its registered office or a place of business in Hong Kong. A director may also be the company secretary except where the company has only one director. The company must keep an up-to-date register of company secretaries.
- The company must have a registered office to which any official notices or communications may be sent. The registered office need not be the address from which the company operates. It may be an address provided by a service provider.
- The company would need to appoint a Hong Kong qualified independent auditor.

The process of incorporating a limited company in Hong Kong is generally straightforward. The company must file with the Companies Registry the signed articles of association and an Incorporation Form, together with a registration fee. The incorporation occurs once the Companies Registrar has issued a certificate of incorporation and thereafter the company may commence business. Every company in Hong Kong must also obtain a Business Registration Certificate, even if it is not actually carrying on business in Hong Kong. The Business Registration Certificate must be renewed either annually or every three years, at the election of the company. Depending on the nature of the business, there may be a requirement for additional authorisations to be obtained.

3.1.2 Acquiring and activating a shelf company

As an alternative to incorporating a new company, acquiring and activating a shelf company can offer a faster and more convenient option for businesses. A shelf company can be purchased from service providers in Hong Kong. It can be activated by effecting changes in shareholders, directors and company secretaries, and commencing business activities. The Companies Registry and the Business Registration Office should then be notified of the changes.

3.1.3 Branch office and registered non-Hong Kong company

A foreign business may also consider establishing a branch office in Hong Kong. A branch office is not a legal entity and has no existence separate from the foreign business it represents. The liabilities of a branch office are accordingly borne by its foreign parent company. A branch office will also need to apply for business registration. Where a foreign company intends to set up a branch office in Hong Kong, specific legal advice should be sought as to whether it amounts to a 'place of business' within the meaning of Hong Kong legislation.

A foreign company (a company incorporated outside Hong Kong) establishing a place of business in Hong Kong is required to be registered as a non-Hong Kong company under Part 16 of CO 622.

An Application for Registration of Registered Non-Hong Kong Company should be submitted to the Companies Registry. There must be an authorised representative appointed to accept, on behalf of the company, service of any process or notices. The authorised representative must be a natural person resident in Hong Kong, solicitor corporation, corporate practice within the meaning of section 2 of the Professional Accountants Ordinance, or firm of solicitors or professional accountants.

3.1.4 Public company and listed company

A public company is a company that has no restriction on transfer of shares, no limit on the number of shareholders or no prohibition against a public subscription of shares. A public company is subject to additional reporting requirements under CO 622.

A company that fulfils the relevant requirements under the Main Board Listing Rules or GEM Listing Rules can apply to be listed on the Main Board or the GEM board (as applicable) of HKEX. The shares of a company listed on HKEX are freely transferable. Listed companies are subject to continuous obligations on financial reporting and disclosure, and are required to maintain high standards of corporate governance under the Listing Rules. The listing of companies and the activities of listed companies are supervised and regulated by HKEX and the Securities and Futures Commission (SFC).

3.2 Unincorporated businesses

Sole proprietorships and partnerships are common forms of unincorporated business. Neither of these are a separate legal entity. With the exception of a limited partner in a limited partnership, the sole proprietor and partners bear unlimited liability.

The formation and operations of partnership and limited partnership are governed under the Partnership Ordinance (Cap 38) and the Limited Partnership Ordinance (Cap 37).

It is possible to convert an existing unincorporated business into a limited company. This can be done by incorporating a limited company and transferring the business or assets of the business to the limited company. For any business transfer within the scope of the Transfer of Business (Protection of Creditors) Ordinance (Cap 49) (TB(PC)O), the transferee will automatically assume all of the debts and obligations arising out of the carrying on of the business by the transferor unless a notice is issued and advertised in the prescribed form and manner pursuant to the TB(PC)O or unless one of a limited number of alternative defences under the TB(PC)O is available.

3.3 Forms of business collaboration

3.3.1 Commercial cooperation

Businesses may use commercial contracts as the basis of their collaboration. This provides a high degree of flexibility regarding the ownership of underlying assets or rights and allows for bespoke commercial arrangements.

3.3.2 Joint ventures

Joint ventures allow multiple parties to pursue a common business objective. The structure of a joint venture is highly flexible and may take different forms, including incorporated business (ie, based on ownership interests in a joint venture entity), unincorporated business (eg, partnership or limited partnership) or by contractual arrangement.

3.3.3 Acquisitions

Acquisition may be conducted in the form of:

- acquiring a controlling interest in or the entire share capital of an established company; or
- purchase of the business or assets of the company.

The exact structure to be adopted for each acquisition depends on the commercial, legal and tax considerations of the parties involved. If the acquisition is done by way of purchase of business or assets of the company, the operation of the TB(PC)O as discussed above needs to be considered.

For an overview of the takeovers regime in Hong Kong, see Chapter 4 below.

3.3.4 Minority/venture investment

This is typically used when a venture investor acquires a minority stake in the early stage of a startup company. The venture investor provides growth capital and know-how on the development of the business in exchange for access to a unique technology or product. Minority investment provides the venture investor with the advantage of being able to engage in risky ventures with more limited exposure. This is especially common in the innovation and technology industry.

Chapter 4: Takeovers (friendly M&A)

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4.1 Introduction

M&A in Hong Kong is typically structured through the transfer of the target company's shares, or the target company's assets, to the purchaser. Generally, share transfers tend to be more common than asset transfers in Hong Kong. Various factors are relevant in determining which structure is preferable in a particular case. For example:

- a share transfer may not be appropriate if the purchaser only wants to purchase a small or specific part of the target company's business;
- in an asset transfer, the purchaser can choose to avoid the assumption of undisclosed or contingent liabilities; and

- a share transfer may be more appropriate if the target company's assets are not transferable, for example, non-transferable government licences or non-assignable agreements with third parties, subject, of course, to any change of control provisions.

The detailed discussion in this chapter is mostly focused on share transfers involving private companies incorporated in Hong Kong with limited liability. For takeovers and mergers involving companies listed in Hong Kong, the Code on Takeovers and Mergers and the Rules Governing the Listing of Securities on HKEX are applicable. An examination of such rules is, however, beyond the scope of this chapter.

4.2 Hong Kong company law

Company law in Hong Kong has developed through the interaction and interdependence of case law and statutory law.

The Companies Ordinance sets out the general rules and regulations governing Hong Kong companies (with certain provisions applying to overseas companies having a place of business in Hong Kong) and contains a number of specific provisions relating to matters that may impact upon M&A and how they can be structured, including, among other things, the following:

- the giving of financial assistance by a company for the purchase of its own shares is subject to certain restrictions and procedural requirements, including a solvency test, and board and shareholder approval (albeit that there is also a *de minimis* threshold in lieu of obtaining shareholder approval);
- a court-free procedure for two categories of intra-group amalgamations: vertical amalgamations (between a holding company with one or more of its wholly owned subsidiaries) and horizontal amalgamations (between two or more wholly owned subsidiaries of the same company); and
- restrictions on the amount that can be distributed by way of a dividend.

4.3 Other common legal issues

4.3.1 Sectoral regulation

In Hong Kong, consent from the relevant regulatory body is required for a change of ownership of companies operating in certain sectors of the economy, including radio and television broadcasting, banking, insurance and financial services.

4.3.2 Foreign exchange and investment restrictions

Hong Kong currently does not impose controls on the inflow and outflow of foreign exchange, or any restrictions on investment or repatriation of capital or remittance of profits or dividends to or from a Hong Kong company.

Unless one of the few regulated industries is involved, there are generally no approval requirements or restrictions on foreign ownership of Hong Kong companies.

4.3.3 Consent by third parties

In many M&As, consents, approvals or waivers from third parties are required under the articles of association of the target company or shareholders' agreements relating to the target company. For example, in an acquisition of some, but not all, of the shares of a company, the consent of the other shareholders may be required to waive pre-emptive rights or other restrictions on transfer under the articles of association of the target company. Existing agreements of the target company with creditors, landlords, debenture holders, mortgagees and other contracting parties may also require consent by these parties in the event of a change in control.

4.3.4 Stamp duty

Stamp duty is charged on the sale of Hong Kong stock. Currently, the rate is calculated at 0.2 per cent of the higher amount of consideration paid and the value of shares being transferred. It is normally paid in equal proportions by the seller and the purchaser, although there is no hard-and-fast rule. Relief is available (subject to certain conditions) in respect of intra-group share transfers between associated companies (90 per cent ownership being the applicable threshold).

4.4 Typical documentation

Core documentation involved in a sale and purchase of a company or a business in Hong Kong is similar to that used in many international jurisdictions and typically includes the following:

- a confidentiality letter in which the parties undertake to keep confidential the actual transaction and any information they may obtain during the due diligence process; in some cases, it may include a provision for exclusive negotiations for a particular period so that the purchaser knows that there will be no dual negotiations or auction type process;
- a letter of intent, a memorandum of understanding, a term sheet or heads of terms setting out the key commercial terms; normally, this document would not be expressed to be legally binding except for certain specific provisions, such as those relating to confidentiality, exclusivity and liability for costs in the event of an unsuccessful transaction;
- a due diligence questionnaire and report in relation to the business or company;
- a sale and purchase agreement that specifies the obligations and liabilities of each party in relation to the sale. This normally includes detailed representations and warranties regarding the business or company; in a share transfer, all the company's obligations and liabilities remain in the company, whereas in a business sale, subject to the Transfer of Businesses (Protection of Creditors) Ordinance, the purchaser will normally be able to pick and choose which assets it wishes to purchase and which liabilities it wishes to acquire;
- a disclosure letter in which the seller makes disclosures against the representations and warranties in the sale and purchase agreement; and
- instrument of transfer, and bought and sold notes if these are shares in a Hong Kong company.

4.5 Due diligence

In any M&A, in addition to financial and business due diligence, legal due diligence in some form is normally undertaken by the purchaser. Reports on title are sometimes prepared in relation to properties owned by the target company. Other items commonly investigated in a legal due diligence include the statutory books, major contracts, plant and machinery leases, service agreements, loan details, licences/permits and particulars of litigation.

The due diligence process usually involves the following steps: a questionnaire is submitted to the target company, teams of lawyers review documents and a legal due diligence report is prepared. The report may be comprehensive or simply detail disclosures made against warranties given in the contractual documentation. In answering due diligence enquiries, the seller must be careful to avoid any misrepresentation that may subsequently be relied upon by the purchaser to rescind the agreement and claim damages.

As part of the legal due diligence, searches of publicly available information may be made at the relevant government authorities (eg, the Hong Kong Companies Registry, the Hong Kong Land Registry, the Trade Marks Registry, the Official Receiver's Office and the Hong Kong Courts in respect of litigation and winding-up proceedings) to serve as an independent check against the information provided by the seller.

4.6 Sale and purchase agreement

The terms and conditions contained in a sale and purchase agreement will depend on the commercial negotiations of the parties and the circumstances of each particular case. Some of the common provisions typically found in sale and purchase agreements are further discussed below.

4.6.1 Parties

The parties to a sale and purchase agreement would normally be seller(s) (which would be the shareholder(s) of the target company selling the shares in a share transfer, or the company selling the assets in an asset transfer) and the purchaser. Depending on the circumstances, a guarantor may also be made a party to the agreement to guarantee the obligations of the seller (eg, under warranties) or the purchaser (eg, to pay part of the consideration in instalments after completion).

4.6.2 Conditions precedent

Where it is necessary to obtain regulatory and/or other consents or approvals before completion or for the purchaser to complete further due diligence (eg, an audit) after signing the agreement, the sale and purchase agreement will be made conditional upon the fulfilment or (if feasible) waiver of such conditions precedent. In this case, the signing of the agreement and completion of the transaction will not be simultaneous. There will be a period of time between signing and completion during which the conditions precedent are to be satisfied. This would normally give rise to questions, such as who will be responsible for the fulfilment of which conditions, the conduct of the affairs of the target company during the period between signing and completion, and the allocation of risk regarding any adverse changes in the business of the target company during such period. These questions should be addressed in the sale and purchase agreement to avoid any doubt.

4.6.3 Consideration

The sale and purchase agreement will usually stipulate the amount of the consideration, the form it will take and the timing of the payment. The consideration will usually take the form of cash, shares or loan notes, or a combination.

4.6.4 Representations and warranties

The common law rule of *caveat emptor* (or 'purchaser beware') still applies to the acquisition of shares or assets in private companies in Hong Kong. In respect of a share transfer, there is no statutory protection by way of implied terms in favour of the purchaser. A purchaser will normally require comprehensive representations and warranties to be provided by the seller in the sale and purchase agreement, covering the seller's capacity and its title to the shares in the target company (and ownership of any shareholder's loan to be assigned), the target company's financial statements and related matters, business/trading, contracts, taxation, corporate matters, title to assets, land and properties, plant and equipment, insurance, intellectual property rights, goodwill, employment matters, environmental matters, banking and finance, regulatory and tax compliance, disputes and litigation, and the accuracy and completeness of information provided by the seller.

4.6.5 Restrictive covenants

The purchaser will usually seek to include in the sale and purchase agreement provisions that restrict the competitive freedom of the seller, such as non-compete covenants, non-solicitation clauses in relation to the target company's customers, suppliers or employees, confidentiality provisions prohibiting the seller from disclosing or using any confidential information about the target company and its customers, and provisions restricting the seller from using the same or similar name as the target company. In common law, restrictive covenants are *prima facie* unenforceable as they restrain trade and are therefore contrary to public policy. However, the courts are willing to uphold restrictive covenants that they consider to be reasonable in order to protect the legitimate interest of a purchaser, for example, where there are sensible limitations in broadly three typical aspects: the geographical area restricted, the duration of the restraint and the business activities prohibited.

4.6.7 Completion

The sale and purchase agreement will usually provide that completion takes place by the delivery of a properly executed instrument of transfer and the related sold note, the original share certificate(s), the books and records and other documents of the target company by the seller in exchange for the payment of consideration by the purchaser.

The seller will procure a board meeting of the target company to be held at completion for approving the following matters:

- (subject to due stamping, if required) the registration of the purchaser or its nominees as members of the target company in its statutory records and the issuance of a new share certificate to the purchaser or its nominees;
- the appointment of the purchaser's nominees as directors and officers;
- the acceptance of the resignations of the existing directors and other officers; and
- the alterations to the authorised signatories of the target company's bank accounts

After completion, the purchaser will attend to the stamping of the instruments of transfer and the bought and sold notes, after which the transfer can be reflected in the register of members, and such registration is determinative of legal title. The purchaser should also ensure that the register of directors of the target company is updated to reflect all changes pursuant to the sale and purchase agreement, and that all necessary filing forms – for example, those relevant to the change of directors and company secretary – are submitted to the Companies Registry by the prescribed deadlines.

Chapter 5: Foreign Investment

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5.1 Overview of Hong Kong's business and investment environment

As briefly indicated in Chapter 1, over the past decade Hong Kong has consistently been recognised as having one of the most business-friendly environments in the world. Unsurprisingly, the city's business-friendly environment also appeals to investors. Among enterprise groups with existing direct investment in Hong Kong, 71 per cent considered the overall investment environment of Hong Kong to be favourable in early 2019. In the information and communications sector, this figure was 85 per cent, while as many as 92 per cent of enterprises in the banking sector had a favourable view of the city's investment environment.

The continuing attractiveness of Hong Kong as a host state for investment is likewise reflected in recent figures regarding FDI. According to the UNCTAD *World Investment Report 2019*, Hong Kong's FDI inflows amounted to approximately US$115,662m in 2018, while for the same year the amount of outward FDI was US$85,162m (with mainland China being the most important destination for outflow).

A snapshot of Hong Kong's dispute resolution framework for commercial litigation, arbitration and mediation is provided in Chapter 13. For present purposes, it is worth noting that the PRC and the Permanent Court of Arbitration signed a host country agreement and a related memorandum of administrative arrangements in January 2019. The agreement and memorandum concern the conduct of Permanent Court of Arbitration-administered arbitration proceedings in Hong Kong, which in turn has further enhanced the city's status as an international arbitration centre, including for investor-state arbitration.

The following section considers, at a high level, the foreign investment regulatory landscape in Hong Kong. An overview of Hong Kong's business environment more generally is contained in Chapter 2.

5.2 Restrictions on foreign investment

The Hong Kong government has always upheld a free market economy policy: Article 105 of the Basic Law of Hong Kong stipulates that the ownership of enterprises and investment from outside Hong Kong must be protected by law.

There are no general restrictions on the foreign ownership of companies in Hong Kong, except in respect of certain restrictions on voting control by non-Hong Kong residents and corporations in the telecommunications sector, as set out below.

5.2.1 Sound broadcasting

Under the Telecommunications Ordinance (Cap 106), an 'unqualified person' (ie, a person that is not ordinarily resident in Hong Kong and has not at any time been resident for a continuous period of seven years or more, or a company that is not ordinarily resident in Hong Kong) shall not have an aggregate of voting shares (to or in which the unqualified person directly or indirectly has any right, title or interest) of more than 49 per cent of the total number of voting shares in a sound broadcasting licensee.

5.2.2 Domestic free television programme service

Currently, under the Broadcasting Ordinance (Cap 562), an 'unqualified voting controller' (ie, a person that is not ordinarily resident in Hong Kong and has not at any time been resident for a continuous period of seven years or more, or a company that is not ordinarily resident in Hong Kong) of a licensee of a domestic free television programme service licence must not, without the prior approval of the Communications Authority, hold, acquire, exercise, cause or permit to be exercised: (1) two per cent or more but less than six per cent; (2) six per cent or more but not more than ten per cent; or (3) more than ten per cent in the aggregate, of the total voting control[9] of such licensee (the unqualified voting controller restriction).

Where the total voting control exercised by unqualified voting controllers would exceed, in aggregate, 49 per cent of the total voting control exercised in a poll by both qualified and unqualified voting controllers, the votes cast on the poll by unqualified voting controllers must, for the purpose of determining the question or matter, be reduced in accordance with a formula set out in the Broadcasting Ordinance.

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9 Voting control means the control of or the ability to control, whether directly or indirectly, the exercise of the right to vote attaching to one or more voting shares of a licensee: (1) by the exercise of a right, where such exercise confers the ability to exercise a right to vote or to control the exercise of a right to vote; (2) by an entitlement to exercise such a right to vote; (3) under a duty or obligation; (4) through a nominee; (5) through or by means of a trust, agreement or arrangement, understanding or practice, whether or not the trust, agreement or arrangement, understanding or practice has legal or equitable force or is based on legal or equitable rights; or (6) as a chargor of voting shares of a licensee unless the chargee of the voting shares or the nominee of the chargee has given notice in writing to the chargor under the charge of an intention to exercise the right to vote attaching to such voting shares.

Further, an 'associate' (regardless of whether the associate is a qualified or an unqualified voting controller) of an unqualified voting controller is restricted from holding or acquiring voting control of the voting shares of a licensee if it appears that the purpose of holding or acquiring is to avoid the unqualified voting controller restriction or other restriction imposed on the unqualified voting controller.

Chapter 6: Restructuring and insolvency

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This chapter explains the options available under Hong Kong law to deal with financial distress. In essence, the two major options are liquidation and restructuring. The various types of liquidation and restructuring techniques are explained below.

In addition, as most businesses have international elements, how Hong Kong law facilitates cross-border insolvency and restructuring will also be explained.

6.1 Legal framework

Hong Kong insolvency law draws a distinction between corporate insolvency and personal bankruptcy.

Corporate insolvency law is mainly governed by the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap 32) (CWUMPO), whereas personal bankruptcy law is mainly governed by the Bankruptcy Ordinance (Cap 6).

Further, as Hong Kong's legal system is shaped by a unique constitutional framework known as 'one country, two systems', Hong Kong law maintains the use of common law and rules of equity.

The focus of this chapter is on corporate insolvency.

6.2 Liquidation

CWUMPO provides for several different procedures to wind up an insolvent company. The winding-up procedure can be invoked on either a 'compulsory' or a 'voluntary' basis:

- compulsory winding-up: the winding-up of a company pursuant to the order of the court; or
- creditors' voluntary winding-up: the winding-up of an insolvent company without a court order.

Upon a winding-up, the company will be managed and controlled by the liquidator. The liquidator will be under a statutory duty to gather and realise the company's assets in order to make a distribution to creditors in accordance with the priority set out in CWUMPO.

Upon completion of the winding-up process, the company will be dissolved.

6.2.1 Compulsory winding-up

A company can be wound up by the court on six principal grounds, which are set out in section 177 of the CWUMPO:

- the company has, by special resolution, resolved that the company be wound up by the court;
- the company does not commence its business within a year from its incorporation, or suspends its business for a whole year;
- the company has no members;
- the company is unable to pay its debts;
- the event, if any, occurs on the occurrence of which the articles provide that the company is to be dissolved; or
- the court is of the opinion that it is just and equitable that the company should be wound up.

Of the six principal grounds, the two most commonly used grounds are that the company is unable to pay its debts and that it is just and equitable for the company to be wound up.

6.2.2 Creditors' voluntary winding-up

Creditors' voluntary winding-up occurs when:

- a company in a general meeting passes a special resolution for voluntary winding-up in the absence of a certificate of solvency;
- a company is not solvent in the opinion of its directors and the directors resolve to deliver a winding-up statement to the Registrar of Companies; or
- the liquidation of the company commences as a solvent members' voluntary liquidation, but the liquidator becomes of the opinion that the company is insolvent.

6.3 Restructuring

There are two statutory methods to effect a corporate rescue.

The first is the use of provisional liquidators. In the case of a compulsory winding-up, the court may appoint a provisional liquidator after a winding-up petition is presented (before any winding-up order is made). Upon such an appointment, further proceedings against the company would be barred; in essence an automatic stay. This feature has led to a practice in the early 21st century whereby provisional liquidators were appointed pending efforts to effect a corporate rescue.

Such a practice was restricted in 2006, when the Court of Appeal in *Re Legend International Resorts Ltd* [2006] 2 HKLRD 192 held that the appointment of a provisional liquidator must be for the purpose of winding up the company. But it has recently been clarified that, as long as provisional liquidators were appointed on conventional grounds (eg, asset preservation and investigation in order to wind up the company), they can be used to effect a corporate rescue (*Re China Solar Energy Holdings Ltd (No 2)* [2018] 2 HKLRD 338).

The second method is the scheme of arrangement procedure under CO 622. The scheme procedure provides that if: (1) a debt restructuring arrangement is reached between the company and a requisite majority of creditors (ie, a majority in number representing at least 75 per cent in value voting in favour of the scheme); and (2) the court sanctions the arrangement, it will be binding on all, including dissenting, creditors. This statutory mechanism offers a helpful alternative when a unanimous work-out cannot be achieved.

The scheme procedure is, in practice, the most popular restructuring technique and it is often coupled with the use of provisional liquidators.

6.4 International insolvency

Hong Kong does not have any statutory cross-border insolvency provisions. The Hong Kong court relies only on common law to manage cross-border insolvency cases.

Under the common law cross-border insolvency regime, the Hong Kong court ordinarily recognises and assists a liquidator appointed in the country of the company's incorporation where there are no public policy issues that would prevent recognition. This includes recognising a foreign liquidator appointed voluntarily. It is possible that the Hong Kong court will recognise an insolvency office holder appointed in a jurisdiction other than the company's place of incorporation, though this point has yet to be formally decided.

Hong Kong proceedings may be required to establish the foreign insolvency officer's authority to deal with assets in Hong Kong. Recognition of a foreign insolvency officeholder's position will, in itself, confer standing on the officer to represent the foreign company in the Hong Kong courts. The insolvency office-holder may bring proceedings in the Hong Kong courts in the name of the foreign company and generally administer the assets of the foreign company situated in Hong Kong.

However, the Hong Kong courts' power to assist a foreign insolvency office-holder is limited by the extent to which the type of order sought is available under the Hong Kong insolvency regime and common law or equitable principles: hence, the court has recently refused to grant the application of administrators appointed in England for an order restraining the sale of property subject to security, on the basis that no such statutory moratorium or equivalent power exists in Hong Kong (*Joint Administrators of African Minerals v Madison Pacific Trust* [2015] 4 HKC 215).

The common law recognition regime is often used to facilitate cross-border restructuring in Hong Kong. A typical example is the recognition in Hong Kong of offshore soft-touch provisional liquidators in respect of offshore-incorporated companies that are listed in Hong Kong. Upon recognition, the offshore provisional liquidators are granted powers to pursue restructuring in Hong Kong, typically by means of a scheme of arrangement.

Insolvency protocols have been used in cross-border insolvencies between insolvency representatives appointed by the Hong Kong court and the insolvency representatives in other jurisdictions to harmonise the parallel insolvency proceedings. The Hong Kong courts have power to permit Hong Kong insolvency officeholders to enter into such protocols with their counterparts.

Chapter 7: Employment, industrial relations, and work health and safety

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7.1 Basic employment rights

The main legislation in Hong Kong prescribing the minimum rights, benefits and protections for employers and employees are the Employment Ordinance, Minimum Wage Ordinance, Mandatory Provident Fund Schemes Ordinance and Employees' Compensation Ordinance.

Such minimum rights and protection granted to all employees include (but are not limited to) the payment of wages, restrictions on wage deductions, the granting of statutory holidays, statutory minimum wage and coverage by mandatory employees' compensation insurance taken out by employers for work-related injuries under the Employees' Compensation Ordinance (such insurance should not be confused with medical benefits, which employers are not statutorily obliged to provide). All employees between the ages of 18 and 65, subject to prescribed relevant income levels and limited exemptions, must be enrolled in a recognised mandatory provident fund scheme by their employers, who in turn must make regular contributions on behalf of their employees. Whether there is an employment relationship is entirely a question of fact. An employment relationship will depend on the substance of the relationship, instead of mere formality (eg, the existence or absence of an employment contract or independent contractor agreement).

The Mandatory Provident Fund Schemes Ordinance requires both the employer and employee to contribute five per cent of the employee's salary into a mandatory provident fund. Currently, the minimum relevant income is fixed at HK$7,100 (approximately US$910). This means that if the monthly relevant income of an employee is less than HK$7,100, the employee will not be required to make the employee's contribution, but his employer remains obliged to make the employer's contribution. The current maximum level of mandatory contribution required is HK$1,500 (approximately US$190) paid each month by both the employer and the employee. The employer and/or the employee may make additional voluntary contributions to the scheme if they wish.

All employees (including prospective employees) are also protected from discrimination. Hong Kong has four discrimination ordinances (Sex Discrimination Ordinance, Disability Discrimination Ordinance, Race Discrimination Ordinance and Family Status Discrimination Ordinance) which prohibit discrimination on the grounds of sex, marital status, pregnancy, disability, race and family status in certain fields, including employment. Discrimination on the basis of trade union membership also is protected by the Employment Ordinance. Although there is currently no legislative prohibition of discrimination on the ground of age in Hong Kong, the Labour Department of Hong Kong has issued practical guidelines for employers on eliminating age discrimination in employment. Although these guidelines are not backed up by legislation, they set forth best practice, and employers and employment agencies are encouraged to follow them on a voluntary basis.

Each of the discrimination ordinances provides that it is unlawful for an employer to discriminate against a job applicant on any of the relevant prohibited grounds:

- in the arrangements the employer makes for determining who should be offered employment;
- in the terms of employment offered to a job applicant; and
- by refusing or deliberately omitting to offer employment to a job applicant.

Furthermore, each of the discrimination ordinances provides that it is unlawful to publish or cause to be published an advertisement that indicates (or might reasonably be understood to indicate) an intention to discriminate on the aforementioned grounds. Employers, therefore, should not advertise job vacancies suggesting that applicants must be, for example, of a particular gender or marital status, unless such discrimination would not be unlawful under the applicable ordinance. For example, under the DDO, it would not be unlawful for an employer to refuse to employ an applicant on the ground of his or her disability if being a person without a disability is a 'genuine occupational requirement' or where the applicant's disability would prevent him or her from performing the 'inherent requirements' of the position; although, the employer and must consider if there could be reasonable accommodation.

In regard to trade union membership, the Employment Ordinance provides that it is an offence for employers to make an offer of employment conditional upon the applicant relinquishing his or her union membership, not becoming a member of a trade union or not associating with persons for the purpose of forming a trade union.

7.2 Employment contract

Parties cannot contract out of these ordinances. The ordinances cover all employees in Hong Kong, with limited exceptions (but these exceptions do not include part-time employees). They generally also apply to expatriates working in Hong Kong and employees with an employment contract from Hong Kong who are working abroad.

Although parties are free to choose the governing law of an employment contract, the chosen governing law must have sufficient connection with the employment or it may be deemed to be an attempt to contract out of the EO. In practice, employers are advised to comply with Hong Kong employment law standards.

Although not required, a written contract is usually entered into. In addition to the express terms that are included in writing in the contract or agreed verbally, a contract of employment also consists of a number of terms implied by legislation (which parties cannot exclude) or by common law (which parties may be able to vary or exclude by express agreement).

Depending on the particular industry or employer, there may also be trade unions that negotiate workplace agreements between employers and employees. However, if an employee wishes to be bound by such agreement, he or she must make such express provision in his or her employment contract to this effect. Further, the trade union movement in Hong Kong is not particularly strong (although there has been growth recently), and employers are not obliged by law to participate in collective bargaining as there is no collective bargaining law in Hong Kong.

7.3 Expatriates

Foreign employees must obtain a proper Hong Kong visa (eg, an employment, dependant or investment visa) to work in Hong Kong. To qualify for an employment visa, a person must possess skills, knowledge or experience relevant to the job that are unavailable locally. This test can generally be satisfied in the case of an intra-company or intra-group transfer. The applicant also needs to nominate a sponsor, which must be a Hong Kong company or a foreign company registered in Hong Kong. The sponsor is usually the employer company. It normally takes six weeks for the application to be processed. The government charges a nominal fee for the visa if the application is approved.

Expatriates who either enter Hong Kong with a work visa for employment of not more than 13 months, or those who are covered by overseas retirement schemes, are exempt from the mandatory provident fund system.

7.4 Termination

It is unlawful for an employer to dismiss an employee who is: (1) pregnant or on maternity leave; (2) on paid sick leave; (3) involved in giving evidence or information in any proceedings or inquiry; (4) involved in trade unions or their activities; or (5) injured and has not yet agreed his/her compensation for the work-related injury with the employer, or before the issue of a certificate of assessment. It is also unlawful to dismiss an employee in contravention of any of the various ordinances on discrimination (currently, there are four ordinances regulating discrimination in the areas of sex, race, disability, marital status, pregnancy and family status; a recently gazetted bill is seeking to also render discrimination on the ground of breastfeeding unlawful). In the event that such employees have to be terminated, settlement agreements should be reached.

An employer can otherwise terminate an employee's employment at any time by giving notice or payment in lieu (unless prohibited for any of the reasons stated above). However, employers must ensure that employees are terminated only for valid reasons as set out in the Employment Ordinance (eg, conduct, capability/qualification and redundancy), and that the minimum notice periods are observed.

In cases of serious misconduct, an employer may terminate an employee without notice or payment in lieu of notice (summary dismissal). However, if the summary dismissal was not justified, the termination will amount to wrongful termination and the employer will be liable to pay the employee his or her entitlements had he or she been lawfully terminated (ie, with notice).

The EO sets out a statutory regime governing an employer's obligations in situations of layoff and redundancy. Unless summarily dismissed for good cause, an employee is entitled to notice (or a specific payment in lieu of notice) in such situations.

In addition, employees who have been made redundant or who are laid off are entitled to severance pay if they have been employed for two years or more.

7.5 Work health and safety

The Occupational Safety and Health Ordinance (OSHO) obliges employers to ensure, as much as reasonably practicable, the health and safety of their employees at work, such as by providing and maintaining a workplace in a safe condition without any health risks; providing information as may be necessary to ensure the health and safety of employees at work; and providing or maintaining a means of access to and egress from the workplace that are safe and without any health risks.

The Occupational Safety and Health Regulations (the 'OSHO Regulations') additionally impose certain basic minimum standards to which all workplaces must conform, including in relation to cleanliness, ventilation, lighting, drainage and hygiene. The OSHO Regulations also impose specific duties on employers to maintain fire precautions and first aid facilities, such as to ensure that at least two employees are designated with the responsibility to provide and maintain the required first aid facility, and that at least one employee for each 150 employees employed in the workplace is trained in first aid.

An employer's statutory liability regarding health and safety extends only to its employees and not to third parties, such as subcontractors and agency workers who are working on the premises. However, liability may arise with respect to the employer as an 'occupier' to the extent that the third parties are working on premises that are not controlled by their own employer. In such cases, liability for health and safety issues lies with the employer as occupier of the premises.

The Factories and Industrial Undertakings Ordinance imposes an additional general statutory duty on employers of 'industrial undertakings' (defined as including, inter alia, work in a factory, mine or quarry, restaurant or construction) to ensure, as much as reasonably practicable, the health and safety of their employees.

Furthermore, the Factories and Industrial Undertakings (Safety Management) Regulation requires proprietors and contractors, with respect to construction sites, shipyards, factories and other designated industrial undertakings (eg, electricity and gas generation and transmission, and container handling), to develop, implement and maintain a safety management system.

Other than for 'industrial undertakings', there is no specific requirement for employers to have a written health and safety policy. All employers, however, would be well advised to do so as proof that they have complied with their general duty to provide the necessary information, instruction, training and supervision regarding employee health and safety.

There also is no express statutory obligation for employers, other than those in industrial undertakings, to undertake health and safety risk assessments, even though such assessments are necessary to show compliance with the general statutory duty of care. Without periodic assessments, it may be difficult for employers to demonstrate compliance with this obligation. It also should be noted that there is a specific duty under the OSHO Regulations to assess risks to health and safety in relation to manual handling operations and display screen equipment used in the office.

Generally speaking, other than sickness leave records, there are no specific health and safety records that an employer must keep.

Chapter 8: Taxation

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8.1 Outline

Hong Kong's tax regime evolved from the colonial income tax and duty ordinances bestowed by the UK on its colonies. Unlike most former British colonies, however, Hong Kong has preserved a largely territorial system of taxation, and prides itself on being an efficient and low-tax jurisdiction. Recent developments in international taxation, however, including the emergence of Organisation for Economic Co-operation and Development (OECD)-driven global consensus on the automatic exchange of financial account information and hostility to aggressive tax planning, have impelled the rapid evolution of Hong Kong's tax code. In terms of content, form and concept, Hong Kong's tax code bears marked similarities with other common law jurisdictions, most notably Malaysia and Singapore.

Direct taxation in Hong Kong is governed by the Inland Revenue Ordinance (IRO). There is no general income tax as such, but the IRO provides for a schedular system that taxes business and trading profits, income and other emoluments from employment, and income from immovable property situated in Hong Kong. The other principal tax in Hong Kong is stamp duty, which is governed by the Stamp Duty Ordinance. Stamp duty is most relevantly charged on the sale and purchase or other transfer of beneficial interest in immovable property in Hong Kong and Hong Kong stock. Finally, there are a number of relatively minor taxing statutes, such as the Rating Ordinance, which provides for a periodic tax on tenements of land in Hong Kong, and the Dutiable Commodities Ordinance, which charges customs and excise duty.

There is no GST, VAT, or other turnover tax in Hong Kong. It is often misstated that there is no inheritance tax or estate duty in Hong Kong; in reality, the Estate Duty Ordinance remains in force, but the effective rate is currently zero per cent.

The tax year in Hong Kong runs from 1 April to 31 March of the following calendar year. The public body charged with the collection of tax and the application of Hong Kong's tax laws is the Inland Revenue Department. Certain revenue-gathering functions are also performed by the Ratings and Valuation Department and the Customs and Excise Department.

By the standards of other developed jurisdictions, tax administration and compliance in Hong Kong are relatively simple and light-touch.

8.2 Profits tax

Commercially speaking, the most important tax in Hong Kong is profits tax, which approximates tax on corporate profits in other jurisdictions. The charge to profits tax is paradigmatically territorial. Generally, in order to be chargeable to profits tax, a person must: (1) carry on a trade, profession or business in Hong Kong; (2) derive Hong Kong source profits; and (3) such profits must be the profits of the trade, profession or business carried on in Hong Kong. Those three conditions are cumulative: if any one condition is not met, no charge to tax may arise. Consequently, the notion of tax residence is of limited relevance in the context of domestic Hong Kong taxation: profits sourced outside of Hong Kong and arising to a Hong Kong resident person will in the ordinary course not be taxable.

The most difficult concept in understanding the charge to profits tax is that of 'source'. The judicial consensus is that the source or profits is a hard, practical matter of fact to be understood in commercial rather than technical or legal terms. One looks to what the person has done to earn their profits and where they have done it, discounting antecedent or incidental matters. Put another way, one must identify the operations of the taxpayer that in substance give rise to the profits; the locality where the taxpayer conducts those operations will in most cases be taken to be the source of their profits.

Certain receipts are deemed to be chargeable to profits tax irrespective of their locality, of which the most relevant are as follows:

- royalties for the use or the right to use intellectual property rights in Hong Kong;
- interest arising to financial institutions in Hong Kong and Hong Kong source interest arising to corporations carrying on a trade or business in Hong Kong;
- sums for the right to use movable property in Hong Kong; and
- grants, subsidies and other financial assistance in connection with a trade or business carried on in Hong Kong.

Capital gains are expressly exempt from tax; note, however, that assets usually regarded as capital assets, such as securities or immovable property, may be treated as trading stock, and the gains thereof consequently charged to profits tax, if and to the extent that the vendor disposes of such assets in the ordinary course of its trade or business.

Dividends are in general not taxable. There is no WHT in Hong Kong, save in the case of royalties arising to a non-resident for the use or the right to use intellectual property rights in Hong Kong.

The deductions regime is very generous: all expenditure and outgoings incurred in the production of taxable profits (even if not wholly and exclusively so incurred) are deductible in ascertaining the assessable profits of the taxpayer. A crucial limitation to the generosity of the general deduction provision is that capital expenditure is not deductible. There are exceptions to that prohibition for, among other things:

- plant and machinery, which are eligible for depreciation allowances;
- the acquisition of trademarks, patents and certain intellectual property rights;
- environmentally friendly machinery and installations; and
- the construction of commercial and industrial buildings.

Hong Kong now offers a wide range of competitive tax incentives, including:

- reduced rates of profits tax for corporate treasury centre and aircraft-leasing businesses;
- total exemption from profits tax for bona fide widely held collective investment schemes carrying out financial transactions in or through Hong Kong; and
- super-deductions of up to 300 per cent of expenditure for R&D undertaken in Hong Kong.

Since 2018 the IRO has contained a comprehensive transfer pricing and permanent establishment regime consistent with the OECD Model Convention. Arrangements between associated parties are expected to be carried out at arm's length, and the Inland Revenue Department has extensive powers to make transfer pricing adjustments.

Profits tax is charged at the standard rate of 16.5 per cent for corporations and 15 per cent for unincorporated businesses. A lower rate of profits tax of 8.25 per cent for corporations and 7.5 per cent for unincorporated businesses is available for the first HK$2m of assessable profit, subject to certain conditions, the most relevant of which is that only one taxpayer in a given set of associated taxpayers may elect to be taxed at the two-tiered rate. WHT on royalties ranges from 16.5 per cent to 2.25 per cent, subject to the application of any applicable double taxation treaty.

8.3 Salaries tax

Salaries tax is charged on the income and other emoluments from employment arising to a person in a Hong Kong employment. A sum is from employment if it is a reward for past, present or future services of an employee in employment, or otherwise for acting as an employee. Broadly speaking, a person who renders services in employment in Hong Kong for more than 60 days will be chargeable to salaries tax with respect to the income and emoluments he or she derives from employment, though under certain circumstances he or she may be assessable on a pro rata basis as a function of the proportion of a given tax year he or she spent in Hong Kong as opposed to abroad. Again, the notion of tax residence is of limited relevance in the context of salaries tax: one in practice looks to the place where the employment contract was made and services in employment rendered. A person who spends 60 days or fewer rendering services in Hong Kong will not be chargeable to salaries tax.

The charge to salaries tax includes bonuses, perquisites and other emoluments from employment. Gains arising from the grant of shares or the exercise of options are taxable, as are other benefits in money or money's worth, though a benefit in kind will usually not be taxable if it is not capable of being converted into cash. An important exception to that rule is that accommodation provided by an employer to an employee is taxable, albeit on a highly favourable basis. The taxable value of accommodation provided by an employer is deemed to be, variously, four per cent, eight per cent or ten per cent of the employee's taxable income from employment, depending on the size of the accommodation, irrespective of the actual market rent of the property.

Hong Kong does not operate a pay-as-you-earn withholding system of salaries taxation. In the ordinary course, employees are exclusively responsible for filing their own tax returns and for accounting for any tax due.

Director's fees are chargeable to salaries tax to the extent that the company is centrally managed and controlled in Hong Kong. Pensions sourced in Hong Kong are likewise chargeable to salaries tax.

Broadly speaking, salaries tax is charged at progressive rates of up to 17 per cent or at a flat rate of 15 per cent, whichever yields the lower amount of tax.

8.4 Property tax

Property tax is charged on consideration in money or money's worth received for the right to use immovable property in Hong Kong at the flat rate of 15 per cent.

8.5 Stamp duty

Ad valorem stamp duty is a tax on instruments, that is, documents, not transactions. It is most notably charged on:

- the sale and purchase or other transfer of beneficial interest in immovable property situated in Hong Kong;
- the sale and purchase or other transfer of beneficial interest in Hong Kong stock; that is, stock the transfer of which is required to be registered in Hong Kong, which most relevantly includes shares in a company incorporated in Hong Kong or otherwise listed on HKEX; and
- the issue of bearer bonds.

The rates of stamp duty for the transfer of Hong Kong stock are relatively modest: 0.2 per cent on the higher of the consideration or value of the stock transferred. Technically, 0.1 per cent is borne by each of the vendor and the purchaser. There is no stamp duty on the issue, redemption or cancellation of Hong Kong stock.

Stamp duty on the transfer of immovable property can, in view of Hong Kong's overheated property market, be especially onerous. The transfer of residential property is subject to rates considerably higher than those applicable to commercial property. Standard *ad valorem* stamp duty is charged at rates of between 1.5 per cent to 15 per cent on the higher of the consideration given or the value of the property transferred. In addition, special stamp duty is payable at rates of up to 20 per cent if the property is sold within 36 months of its acquisition. Further, buyer's stamp duty at a flat rate of 15 per cent is payable where the purchaser of a residential property is a person other than a Hong Kong permanent resident acting on his/her own behalf. It would follow that rates of stamp duty of up to 50 per cent of the transfer consideration or the value of the property may be charged.

Relief for intra-group transfers is available where the transferor and the transferee are bodies corporate and are 90 per cent associated; that is, one is the direct or indirect owner of 90 per cent of the issued share capital of the other or 90 per cent of the issued share capital of both is owned, directly or indirectly, by the same body corporate.

It is not possible to avoid stamp duty by orally transferring property: both immovable property and Hong Kong stock require an instrument in writing in order to transfer legal title and, in the case of immovable property, beneficial title. Such documentation requirements are in practice symbiotic with stamp duty.

8.6 Tax disputes

Hong Kong has a common law judicial system. Tax appeals arise from a determination of the Commissioner of Inland Revenue or a final adjudication of the Collector of Stamp Revenue, as the case may be, which may be appealed, respectively, to the Board of Review or to the District Court. The Board of Review has original jurisdiction over all tax appeals relating to the IRO and is a judicial tribunal; its proceedings are not open to the public and its judgments are published in an anonymised format. Subsequent appeals may be brought to the Court of First Instance (CFI) or Court of Appeal and, thence, to the Court of Final Appeal (CFA). Historically, there has been a marked preference for out-of-court settlement of tax disputes in Hong Kong, though it should be noted that the higher courts have been consistent in applying orthodox and generally pro-taxpayer interpretations of cardinal principles of Hong Kong tax law.

The assessing practice of the various revenue-gathering bodies in Hong Kong has, in recent times, become more aggressive, in part because of the rapid integration of OECD measures targeting transfer pricing irregularities, treaty abuse and aggressive tax planning.

Revenue clearance may be obtained from the Commissioner of Inland Revenue on matters relating to the chargeability of any person to tax under the IRO through the so-called advance ruling process.

8.7 Anti-avoidance

The IRO contains both general and specific anti-avoidance provisions. Generally, transactions or arrangements that are shams or contrivances, or that have as their principal purpose or one of their principal purposes the gaining of a tax advantage, are disregarded for the purposes of ascertaining a person's liability to tax to the extent necessary to negate the advantage that would otherwise have been obtained by the taxpayer. The Ramsay principle also applies to the construction of revenue statutes in Hong Kong.

Chapter 9: Intellectual property

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Hong Kong is a focal point of the generation of works of intellectual property. The 2019 Global Innovation Index published by the World Intellectual Property Organization (WIPO) ranked Hong Kong as the 13th most innovative economy in the world. In support of innovation, Hong Kong has devised a sophisticated legal framework to protect intellectual property rights.

There are seven main categories of protected intellectual property rights under the laws of Hong Kong (consisting of legislation and the common law). This chapter will provide a general overview of the scope of protection of each of the main categories.

9.1 Trademarks

Registration, validity and protection of trademarks are governed by the Trade Marks Ordinance (Cap 559) (TMO). In addition, the Trade Descriptions Ordinance (Cap 362) also provides for criminal liability arising from the use of false trade descriptions, misleading information and false marks in respect of goods provided in the course of trade.

The TMO sets out detailed requirements for the registration of trademarks in Hong Kong. Section 3 of the TMO defines a 'trademark' as 'any sign which is capable of distinguishing the goods or services of one undertaking from those of other undertakings and which is capable of being represented graphically'.

There are 'absolute' and 'relative' grounds for refusal of registration. The absolute grounds include objections based on the signs not satisfying the definition under section 3 of the TMO (therefore not being apt to perform the function of a trademark in distinguishing the goods or services of one undertaking from another), are lacking in the inherent qualities of a trademark, such as being devoid of distinctiveness, or are descriptive. On the other hand, the relative grounds include, inter alia, prohibition of registration of trademarks that are identical or similar to an earlier trademark in respect of identical or similar goods or services (section 12 of the TMO). The relative grounds of objection to an application for registration mirror the grounds for a registered proprietor alleging infringement of its mark by the use of another sign (section 18 of the TMO).

'Well-known trademarks' that are entitled to protection under the Paris Convention do not require registration for protection. Whether a mark qualifies as a well-known mark is to be tested with a number of factors as stipulated in section 4 and Schedule 2 of the TMO. Under section 12(4) of the TMO, the use of a mark similar to a well-known mark, even in relation to dissimilar goods or services, would still attract liability for infringement. The ultimate question is not whether there exists any likelihood of confusion, but whether the use of the conflicting mark is without due cause, and would take unfair advantage of, or be detrimental to, the distinctive character or repute of the well-known trademark.

Unregistered signs are also protected by the common law doctrine relating to passing-off. A business's goodwill is protected against acts of misrepresentation that cause damage.

The principles on infringement of trademarks and passing-off have been succinctly summarised in the Hong Kong CFA decision *Tsit Wing (Hong Kong) Co Ltd & Ors v TWG Tea Company Pte Ltd* (2016) HKCFAR 20.

9.2 Copyright

In Hong Kong the Copyright Ordinance (Cap 528) (CO 528) is the principal statute concerning protection of copyright and related rights, such as moral rights and rights against use of devices that circumvents copyright. CO 528 provides for both civil and criminal liabilities, the latter being enforceable by the Customs and Excise Department endowed with extensive powers of investigation and prosecution of alleged infringements.

Copyright is defined under the CO 528 as a property right comprising both economic rights and moral rights that is generated by the operation of law, not by registration.

In general, copyright subsists in a work if the work is original, is recorded in a material form, falls within any of the descriptions of work (eg, literary, dramatic, musical or artistic works, sound recordings, films, broadcasts or cable programmes, or typographical arrangement of published editions), and is created by an author who satisfies the qualification requirements or is published in Hong Kong or elsewhere.

Copyright is defined negatively as a right to do acts within Hong Kong that are restricted to be exercised exclusively by the owner or a person with his licence or consent. A copyright owner or its exclusive licensee can take civil legal action against any person who infringes the copyright in the work. Acts of infringement are defined broadly as primary acts, for example, making, publishing or copying, and secondary acts, such as selling, distributing and importing. The former requires no proof of knowledge of infringement on the part of the infringer, whereas reliance on secondary infringing acts requires proof that the infringer has committed the acts knowing such acts would infringe copyright.

The CO 528 provides for a fair dealing exception as a defence to infringement, and a plea of lack of knowledge as defence to damages for infringement.

9.3 Registered designs

A design registration system was created under the Registered Designs Ordinance (Cap 522) (RDO) in Hong Kong. Pursuant to the RDO, applications for registration are made directly to the Hong Kong Designs Registry, and will be subject to a formalistic examination without verification of novelty in relation to prior art. Persons aggrieved by the registration may apply for opposition or rectification.

Pursuant to section 2 of the RDO, any design applied to an article in any industrial process that consist of features of shape, configuration, pattern or ornament with aesthetic appeal may be registered in relation to the article.

In order for a registration to stand up to challenge, it must be a novel design as of the date of the application. Novelty can be defeated by a design of any article previously published anywhere in the world (including in another design registration) that is not substantially different from the subject design. Infringement of a registered design within the territory is established by showing the use of a design that differs only in immaterial details or in features that are variants commonly used in the trade on the same article as registered.

9.4 Patents

Patents in Hong Kong are governed by the Patents Ordinance (Cap 514) (PO), updated by the Patents (Amendment) Ordinance 2016 and the Patents (General) (Amendment) Rules 2019 (with commencement date of 19 December 2019). Three types of patents may be granted under the PO: (1) standard patents (R) (available under the PO 2008 and 2016, for a maximum term of 20 years);

and (2) short-term patents (available under the PO 2008 and 2016, for a maximum term of eight years); and (3) standard patents (O) (available under the PO 2016, for a maximum term of 20 years). The main difference for the newly introduced standard patents (O) is that both formality and substantive examinations are mandatory for a successful application, whereas for standard patents (R) and short-term patents, only formality examination is required. In other words, the new patent system under PO 2016 supplemented by the 2019 rules essentially comprises an original grant patent system that creates a direct route for seeking standard patent protection in Hong Kong with a maximum term of 20 years as an alternative to the 're-registration' route. Original grant patent applications are subject to substantive examination by the registry for determining the patentability of the underlying inventions.

The substantive requirements for registration of patents in Hong Kong include, inter alia, patentable subject matter, susceptibility of industrial application, novelty and inventive step.

9.5 Confidential information

Confidential information is protected under the general common law principles. In summary, the law prevents breach of confidence when the information in question has the necessary quality of confidence, the person in breach has an obligation of confidence, and there is a 'breach' of confidence.

Defences include, inter alia, consent, miscellaneous immunities and disclosure in public interest. The scope of the public interest defence has been thoroughly examined in *The University of Hong Kong v Hong Kong Commercial Broadcasting Co Ltd and Anor* [2016] 1 HKLRD 536 at sections 50–53 in the context of interlocutory injunction; and *The University of Hong Kong v Hong Kong Commercial Broadcasting Co Ltd and Anor* [2016] 4 HKLRD 113 at sections 37–49 in the context of trial. In summary, the court held that there is a constitutionally guaranteed freedom of expression as provided for under Article 16 of the Bill of Rights and Article 27 of the Basic Law in Hong Kong, but the freedom is not absolute. It is qualified by, inter alia, the need to respect the right of others to confidentiality. The test is not whether the matters disclosed would interest the public or be of interest to the public or even 'newsworthy', but whether it is in the public interest that disclosure should be made and the confidence breached. The disclosure must be shown to be required in the public interest. More particularly, where there is justification for disclosure, the disclosure should be to one who has a proper interest to receive the information.

9.6 Private information

The focus is on the 'nature of the information', and whether there is any 'reasonable expectation of privacy', as outlined in *Sima Sai Er v Next Magazine Publishing Ltd and Ors* (unreported, HCA 1500/2014, 8 August 2014) at section 7.

Interaction between the misuse of private information and breach of confidence has been discussed in *Sim Kon Fah v JBPB & Co* [2011] 4 HKLRD 45 at sections 38–45. There may have been an issue that the misuse of private information was shoehorned under the cause of action of breach of confidence:

'42. The second development in the law of breach of confidence identified and discussed by Lord Hoffmann relates to the impact brought upon this branch of the law by art.8 (right to respect for private and family life) and art.10 (right to freedom of expression) of the European Convention and s.6 of the Human Rights Act 1998. The legal development in this regard, including the emergence of what has been described as a tort of "misuse of private information" (per Lord Nicholls of Birkenhead in ***Campbell v. MGN Ltd***, para.14) which has been "shoehorned" into the law of confidence (per Lord Philips of Worth Matravers MR in ***Douglas v. Hello! Ltd (No 3)***), whilst interesting, has no application to the matter before me and thus it is not necessary for me to trace the development in English law or consider how such development may impact upon Hong Kong law.'

9.7 Layout designs

The Layout-Design (Topography) of Integrated Circuits Ordinance (Cap 445) (the 'Layout-Design Ordinance') provides for the rights and protections in relation to layout designs.

Layout design is defined as the three-dimensional disposition, however expressed, of the elements of an integrated circuit and of some or all of the interconnections of an integrated circuit, or such a three-dimensional disposition prepared for an integrated circuit intended for manufacture.

Like copyright, originality is also an essential requirement as per section 2 of the ordinance.

Chapter 10: Financing

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The main ways in which a company can raise funds in Hong Kong are debt finance (whereby investors make available capital for a limited period in return for interest) and equity finance (whereby investors make available capital in consideration for shares in the company).

The focus in this chapter will be on debt finance, which in turn comprises bank lending and raising finance on the capital markets.

10.1 Bank lending

10.1.1 Overview of the legal and regulatory framework

The provision of financial services in Hong Kong is governed by statute, common law, and an array of rules and regulations legislated by government bodies and regulatory authorities.

The main pieces of Hong Kong legislation regarding the activities of banks and money lenders are the Banking Ordinance (Cap 155) (BO), the Securities and Futures Ordinance (Cap 571) (SFO) and the Money Lenders Ordinance (Cap 163) (MLO), while the main regulatory bodies are the Hong Kong Monetary Authority (HKMA), the SFC and, insofar as money lending is concerned, the Hong Kong Companies Registry and the Commissioner of Police. Various industry bodies likewise perform regulatory functions and frequently publish industry-specific guidelines or codes of conduct.

In general terms, money lending activities in Hong Kong can fall into one of two categories:

Lending by an 'authorised institution' (as defined in the Banking Ordinance)

There are three types of authorised institutions, namely banks, restricted-licence banks and deposit-taking companies, each of which has a different scope of permitted activities under the BO. Regulatory oversight of the BO rests with the HKMA, which, among other things, has the power to issue guidelines to approve, suspend or revoke banking licences. Virtual banks also fall within this lending category and are subject to the same application procedure and supervision requirements as conventional banks. As of 24 February 2020, the HKMA had issued eight banking licences to virtual banks in Hong Kong.

Lending by a person that is not an 'authorised institution' or lending by any person to an 'authorised institution'

Loans falling within this category are covered by the MLO and are regulated by the Hong Kong Companies Registry and the Commissioner of Police. Among other things, the MLO requires persons carrying on a lending business to be licensed. Schedule 1 of the MLO sets out certain types of loans and persons that are exempt from this requirement. If a lender that is not exempt makes a loan otherwise than in compliance with the MLO, it will not be entitled to recover any principal or interest or enforce any security in respect of that loan; however, a court may grant relief to the extent it considers equitable.

Further, if a person (including an authorised institution) carries on a business in a 'regulated activity' (as defined in the SFO), that person must also comply with the licensing requirements under the SFO. This means that banks engaging in regulated activities must be registered with the SFC as 'registered institutions', while non-bank entities must be licensed as 'licensed corporations'. In the context of lending, the most relevant type of regulated activity is securities margin financing (which means providing a financial accommodation in order to facilitate the acquisition of securities listed on any stock market and, where applicable, the continued holding of those securities); however, it is noteworthy that there is an exemption for authorised institutions engaging in securities margin financing. Furthermore, lending activities that involve any dealing in securities (eg, bonds, notes or other securities), futures contracts or leveraged foreign exchange contracts, may amount to one or more regulated activities (eg, dealing in securities, dealing in futures contracts or leveraged foreign exchange trading).

Additional requirements apply under the MLO. If a court finds a loan transaction to be extortionate, that is, one that requires the debtor to make grossly exorbitant payments, or which otherwise grossly contravenes ordinary principles of fair-dealing, the court may reopen the transaction so as to do justice between the parties. In addition, any person who lends money at an effective rate of interest exceeding 60 per cent per annum commits an offence. The foregoing requirements apply regardless of whether the creditor is a money lender under the MLO or not, but do not apply to loans to companies with a paid-up share capital of at least HK$1m (or equivalent).

As indicated at the outset, the regulatory regime for financial services in Hong Kong is detailed, comprising numerous rules and regulations on matters such as capital adequacy, transparency, liquidity, and systems and controls. Given the complexity of the legal and regulatory framework, it is vital that persons seeking to navigate it do so with the benefit of adequate legal advice as may be required.

10.1.2 Lender liability regimes

A lender may incur liability in accordance with ordinary principles of Hong Kong contract law, which in turn has adopted many English law principles. In general, a claimant may recover damages if it can demonstrate that the lender has breached the loan agreement, and that such breach has caused the claimant to suffer a loss. Whether a breach has occurred, in turn, would depend on the terms of the loan agreement, as construed in accordance with the rules on contractual interpretation.

Other types of liability may arise. For instance, if a financial institution has acted in an advisory capacity to the borrower in connection with the loan transaction, it may, depending on the circumstances, incur liability for misrepresentation, or negligent or unsuitable advice. Further, the lender may become liable for market misconduct or mis-selling if, having made a recommendation or solicitation, it commits a breach of duty of care and the claimant incurs a loss as a result of that breach. A lender found to have committed market misconduct can incur civil liability, but could also be found criminally liable or face regulatory sanctions.

10.1.3 Exchange controls

There are no foreign exchange controls in Hong Kong that would prevent the repatriation of enforcement proceeds or other payments to a non-Hong Kong-based lender under a loan agreement with a Hong Kong-based counterparty.

10.1.4 Taking security

Under Hong Kong law, a company can grant security over all its present and future assets under a single security agreement. It is also possible for a company to grant security over specific assets (eg, real property, shares, receivables, bank accounts, equipment, inventory, intellectual property, insurances, ships and aircraft) or generic classes of assets.

Security in Hong Kong can secure both *present* and *future* obligations. In addition, security interests may be *fixed* or *floating*. There are several important differences in the legal regimes applicable to fixed and floating charges:

- Fixed charges are usually taken over specific and identifiable assets. Typically, the chargor will be restricted under the terms of the relevant security agreement from disposing of assets subject to a fixed charge (or, in the case of credit balances, from making withdrawals), except with the approval of the secured creditor, until the security interest has been discharged.
- By contrast, a floating charge does not attach to specific assets but 'floats' over a generic class of assets that fluctuates from time to time. It is only upon the occurrence of certain events that the floating charge 'crystallises' and is converted into a fixed charge. A floating charge has the advantage of allowing the chargor to deal with its assets in the ordinary course of business

unless and until crystallisation occurs. A floating charge will be crystallised if the terms of the security agreement specify that on a certain event it will crystallise (eg, when the chargor defaults or the floating charge assets are threatened by execution), upon the appointment of a receiver by the secured creditor or the court, when the chargor commences winding up, or upon the chargor ceasing to do business.

- Generally speaking, a fixed charge provides greater protection to the secured creditor than a floating charge in several respects. A floating charge ranks behind a fixed charge and, upon distribution of a chargor's assets in the case of insolvency, also ranks after certain statutorily preferred creditors (eg, employees and tax authorities). A floating charge granted within the 12 months (or two years, in the case of a connected person) preceding the onset of insolvency of the chargor may be invalid except to the extent of money paid to the chargor, or property or services supplied to it, at the time of or after the creation of the charge.

In terms of perfection, all companies incorporated in Hong Kong are required under CO 622 to register the following security interests with the Hong Kong Companies Registry:

- a charge on uncalled share capital of a company;
- a charge created or evidenced by an instrument that, if executed by a natural person, would require registration as a bill of sale;
- a charge on land (wherever situated) or on any interest in land, except a charge for any rent or other periodical sum issuing out of land;
- a charge on book debts of a company;
- a charge on calls made but not paid;
- a charge on instalments due, but not paid, on the issue price of shares;
- a charge on a ship or any share in a ship;
- a charge on an aircraft or any share in an aircraft;
- a charge on (1) goodwill; (2) a patent or a licence under a patent; (3) a trademark; or (4) a copyright or a licence under a copyright; and
- a floating charge on a company's undertaking or property.

The registration requirement also applies to all non-Hong Kong companies registered in Hong Kong that have property in Hong Kong, where such property is subject to a security interest falling within the list set out above.

Registration with the Hong Kong Companies Registry must generally be effected within one month after the date of creation of the security. Failure to file within the statutory time frame under CO 622 will (unless court approval is obtained to register 'out of time') render the charge void against the liquidator and creditors of the chargor/debtor, but does not prejudice the underlying contract or obligation giving rise to the debt. If the charge is not registered within the statutory timeframe, the beneficiary of the charge may decide at that point in time whether or not the debt is to become immediately payable. In addition to the charge becoming void, the relevant chargor/debtor and any responsible persons may be found to have committed an offence and be liable to a fine.

In addition to registration at the Companies Registry, registration at a specialist register may also be desirable or necessary for priorities as against subsequent mortgagees and purchasers. These specialist registers include, for example, the Hong Kong Land Registry, the Hong Kong Intellectual Property Department and the Registrar of Ships.

Further, where security is granted over contractual rights (eg, by way of a security assignment over receivables), the giving of notice to the counterparties of the underlying contract, while not essential to the effectiveness of the security, may nonetheless be desirable for various reasons. For instance, the provision of notice prevents the counterparty from discharging the assigned debt by payment to the assignor, fixes priorities between competing secured creditors, and limits set-offs from arising between the counterparty and the assignor.

10.1.5 Guarantees

As a general principle, directors of a company are required to act in the company's best interests. In the context of guarantees, this means that the giving of the guarantee must be of commercial benefit to the company. This is a question of fact and depends on the specific facts of any given transaction. Downstream guarantees are typically easier to justify than upstream or cross-stream guarantees, and for this reason it is market practice to arrange for shareholder resolutions to be passed by third-party guarantors in respect of any upstream or cross-stream guarantees. A guarantee given without corporate benefit in violation of the directors' duties may be set aside if the creditor is not acting in good faith (eg, the creditor knew of the breach of directors' duty). Directors may also be personally liable.

10.1.6 Financial assistance

Under Hong Kong law there are rules on financial assistance that prohibit a company from providing financial assistance for the purpose of an acquisition of its own shares or for the acquisition of shares in a holding company (which is itself also incorporated in Hong Kong and of which the company is a direct or indirect subsidiary), unless an exception applies. Such financial assistance may take many forms, including by way of the granting of guarantees and security.

Any company or directors who give unlawful financial assistance are criminally liable. Previously, transactions amounting to unlawful financial assistance were void. CO 622 now provides that the validity of the financial assistance and of any contract or transaction connected with such assistance is not affected only because of contravention of sections in connection with unlawful financial assistance of CO 622.

10.2 Debt capital markets

10.2.1 General overview

In Hong Kong the rules relating to the offer of debt securities are primarily governed by the CWUMPO, SFO and BO. In May 2013 the regulation of public offers of structured products in the form of shares or debentures was transferred by statute from the prospectus regime under the CWUMPO to the regime for public offers of investment under the SFO. The term ‘structured products’ is broadly defined and includes notes that are linked to securities, commodities, indices, properties, interest rates, currency exchange rates or futures contracts; however, there are also certain exclusions from the definition.

There are no specific listing requirements in Hong Kong for the issuance of Hong Kong dollar-denominated debt securities. If relevant debt securities are listed on HKEX, the SFO requires the issuer to maintain a register in Hong Kong of interests in its shares and short positions, as well as a register of its directors’ and chief executives’ interests in its shares and short positions. However, exemptions to this requirement can be obtained from the SFC.

It is not necessary for Hong Kong dollar-denominated issues to be governed by Hong Kong law, although the standard Hong Kong selling restrictions will apply. Further, there are no maturity restrictions, and while no fixed minimum denomination is specified in the relevant regulations, a minimum denomination may be imposed if SFC authorisation is required in connection with the issue.

10.2.2 Regulatory requirements

Companies (Winding Up and Miscellaneous Provisions) Ordinance

The requirements of the CWUMPO regarding the registration and content of prospectuses must be complied with if the issue of ‘debentures’ (which is defined to include debenture stock, bonds and any other debt securities of the company, whether or not constituting a charge on the assets of the company) that are not a ‘structured product’ as defined in the SFO amounts to an ‘offer to the public’.

These requirements can be avoided (for Hong Kong and non-Hong Kong incorporated issuers) if the documents containing or relating to offers of debentures fall within Part 1 of Schedule 17 of the CWUMPO. Such offers include the following:

1. an offer to ‘professional investors’ as defined in the SFO;
2. an offer to no more than 50 persons;
3. an offer in respect of which the total consideration payable does not exceed HK$5m; or
4. an offer in respect of which the minimum principal amount to be subscribed or purchased is no ess than HK$500,000 or its equivalent in another currency

Together, these offers make up the Schedule 17 Safe Harbours.

Offers referred to in (1) and (2) may be combined. It should be noted that in relation to a number of the offers falling within the Schedule 17 Safe Harbours (including the offers referred to in (2), (3) and (4) above), a specific statutory warning legend, as set out in Schedule 18 of the CWUMPO, is required to be included in the relevant documents. In addition, certain other exemptions (in respect of foreign issuers, offers to 'persons whose ordinary business is to buy or sell shares') are also available.

Banking Ordinance

The issue of debt securities may amount to 'taking deposits' under the BO given that 'deposit' is broadly defined to mean a loan of money at interest, at no interest or at negative interest, or repayable at a premium or repayable with any consideration in money or money's worth. This, in turn, can give rise to certain concerns regarding compliance with the BO, as:

1. only authorised institutions can carry on a business of taking deposits in Hong Kong; and
2. unless the issuer is an authorised institution, the issue of an invitation or other offering material in Hong Kong may amount to 'advertising for deposits' from the public in breach of the BO.

These concerns can be addressed in a number of ways, for instance by ensuring that dealers act as principals and are either authorised institutions in Hong Kong or banks incorporated or established outside Hong Kong that are not licensed under the BO. Furthermore, the concern in (1) may be overcome if it can be shown that the issuer is not carrying on in Hong Kong a business of taking deposits.

Securities and Futures Ordinance

It is an offence under the SFO for a person to issue (or to have in their possession for the purposes of issue), whether in Hong Kong or elsewhere, an advertisement, invitation or document that, to his or her knowledge, is or contains an invitation to the public to enter into (or offer to enter into) an agreement to acquire, dispose of, subscribe for or underwrite securities ('securities' for the purposes of the SFO exclude debentures of unlisted Hong Kong-incorporated private companies), structured products or shares, unless the issue is authorised by the SFC.

This can be avoided if the advertisement, invitation or document relates to an offer falling within the Schedule 17 of the Safe Harbours in respect of the issue of 'debentures' that are not structured products, or if an exemption is available under the SFO. Alternatively, approval for the advertisement or invitation can be obtained from the SFC. Certain exemptions are available if the issue (or the possession for the purposes of issue) of any advertisement, invitation or document is made by an entity licensed or registered to carry out certain regulated activity. Other relevant exemptions apply in respect of an advertisement or invitation that:

- is made with respect to securities or shares that are, or are intended to be, disposed of to persons outside Hong Kong only; or
- relates to securities or shares that are, or are intended to be, disposed of to 'professional investors' only.

10.3 Equity capital markets

Under Hong Kong law, the main pieces of legislation concerning the offer of shares to the public are the CWUMPO and SFO.

In general, if an offer of shares is made to the public (which is not being listed on HKEX), then the offering circular must, subject to any applicable exemptions:

- be approved by the SFC;
- contain certain information prescribed by the CWUMPO in relation to prospectuses; and
- be registered with the Registrar of Companies in Hong Kong.

Companies (Winding Up and Miscellaneous Provisions) Ordinance

The requirements of the CWUMPO regarding the registration and content of prospectuses must be complied with if the issue of 'shares' amounts to an 'offer to the public'.

It is market practice for most international offers of shares not involving a listing in Hong Kong to structure the offer and distribution of the offering circular so that the full burden of Hong Kong legal and regulatory requirements does not apply. To this end, issuers may seek to rely on certain statutory exemptions, including the Schedule 17 of the Safe Harbours (see section 10.2.2 (Companies (Winding Up and Miscellaneous Provisions) Ordinance) above), the effect of which is that offering circulars can be distributed in Hong Kong without the need for regulatory approval or compliance with the prospectus content and registration requirements.

Securities and Futures Ordinance

In addition to the rules under the CWUMPO relating to the offer of shares to the public, as seen in section 10.2.2 (Securities and Futures Ordinance) above, the SFO makes it a criminal offence for a person to issue advertisements or invitations in connection with offers of shares to the public under certain circumstances. The exemptions set out above equally apply in connection with the issue of shares to the public.

Further, as mentioned in section 10.1.1 above, the SFO prohibits any person from carrying on business in a 'regulated activity' in the absence of a relevant exemption or registration. This prohibition extends to persons based overseas but marketing (directly or through an agent) their services to the public in Hong Kong. One of the regulated activities is 'dealing in securities' (a Type 1 regulated activity), which includes marketing securities ('securities' for the purposes of the SFO exclude shares of unlisted Hong Kong-incorporated private companies) to Hong Kong persons but specifically excludes where a person, as principal, performs the act by way of dealing with institutional professional investors, or (generally speaking) where a person performs the act through a licensed securities dealer (noting, however, that there are certain carve-outs to this).

Chapter 11: Privacy laws and data protection

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This chapter considers, at a high level, the data protection regime in Hong Kong.

11.1 Regulatory framework

The main legislation relating to data protection is the Personal Data (Privacy) Ordinance (Cap 486) (PDPO). The Office of the Privacy Commissioner for Personal Data (PCPD) is an independent statutory body set up to oversee the enforcement of the PDPO. While it is not made clear on the face of the legislation, the PDPO is not generally considered to have extraterritorial application and so is only considered to apply to data users who control the collection, holding, processing or use of 'personal data' from within Hong Kong.

'Personal data' means any data:

- relating directly or indirectly to a living individual;
- from which it is practicable for the identity of the individual to be directly or indirectly ascertained; and
- in a form in which access to or processing of the data is practicable.

The PDPO does not currently regulate the transfer of personal data to places outside of Hong Kong (see section 11.5 for further discussion).

11.2 The six data protection principles

Generally speaking, data users must not do any act, or engage in any practice, that contravenes any of the six data protection principles set out in Schedule 1 of the PDPO, unless an exemption applies.

The data protection principles are summarised by the PCPD as follows:

1. Personal data must only be collected for a lawful purpose directly related to a function or activity of the data user. The data collected should be necessary and adequate but not excessive for such purpose. The means of collection should be lawful and fair.
2. Data users must take all practicable steps to ensure that personal data is accurate and is not kept longer than is necessary for the fulfilment of the purpose for which the data is used.
3. It is prohibited to use personal data for any new purpose that is not or is unrelated to the original purpose when collecting the data, unless with the data subject's express and voluntary consent. A data subject can withdraw his/her consent previously given by written notice.
4. Data users must take all practicable steps to protect the personal data they hold against unauthorised or accidental access, processing, erasure, loss or use. Among other things,

data users should have particular regard to the nature of the data, the potential harm if those events were to happen, and measures taken for ensuring the integrity, prudence and competence of persons having access to the data.

5. Data users must take all practicable steps to ensure openness of their personal data policies and practices, the kind of personal data held and the main purposes for holding it.

6. Data subjects have the right to request access to and correction of their own personal data. A data user should give reasons when refusing a data subject's request to access to or correction of his or her personal data.

Apart from the high-level principles, the PDPO also prescribes rules in relation to the use and provision (including to third parties) of personal data for direct marketing purposes and third-party processing of personal data.

11.3 Third-party processing of personal data

Currently, the PDPO does not regulate data processors (a person who processes personal data on behalf of another person and does not process the data for any of the person's own purposes) but places the obligation to protect personal data on data users.

If a data user engages a data processor, whether within or outside Hong Kong, to process personal data on the data user's behalf, the data user must, under data protection principles 2(3) and 4(2) respectively, adopt contractual or other means to: (1) prevent any personal data transferred to the data processor from being kept longer than is necessary for processing of the data; and (2) prevent unauthorised or accidental access, processing, erasure, loss or use of the data transferred to the data processor for processing.

In an information leaflet on Outsourcing the Processing of Personal Data to Data Processors issued in 2012 (which is non-binding), the PCPD indicated by way of example the types of obligations that could be imposed on a data processor by contract:

- security measures required to be taken by the data processor to protect the personal data entrusted to it and obligating the data processor to protect the personal data by complying with the data protection principles;
- timely return, destruction or deletion of the personal data when it is no longer required for the purpose for which it is entrusted by the data user to the data processor;
- prohibition against any use or disclosure of the personal data by the data processor for a purpose other than the purpose for which the personal data is entrusted to it by the data user;
- absolute prohibition or qualified prohibition on the data processor against subcontracting the service that it is engaged to provide;
- immediate reporting of any sign of abnormalities;
- data user's right to audit and inspect how the data processor handles and stores personal data; and
- consequences for violation of the contract.

11.4 Direct marketing

For the purposes of the PDPO, 'direct marketing' is defined as offering or advertising goods, facilities or services, or soliciting donations or contributions by communications addressed or directed to a specific person by name. Therefore, direct marketing does not include communications that are not directed to a specific individual (eg, a telemarketer who calls randomly generated phone numbers; although, that could separately be subject to the Unsolicited Electronic Messages Ordinance (Cap 593)).

The PDPO requires the data user to provide the following information to the data subject before using personal data for direct marketing purposes:

- the intention to use their personal data for direct marketing and that it can only do so with the data subject's consent;
- the types of personal data it proposes to use for direct marketing; and
- the classes of marketing subjects to which the proposed direct marketing will relate.

In addition, the data user must not use personal data in direct marketing without the data subject's written consent. The PDPO also requires the data user to notify the data subject when using personal data in direct marketing for the first time, while the data subject may require the data user to cease using personal data in direct marketing at any time.

11.5 Cross-border transfer of data

Section 33 of the PDPO, which has not yet come into force, prohibits the transfer of personal data outside of Hong Kong, except in certain circumstances (including, eg, where consent has been given, or the transfer is to a place that has laws substantially similar to the PDPO).

There is no clarity as to when (if ever) section 33 will be brought into force. Therefore, the PDPO does not currently regulate the transfer of personal data to places outside of Hong Kong. However, as a matter of good practice, certain local regulators (eg, HKMA) require their regulated entities to treat section 33 of the PDPO as if it were in force.

11.6 Proposed changes

On 20 January 2020 the Constitutional and Mainland Affairs Bureau presented a paper to the Legislative Council proposing the following changes to the PDPO (the 'Paper'):

- Introduction of a mandatory breach notification: this would require data users to notify both the PCPD and the relevant data subject within a specified timeframe in the event of a data breach.
- Certainty around data retention periods. Data users would be required to maintain a clear retention policy specifying: (1) a maximum retention period for different categories of personal data; (2) legal requirements that may affect the retention period (eg, taxation, employment or medical requirements); and (3) how the retention period will be counted. Currently the PDPO

is not specific in this regard and requires data users to take all practicable steps to ensure that personal data is not kept 'longer than is necessary'.

- Enhanced powers to sanction. The PCPD would be conferred power to directly impose administrative fines for any contravention of the PDPO instead of first having to issue an enforcement notice. The Paper contains proposals to increase the level of fines that may be imposed for criminal liability, and links the level of fines to the annual turnover of the data user. The Paper suggests that data users be classified with different scales according to turnover and that those scales be matched to different levels of administrative fines.
- Regulation of data processors. As noted above, the PDPO does not currently regulate data processors. The proposals would expand the PDPO's regulatory reach to cover data processors.
- Amendments to the definition of personal data. The Paper proposes expanding the definition of 'personal data' to cover information relating to an 'identifiable' natural person.

However, there is no clear timeframe as to when concrete amendments will be tabled for the Legislative Council's debate and approval.

Chapter 12: Competition law

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12.1 Overview

The primary source of competition law in Hong Kong is the Competition Ordinance (Cap 619) (CO 619) and its related subsidiary legislation.[10] CO 619 applies to all sectors of the economy in Hong Kong and is principally enforced by the Competition Commission (the 'Commission'). The Communications Authority shares concurrent jurisdiction with the Commission to enforce CO 619 in respect of undertakings operating in the telecommunications and broadcasting sectors.

CO 619 primarily prohibits conduct that has the object or effect of preventing, restricting or distorting competition in Hong Kong. Such conduct includes horizontal and vertical anti-competitive arrangements between undertakings and abuses of a substantial degree of market power. CO 619 also prohibits mergers that have or are likely to have the effect of substantially lessening competition in Hong Kong (currently only applicable to mergers involving a telecommunications carrier licence holder). In short, CO 619 prohibits three types of anti-competitive conduct under: (1) the First Conduct Rule; (2) the Second Conduct Rule; and (3) the Merger Rule, which will be explained further below.

The prohibitions apply to anti-competitive conduct, whether the arrangement was made or given effect to within or outside Hong Kong, if it has the object or effect of harming competition in Hong Kong.

10 CO 619 came into full effect on 14 December 2015.

Substantial sanctions for contravention of the competition rules may be imposed by the Competition Tribunal (the 'Tribunal'), including pecuniary penalties up to ten per cent of the turnover of the relevant undertaking obtained in Hong Kong for each year in which the contravention occurred, up to a maximum of three years, disgorgement of profits, injunctions and director disqualification orders for a period up to five years. A list of the sanctions that may be ordered is set out in Schedule 3 of CO 619.

CO 619 includes a leniency regime. The Commission may agree with a person that it will not bring or continue proceedings in the Tribunal for a pecuniary penalty in exchange for the person's cooperation in an investigation or in proceedings under CO 619.

Standalone private enforcement actions are not permitted.[11] However, a party may raise a contravention of the conduct rules as a defence to a private civil action.[12] Follow-on private actions for damages resulting from any conduct that has been determined to be a contravention of a conduct rule may be brought before the Tribunal.[13]

12.2 The First Conduct Rule

The First Conduct Rule prohibits any agreement, concerted practice or decision where the object or effect is to prevent, restrict or distort competition in Hong Kong.[14] This includes horizontal arrangements between competitors and vertical arrangements, such as resale price maintenance in a distribution agreement.

Conduct involving price fixing, market sharing, output restriction and bid-rigging (or any combination of these activities) constitutes 'serious anti-competitive conduct'.[15] Where conduct falls within 'serious anti-competitive conduct', the Commission is not required to issue a warning notice to the undertaking before bringing proceedings in the Tribunal.[16] In addition, the general exclusion for agreements of lesser significance (ie, agreements between undertakings with a combined global turnover of less than HK$200m) does not apply to 'serious anti-competitive conduct'.

Where the contravention of the First Conduct Rule does not involve 'serious anti-competitive conduct', the Commission must issue a warning notice to provide the undertaking with an opportunity to cease the contravening conduct within a specified period. If the undertaking complies with the warning notice, it is protected from prosecution. If the undertaking continues or repeats the contravening conduct after the expiry of the specified period, the Commission may bring enforcement proceedings without further notice, but not in respect of any contravening conduct that precedes the specified period.

Conduct subject to the First Conduct Rule may be excluded or exempt from its application by virtue of: (1) the general exclusions under section 30 of CO 619 and Schedule 1; (2) the exemptions granted on public policy grounds under section 31 or to avoid conflict with international obligations

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11 *Loyal Profit International Development Limited v Travel Industry Council of Hong Kong* (unreported, HCMP 256/2016, 27 April 2017).

12 *Taching Petroleum Company Limited v Meyer Aluminium Limited* [2019] HKCT 1 where the defence raising price fixing and exchange of pricing information was transferred to the Tribunal under section 113 CO 619. Hon Au-Yeung J refused to stay the remainder of the High Court action, ordering instead that both sets of proceedings should be tried together before the same judge constituting the Tribunal.

13 S 110 of CO 619.

14 S 6 of CO 619.

15 This term is defined in s 2 of CO 619.

16 S 82 of CO 619.

under section 32; or (3) the disapplication of certain provisions of CO 619 to statutory bodies, specified persons and persons engaged in specified activities as provided for in sections 3 and 4 of CO 619.

Agreements may be exempt from the First Conduct Rule on an individual basis or via a block exemption. On 8 August 2017 the Commission issued a Block Exemption Order in respect of vessel sharing agreements in the liner shipping industry, excluding such agreements from the application of the First Conduct Rule by virtue of the economic efficiencies generated by them. The exemption is for five years and is subject to certain conditions.

On 17 May 2019 the Tribunal handed down two landmark decisions relating to cartel conduct. These decisions are the first two successful enforcement actions brought by the Commission.

In *Competition Commission v Nutanix Hong Kong Limited* [2019] HKCT 2, the Tribunal found all but one of the five respondent IT firms liable for contravening the First Conduct Rule by engaging in bid-rigging in respect of a tender for the supply and installation of a Nutanix cloud-based server system for the Young Women's Christian Association in 2016. A previous tender had failed as BT Hong Kong Ltd (BT) was the only company that submitted a bid and the Young Women's Christian Association's procurement policy required a minimum of five bids. To assist BT in winning the second tender, Nutanix agreed with BT that it would obtain 'dummy' or 'non-genuine' bids from its channel partners to make up the required number. BT's completed bid was provided to an employee of Nutanix who prepared bids for SiS International Ltd (SiS), Innovix Distribution Ltd (Innovix) and Tech-21 Systems Ltd (Tech-21) with substantially higher bid prices than BT.

The Tribunal held that each of the vertical bilateral arrangements between Nutanix and BT, and Nutanix and Tech-21, as well as the trilateral arrangement among Nutanix, BT and Innovix, constituted 'serious anti-competitive conduct' and a breach of the First Conduct Rule. However, the acts of a junior employee who had no authority to commit SiS to any expenditure or set the price for any deal could not be attributed to SiS. The junior employee in question had essentially gone rogue in submitting the 'dummy' bid and was not acting in the course of his employment or as part of SiS.

Importantly, the Tribunal ruled that the criminal standard of proof beyond reasonable doubt applied to enforcement proceedings involving a pecuniary penalty. This sets Hong Kong as the only common law jurisdiction that applies the criminal standard of proof in competition law proceedings.

In *Competition Commission v W Hing Construction Co Ltd & Ors* [2019] HKCT 3, the Tribunal found all ten respondents, who were renovation contractors licensed by the Hong Kong Housing Authority, liable for contravening the First Conduct Rule by engaging in market sharing and price fixing. The respondents were found to have entered into arrangements whereby:

- each respondent was allocated four floors in each of the three buildings in an estate and the respondents had agreed to: (1) refrain from actively seeking and accepting business from tenants on floors allocated to other respondents; and (2) direct tenants on the floors allocated to the other respondents to their allocated contractor (the 'Market Sharing Arrangement'); and
- the respondents jointly produced and distributed a promotional flyer to tenants that set out, among other matters, the prices for ten types of commonly requested decorative works and

the service packages and prices for the four types of flats available at the estate (the 'Price Fixing Arrangement').

The Tribunal held both the Market Sharing Arrangement and Price Fixing Arrangement restricted competition by object in breach of the First Conduct Rule, and constituted 'serious anti-competitive conduct'.

The 'efficiency defence' raised by some of the respondents was rejected. Those respondents had claimed that the arrangements enhanced overall economic efficiency by allowing the contractors to work on multiple flats on the same floor on account of the time saved from having to wait for lifts to move equipment and materials from floor to floor, and should be excluded from the application for the First Conduct Rule under section 30 and Schedule 1 of CO 619.

The Tribunal held that the burden was on the relevant respondents to bring themselves within the exclusion by establishing the efficiency defence on the balance of probabilities. Notwithstanding the lower standard of proof applied, the Tribunal found that the conditions for the efficiency defence had not been made out.

The Tribunal further ruled that two respondents who had allowed their subcontractors to use their names in return for a fee to independently carry out the decoration works were liable for the acts of their subcontractors, notwithstanding their lack of knowledge of and participation in such acts. Of note is the fact that the Tribunal appeared to have adopted a liberal interpretation of what constitutes a 'single economic unit', holding that the relevant contractor and subcontractor formed part of the same undertaking by reason of the 'unity' of their conduct on the market.

12.3 The Second Conduct Rule

The Second Conduct Rule prohibits the abuse of a substantial degree of market power where the object or effect is to prevent, restrict or distort competition in Hong Kong.[17] CO 619 specifically refers to two examples of 'abuse', namely: (1) predatory behaviour towards competitors; and (2) production, markets or technical developments to the prejudice of consumers.

The Second Conduct Rule only applies where an undertaking has a substantial degree of market power in the relevant market. There is no guidance from CO 619 or the Commission as to an indicative market share safe harbour or presumptive threshold over which a substantial degree of market power may be presumed. However, CO 619 provides that the following matters (among others) may be taken into consideration, namely: (1) the market share of the undertaking; (2) the undertaking's power to make pricing and other decisions; and (3) any barriers to entry for competitors into the relevant market.

Examples of abusive behaviour may include predatory pricing, anti-competitive tying and bundling, margin squeeze, refusal to supply and exclusive dealing.

Conduct by an undertaking the turnover of which is lower than HK$40m is excluded from the Second Conduct Rule. In addition, CO 619 provides for other exclusions and exemptions with respect to the application of the Second Conduct Rule, namely: (1) compliance with legal requirements;

17 S 20 of CO 619.

(2) services of general economic interest; (3) mergers; (4) public bodies and international obligation exemptions;[18] and (5) the disapplication of certain provisions of CO 619 to statutory bodies, specified persons and persons engaged in specified activities as provided for in sections 3 and 4 of CO 619.

12.4 Mergers

Under the Merger Rule, mergers that have or are likely to have the effect of substantially lessening competition in Hong Kong are prohibited. The scope of application of the Merger Rule is currently limited to mergers relating to undertakings directly or indirectly holding carrier licences issued under the Telecommunications Ordinance (Cap 106).

Chapter 13: Dispute resolution

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The predominant dispute resolution mechanisms for commercial disputes in Hong Kong are litigation before the Hong Kong courts and Hong Kong seated arbitration. Both methods are addressed in this chapter. There are other mechanisms considered as feasible alternatives, such as mediation, conciliation, expert determination and adjudication. Save mediation, which is addressed briefly in section 13.3 below, these alternatives are not discussed further here.

13.1 Litigation before the Hong Kong courts

13.1.1 Overview

Depending on the value in dispute, civil and commercial matters in Hong Kong are generally commenced either in the District Court (for claims with a monetary value between HK$75,000 and HK$3m) or the CFI (for claims with a monetary value exceeding HK$3m). The CFI has unlimited jurisdiction over civil matters and organises specialist lists for particular types of disputes (eg, the construction and arbitration list for cases concerning, among other things, building and other construction work, as well as applications relating to arbitration). Depending on the nature of a dispute, there are also specialist courts and tribunals with jurisdiction over specific subject matters (eg, the lands tribunal and the competition tribunal); however, these are usually less relevant to large commercial disputes.

The procedural steps for disputes before the CFI are governed by the Rules of the High Court (Cap 4A) (RHC). The civil litigation process before the District Court is governed by the Rules of the District Court (Cap 336H) (RDC), which are to a large extent consistent with the Rules of the High Court. Both the RHC and RDC set forth detailed rules concerning all aspects of the proceedings,

18 Ss 31 and 32 of the CO 619.

including matters relating to evidence and document production, summary judgment and interlocutory injunctions.

In terms of timing, the Hong Kong courts generally allow the matter to proceed to a relatively speedy judgment, particularly if uncontested. The length of time to judgment will depend on the arguments raised by the defendant in its defence (if any); although a full trial can, if necessary, proceed within 18 to 24 months for a standard commercial matter.

13.1.2 Appeals

There are two levels of appeal in the Hong Kong court system: the Court of Appeal and the CFA. Appeals against decisions of the CFI are heard by the Court of Appeal, while the CFA is the highest appellate court in Hong Kong and decisions handed down by it are binding on all Hong Kong courts.

Appeals can normally only be made with leave of the court. Leave to appeal to the Court of Appeal will not be granted unless:

- the appeal has a reasonable prospect of success; or
- there are some other reasons in the interests of justice why the appeal should be heard.

While appeals against decisions of the CFI can relate to matters of law or fact, an appeal will not normally involve a full rehearing (eg, of witnesses), and so the grounds of appeal are usually limited to questions of law rather than fact.

13.1.3 Costs

As well as determining the substantive issues in dispute between the parties, the court will normally also make an order regarding the costs incurred by the parties in respect of the litigation. The general rule is that the unsuccessful party pays the costs of the successful party. However the court has complete discretion in this matter and may decide to make a different order. For instance, if one of the parties has conducted the litigation improperly or unreasonably, then the court may penalise that party by making it pay more or receive less (as appropriate) by way of costs. One factor the court will consider in assessing the conduct of the parties is whether one of the parties unreasonably refused to take part in settlement negotiations or mediation at an earlier stage of the dispute.

The amount of the costs to be recovered will be 'taxed' (ie, assessed) by the court if the parties are not able to agree. In practice, the court rarely makes an award of costs which is equal to the costs the successful party actually incurred; typically, recovery will be in the order of between 50 per cent and 70 per cent of actual costs.

13.1.4 Enforcement of foreign judgments

There are two main regimes for the enforcement of foreign judgments in Hong Kong: the statutory regime and the common law regime.

The statutory regime under the Foreign Judgments (Reciprocal Enforcement) Ordinance (Cap 319) applies – to the exclusion of the common law regime – to judgments handed down in certain

Commonwealth countries, as well as the 'superior courts' of certain states listed in the Foreign Judgments (Reciprocal Enforcement) Order (Cap 319A). As of 1 May 2020 the relevant Commonwealth countries were Bermuda, Brunei, India, Malaysia, New Zealand, Singapore and Sri Lanka, while the list of other states comprised Australia, Belgium, France, Israel, Italy and the Netherlands.

Under the statutory regime a judgment creditor may apply to the CFI at any time within six years after the date of the foreign judgment (or the last appeal judgment in respect of it) to have that judgment registered. A registered foreign judgment is of the same force and effect as if it had been a judgment originally given in Hong Kong.

Under the common law regime, a foreign judgment is treated as constituting a cause of action against the judgment debtor, and as such may be sued upon summarily by the judgment creditor in the Hong Kong courts. The Hong Kong courts will generally enter judgment in favour of the judgment creditor without re-examining the merits of the foreign judgment, provided that certain requirements are satisfied. These requirements include, among other things, that:

- the foreign court rendering the judgment was of competent jurisdiction;
- the foreign judgment is final and conclusive; and
- the foreign judgment is for a fixed sum of money not being a tax, fine or penalty.

With respect to mainland China, the CFA observed in *First Laster Ltd v Fujian Enterprises (Holdings) Co Ltd* (2012) 15 HKCFAR 569, at paragraph 43, that:

> '[a]lthough the HKSAR and the PRC are part of one country, for the purposes of the conflict of laws they are separate districts, and a judgment of the Supreme People's Court is a foreign judgment, and will be enforced or recognised in Hong Kong only if it fulfils the conditions for enforcement or recognition at common law'.

Nonetheless, several mutual arrangements between Hong Kong and the mainland are in place to allow for the reciprocal recognition and enforcement of judgments in civil and commercial matters. Of particular importance among these is the arrangement made in 2006 for the recognition and enforcement of judgments in civil and commercial matters pursuant to choice of court agreements (the Choice of Court Arrangement), which is implemented under Hong Kong law in the Mainland Judgments (Reciprocal Enforcement) Ordinance (Cap 597). Pursuant to the Choice of Court Arrangement, a mainland judgment given by a designated court on or after 1 August 2008 may be enforced in Hong Kong by registration in the CFI if:

- the judgment is final and conclusive, and is enforceable in the mainland;
- the judgment is for the payment of a sum of money (not being a tax, fine or penalty) arising from a commercial agreement; and
- the parties have entered into a 'choice of Mainland court agreement' on or after 1 August 2008.

On 18 January 2019 the Hong Kong government and the SPC signed the Arrangement on Reciprocal Recognition and Enforcement of Judgments in Civil and Commercial Matters by the Court of the Mainland and of the Hong Kong Special Administrative Region (the '2019 Arrangement'). The 2019 Arrangement removes some of the limitations to which the current enforcement regime is subject.

Unlike the Choice of Court Arrangement, it is not limited to monetary judgments and does not depend on the existence of a choice of court agreement under a commercial contract. Further, it sets out jurisdictional grounds for recognition and enforcement purposes.

At the time of writing, the 2019 Arrangement had not yet entered into force. Upon becoming effective, it will supersede the Choice of Court Arrangement, which will continue to apply in respect of judgments made before the date of commencement of the 2019 Arrangement.

13.1.5 Sovereign and crown immunity

In *Democratic Republic of the Congo v FG Hemisphere Associates LLC* [2011] HKCFA 41, a 3:2 majority of the CFA held that *state immunity* not only covers sovereign acts, but also states' commercial activities. The decision, which was preceded by an interpretation issued by the National People's Standing Committee to the same effect, confirmed that the concept of absolute immunity applies in Hong Kong. Importantly, the majority of the court further held that a foreign state cannot waive its immunity by agreement in advance of proceedings on the basis that state immunity could be waived only after the commencement of proceedings.

Notwithstanding that certain exceptions may apply, the decision in *FG Hemisphere* means that private parties dealing with foreign state or state-affiliated entities would be well advised to take into account the immunity enjoyed by foreign states from proceedings before the Hong Kong courts and, if necessary, to seek legal advice.

Where the PRC or an entity affiliated to it is involved, the doctrine of crown immunity applies instead. Whether an entity is part of the PRC and therefore entitled to invoke crown immunity is a question of fact. While the amount of control that the state is able to exert over an entity is a material factor, other factors are also relevant (eg, the object and functions of the entity), and as such it is important, in the context of crown immunity as in relation to state immunity, to obtain legal advice if required.

13.2 Hong Kong seated arbitration

13.2.1 Arbitration Ordinance

The primary arbitration legislation in Hong Kong is the Arbitration Ordinance (Cap 609) which creates a unitary regime governing both domestic and international arbitration. The Arbitration Ordinance is based on the UNCITRAL Model Law on International Commercial Arbitration[19] and is regularly amended to keep pace with key developments in the international arbitration sphere. For instance, the most recent set of amendments, which were introduced in 2017 and came into operation on 1 January 2018, clarified that disputes over intellectual property rights are capable of resolution by arbitration, and that the enforcement of awards involving intellectual property rights did not contravene Hong Kong public policy.

The object of the Arbitration Ordinance is to facilitate the fair and speedy resolution of disputes and the avoidance of unnecessary expenses. Further, the statute is based on the principles that parties

19 The Model Law can be accessed at www.uncitral.org/pdf/english/texts/arbitration/ml-arb/07-86998_Ebook.pdf accessed 24 March 2020.

should be free to agree on the resolution of their disputes and that arbitral proceedings should be free from court interference save as expressly provided in the Arbitration Ordinance.

Another key feature of the Arbitration Ordinance is the protection of confidentiality in arbitration and related court proceedings. To this end, the legislation prohibits parties to the arbitration from disclosing information concerning the proceedings or award unless otherwise agreed between the parties or unless one of the limited exceptions under the Arbitration Ordinance applies. These exceptions allow the disclosure by a party of confidential information if such disclosure is:

- made to protect or pursue a legal right or interest of the party;
- required by law to be made to a governmental or regulatory body, court or tribunal; or
- made to a professional or other adviser of the parties.

The Arbitration Ordinance further provides for a wide range of interim relief by empowering a tribunal to grant an order for an interim measure at the request of a party to:

- maintain or restore the status quo pending determination of the dispute;
- take action that would prevent (or refrain from taking action that is likely to cause) current or imminent harm or prejudice to the arbitral process;
- provide a means of preserving assets out of which an award may be satisfied; or
- preserve evidence that may be relevant and material to the resolution of the dispute.

In addition to being able to recognise and enforce interim measures granted by Hong Kong, as well as foreign-seated arbitral tribunals, Hong Kong courts are empowered to grant interim measures in support of arbitration proceedings commenced in Hong Kong and elsewhere.

13.2.2 Hong Kong International Arbitration Centre

The HKIAC, one of the world's leading arbitral centres, is based in Hong Kong. A 2015 study revealed that the HKIAC is the third most preferred and used arbitral institution worldwide, and the most favoured arbitral institution outside of Europe. Since then, Hong Kong has consistently ranked among the top four seats of arbitration in the world.

Under the Arbitration Ordinance, the HKIAC enjoys a statutory role as the body for the appointment of arbitrators and the determination of the number of arbitrators, in the absence of agreement between the parties.

In November 2018 the HKIAC 2018 Administered Arbitration Rules (the '2018 Rules') entered into force. The 2018 Rules, which apply to arbitration commenced after 1 November 2018, introduced a number of amendments to the former set of rules relating to, among other things:

- the use of technology: this has been identified as a factor to be considered by tribunals in the determination of the procedure of the arbitration;
- the emergency arbitrator procedure: in addition to introducing a cap on emergency arbitrator fees and shortening the time limits under the emergency arbitrator procedure, the 2018 Rules

allow parties to file an application for the appointment of an emergency arbitrator up to seven days before a notice of arbitration is submitted to the HKIAC;

- third-party funding: the 2018 Rules introduced a requirement for funded parties to disclose the existence of a funding agreement and the identity of the funder; and
- a new early determination procedure: under the 2018 Rules, a tribunal is empowered, if so requested, to decide points of law or fact by way of early determination on the basis that such points are manifestly without merit or manifestly outside the tribunal's jurisdiction, or would not allow – even if assumed to be correct – an award to be rendered in favour of the other party.

13.2.3 Enforcement of arbitral awards

Hong Kong is not a state and thus cannot of its own be a Contracting State to the New York Convention. However, following the transfer of sovereignty over Hong Kong to the PRC in 1997, the government of the PRC extended the territorial application of the New York Convention to Hong Kong, subject to the reservations originally entered by the PRC on its accession to the Convention.

As such, awards made in Hong Kong can be enforced with relative ease in more than 160 states that are Contracting States to the New York Convention. Conversely, the Arbitration Ordinance provides that awards made in Contracting States can be enforced by action in the court, or in the same manner as awards rendered in Hong Kong or in non-New York Convention states.

Awards made in Hong Kong or non-New York Convention states are enforceable under the Arbitration Ordinance in the same manner as a court judgment; however, only with leave of the court. Leave is not granted automatically. Grounds on which enforcement can be refused are set out in the Arbitration Ordinance and include, for instance, the incapacity of a party to the arbitration, the invalidity of the arbitration agreement, certain procedural irregularities or a conflict with Hong Kong public policy. In practice, however, leave to enforce will only be refused in unusual cases, and if so, it may nonetheless be possible to enforce an award through an action on the award at common law.

The enforcement of Hong Kong awards in mainland China and vice versa is not governed by the New York Convention, as they are not awards made in the territory of another New York Convention state. The same reasoning applies to the enforcement of awards between Hong Kong and Macao. For this reason, the enforcement regime in Hong Kong is complemented by arrangements with the mainland and Macao, respectively, for the reciprocal enforcement of arbitral awards, which provide for enforcement on largely similar terms to the New York Convention.

13.3 Mediation

A significant aspect of the Hong Kong civil justice system is that parties are encouraged to settle their disputes amicably; indeed, 'to facilitate the settlement of disputes' is one of the underlying objectives of the RHC and RDC. In line with this objective, the Hong Kong legal system has developed a robust framework for mediation with the Mediation Ordinance (Cap 620) at its centre. The aim of the Mediation Ordinance is to promote, encourage and facilitate the resolution of disputes by mediation, and to protect the confidential nature of mediation communications.

In addition to administering arbitration, the HKIAC also offers mediation services and has a division – the Hong Kong Mediation Council – specifically dedicated to mediation. However, in recent years an increasing number of mediation institutions and mediation-related bodies have come into existence in Hong Kong, with examples including the Hong Kong Institute of Mediators and the Hong Kong Mediation Accreditation Association Limited. The latter, founded in 2012, is the premier accreditation body for mediators in Hong Kong. The HKMAAL accredits mediators and provides training courses while seeking to promote 'a culture of best practice and professionalism' in Hong Kong mediation.

The proliferation of mediation institutions has been accompanied by the promulgation of the Hong Kong Mediation Code, which has been adopted by a number of mediation service providers (including the HKIAC, Hong Kong Mediation Accreditation Association Limited and Hong Kong Mediation Centre) and aims to serve a quality assurance function by providing a common standard among mediators.

Further, on 7 August 2019 the UN Convention on International Settlement Agreements Resulting from Mediation (the 'Singapore Convention') was signed by 46 states (including the PRC, Singapore and the US) and will come into force on 12 September 2020. The Singapore Convention – noting in its preamble the increasing use of mediation as an alternative to litigation and its role in the development of harmonious international economic relations – establishes a cross-border enforcement mechanism for the enforcement of settlement agreements resulting from mediation. Notwithstanding that the PRC is a signatory to the Singapore Convention, it does not follow that the Convention will apply in Hong Kong following its entry into force, as the Basic Law of Hong Kong provides that international agreements do not automatically apply in Hong Kong on ratification by the PRC. While the future of the Singapore Convention in Hong Kong is therefore currently uncertain, if and when its application is extended to Hong Kong, it is likely to further corroborate the position of Hong Kong as a leading international dispute resolution centre.

India

Chapter 1: Introduction

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As the world's largest democracy, with a population of over 1.3 billion people occupying the world's seventh-largest country (by land area and in terms of its economy), India continues to be one of the world's most attractive investment destinations.

A former British colony, India followed a protectionist/mixed economy path from its independence in 1947 until 1991, when it opened up the economy for foreign investment. The focus on liberalisation, privatisation and globalisation after 1991 has dramatically transformed the country and integrated it with the global economy. Close to 30 years after liberalisation, there is a significant increase in the contribution of FDI to India's GDP thanks to a liberal foreign investment policy.

The key factors contributing to the 'India buzz' are:

- a young demographic profile of the country (over 50 per cent of the population are in the working age group of 15–59 years) forming a large pool of skilled manpower conversant in English;
- a stable political environment and responsive administrative set up supported by a well-established judiciary and a legal system based on common law;
- a labour force of nearly 530 million and low labour costs; and
- robust banking and financial institutions.

India's top five trading partners in 2019–2020 continue to be the US, China, the United Arab Emirates (UAE), Saudi Arabia and Hong Kong. China is the largest exporter to India followed by the US, UAE and Saudi Arabia. In recent times, Hong Kong, South Korea and Singapore have also emerged as significant exporters to India. India's largest export destination country continued to be the US in 2019–2020, followed by the UAE, China and Hong Kong. Major imports include crude petroleum, gold, petroleum products and coal, in addition to electronics, which recorded one of the fastest growth rates in 2019–2020.

In the World Bank's Ease of Doing Business rankings, India ranked 63rd in 2019, jumping up approximately 14 places from the previous year.

Despite global trade slowing down and protectionist winds blowing across countries, India, one of the Group of Twenty (G20) major economies, continues to remain an attractive market.

1.1 Editors' note[1]

This guide was being written over a period spanning pre-Covid and Covid-afflicted times. Hence, it would be remiss of us not to point out that the growth outlook has been sharply revised on account of the impact of Covid-19 on the global and Indian economy. This year India is likely to record its worse growth performance since liberalisation in 1991. As per the World Bank's recent *South Asia Economic Focus* report, India is forecast to grow at a meagre 1.5–2.8 per cent this fiscal year. This is as per pundits who expect other G20 economies to see similar slowdowns.

Persistent financial sector stress had already seen a lukewarm growth rate of 4.8–5 per cent in the last fiscal year of 2019–2020, ending on 31 March. The Covid-19 pandemic and the resultant lockdown has resulted in a shutting down of factories and offices, and suspending travel and also movement of goods. The impact on domestic demand and supply has been catastrophic, and this will be borne out by a spike in the unemployment rate, withering and spoilage of the seasonal rabi crop, and a sharp drop in household incomes.

While federal and state governments have tried to protect vulnerable blue-collar workers with regulations making pay cuts and retrenchments illegal, this may not be sustainable in the long term. Other regulatory interventions, such as a moratorium on loan servicing, a freeze on the fledgling insolvency regime and putting all Chinese investments in the approval route, have yet to positively influence 'Dalal Street'.[2]

Chapter 2: The business environment

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2.1 Government structure

India is a federal union with 28 states and eight union territories. At the union level there is a bicameral legislature comprising the Lok Sabha (House of the People) and the Rajya Sabha (Council of States), jointly comprising the Parliament. At the state level certain states have a bicameral legislature, that is, a legislative assembly and a legislative council, while others have a unicameral legislature, that is, only a legislative assembly.

Schedule VII of the Constitution of India comprises three lists: the union list, state list and concurrent list. The union list comprises all the matters that the Parliament has exclusive power to legislate, including, inter alia, items such as defence, regulating corporations, banking, foreign exchange and corporation tax. The state list comprises the matters that the state legislatures have exclusive power to legislate on, including, inter alia, trade and commerce, agricultural taxes, land and building taxes, stamp duty and local governmental issues. The concurrent list comprises matters that can be legislated by Parliament or the state legislatures (Parliament has primacy), including, inter alia, contracts, bankruptcy and insolvency, arbitration, employment and labour, factories and electricity. Moreover, Parliament has the residuary power to legislate on any matter that has not been covered by the state list or concurrent list. This includes foreign investment and residuary taxing powers.

1 The India section of this guide has been edited by Ramesh Vaidyanathan, Secretary, IBA Asia Pacific Regional Forum and Managing Partner, Advaya Legal, and Satyajit Gupta, Membership Officer, IBA Asia Pacific Regional Forum and Vice-President and Legal Head, EXL Service India.

2 India's Wall Street; the epicentre of India's financial markets.

2.2 Legal system

In India the primary sources of law are the Constitution of India, codified laws and customary law. In addition, concerned government departments make rules for various laws and also pass notifications, circulars and orders. The state legislatures and the state government bodies fulfil these roles for those items under the Constitution wherein the residuary law-making power is with the states.

Further, international treaties and judicial decisions interpreting the law are important secondary sources of law. The courts in India rely on the doctrine of *stare decisis* (adherence to judicial precedents), and a judgment by a higher court has binding value on a lower court. India follows a common law system of adjudication and judicial decisions in India rely on common law doctrines, especially in contract law. The Supreme Court in New Delhi is the apex court in India, followed by the State High Courts. The lowest level of the judiciary comprises various district courts and small causes courts located throughout the country. Additionally, specialised tribunals, like the Income Tax Appellate Tribunal (tax cases) and the National Company Law Tribunal (NCLT) (which replaced the Company Law Board for company law disputes with effect from 1 June 2016), have been set up to decide matters on particular subjects. Depending on the applicable legal provision, appeals from such tribunals may lie either with an appellate body, the High Court or the Supreme Court.

Most foreign judgments are not enforceable in India unless a fresh suit is filed upon the judgment in an Indian court. However, India recognises decrees passed by superior courts of certain countries, and decrees passed by superior courts in those countries are enforceable, provided that such decrees are not against India's public policy.

Chapter 3: Business and corporate structures

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3.1 Common forms of legal entities

A company continues to be the most common form of legal entity for business in India due to the ease of obtaining third-party capital and the general security provided by elaborate laws governing companies. Limited liability partnerships have also evolved as a preferred form for partnerships due to their flexibility in governance and certain tax advantages.

A private company enjoys a certain degree of flexibility, particularly concerning capital structure, governance and related party transactions, and the norms are stricter for a public or public listed company. Further, the government has created relaxed norms for one-person companies, small companies and startup companies, as compared to rules applicable to private companies or public companies, to promote new or smaller businesses.

3.2 Incorporation process

Incorporation timelines and processes have become more efficient in the last few years. Presently, it takes about two to three weeks after the submission of an incorporation form and related documents to incorporate a company. The process is relatively inexpensive and has no minimum capitalisation requirement. Very recently, the incorporation form (SPICe+ form) was revised. Now, in addition to incorporating the company, opening a bank account and obtaining certain regular registrations has been made possible as part of one form.

The SPICe+ form now acts as a single window application for:

- reservation and registration of the name of the new company;
- allotment of the Director Identification Number (DIN) for the first directors (for a maximum of three directors); if the proposed directors do not have a DIN, an application for obtaining a DIN will be included in the SPICe+ form;
- incorporation of the company;
- obtaining mandatory registrations with the Employees' Provident Fund Organisation and the Employees State Insurance Corporation;
- obtaining a mandatory Permanent Account Number and Tax Deduction and Collection Account Number;
- obtaining a mandatory bank account number; and
- obtaining a Goods and Service Tax Identification Number (if applied for).

This is expected not just to reduce timelines but also avoid coordination with various authorities and duplication of documentation.

For foreign shareholders incorporating a company in India, one thing to watch out for is the requirement that at least one director is resident in India at all times, and in particular, at the time of incorporation, at least one director, who is the authorised representative executing documents for company incorporation, should be an Indian citizen and resident.

3.3 Ongoing reporting and disclosure obligations

In the current business environment, the government is faced with twin objectives, which at times are divergent and therefore require the two to be balanced. These are: (1) to make it easy to do business in India; and (2) to increase vigilance and disclosure to prevent dubious or questionable operators. This has resulted in some instances of increased compliance requirements, particularly from a disclosure and liability perspective. Further, most disclosures have been shifted to online submissions, the latest being foreign investment filings. The key corporate compliance relates mainly to the below requirements.

3.3.1 Requirements under the Companies Act

Under the Companies Act, the reporting/disclosure requirements can be broadly categorised as: (1) periodic/mandatory filings, which include the filing of annual returns and other financial statements, disclosure of interest by directors and appointment of auditors; and (2) event-based filings, which include an intimation of the alteration of share capital, issuance of securities, creation and satisfaction of charges, and change in directors and key managerial personnel (KMP). The relevant filings are required to be made with the Registrar of Companies (ROC) within the prescribed timelines, and non-compliance may lead to fines or other penal implications.

3.3.2 Requirements under Securities and Exchange Board of India regulations

For listed companies, the Securities and Exchange Board of India (SEBI) has prescribed: (1) disclosures for a limited audit of quarterly financial statements and annual audit of financial statements; (2) time-bound disclosures for material information; and (3) any other material information that may have an impact on stock prices. The disclosures also differ based on the kind of debt or equity securities listed. The standards of disclosures are, in a way, subject to regular review by SEBI and often result in amendments in disclosure requirements.

3.3.3 Requirements under foreign exchange regulations

Any foreign investment in an Indian company (whether such an investment is made by a subscription of shares or transfer/acquisition of shares) is required to be reported to the Reserve Bank of India (RBI) in the prescribed form. The onus of such a filing is on the Indian entity receiving the foreign investment (in the case of an issue of shares) and on the resident transferee/transferor, as the case may be (in the case of a transfer of shares). In addition to these one-time filing requirements, any company that has received foreign investment is required to make mandatory annual filings on foreign investment it has received.

3.3.4 Other developments

Disclosure of significant beneficial ownership

With the intention of identifying the ultimate beneficiary shareholders, the Ministry of Corporate Affairs (MCA) in 2018 notified the Companies (Significant Beneficial Owners) Rules 2018 (the 'SBO Rules') to identify individuals/entities that have significant control over the affairs of a company. As per the SBO Rules, every individual who is acting alone or together, or through one or more persons or trust, holds directly or indirectly not less than ten per cent of the shares/voting rights in an Indian company or has the right to receive or participate in at least ten per cent of the total distributable dividend or any other distribution or has the right to exercise significant influence or control (directly or indirectly) over an Indian company is deemed a 'significant beneficial owner'. Such persons are required to make a declaration to the concerned investee company, specifying the nature of their interest and other particulars in the prescribed form within 30 days of acquiring significant beneficial ownership. The onus is also on the investee companies to take all necessary steps to identify if there is any individual who is a significant beneficial owner and cause such an individual to make the relevant declarations. The investee company is also required to notify such significant beneficial ownership to the ROC on the prescribed form. However, there are concerns raised by both domestic and foreign holders on the level of disclosures required under the SBO Rules.

Recent disclosure requirements for listed companies

With a view to enhancing the accountability of listed companies from an environmental, social and governance perspective, which has been SEBI's focus in recent years, SEBI has made it mandatory for the top 1,000 listed entities based on market capitalisation (the earlier requirement was limited only to the top 500 companies) to include a business responsibility report in their annual report describing the initiatives taken by them in these sectors. There has also been a tightening of disclosure norms around financial defaults involving listed companies. SEBI now requires: (1) disclosure of any default in payment of interest/instalment obligations on loans by such a company, where such a default continues beyond 30 days; and (2) disclosure by the promoter of the listed company of detailed reasons for creating an encumbrance on its shareholding, if the combined encumbrance by the promoter along with persons acting in concert with it equals or exceeds 50 per cent of their shareholding in the company or 20 per cent of the total share capital of the company.

3.4 Management structures

With the focus on having a robust corporate governance framework and ensuring transparency and accountability, the law provides for having independent directors, and the role of board committees and KMP, with an emphasis on board-managed companies.

Unlisted public companies with significant capital, turnover or outstanding loans are required to have at least two independent directors and one women director on the board of directors. For listed companies, the requirement is even higher, with up to half of the board required to be independent directors if it has an executive officer as the chair of the board. To further scrutinise the decisions, there are requirements for having mandatory committees of the board of directors, with the audit committee and nomination and remuneration committee being the key ones, with a defined scope of reference and requirement of independent directors on such committees. In addition, the Companies Act provides for designations of KMP for a company, which include chief executive officer (CEO), managing director, chief financial officer, company secretary, whole time directors and other officers not more than one level below the directors who are in the employment of the company the entire time and designated as a KMP by the board (typically other CEOs and CFOs). Such KMPs perform important designated management roles, and typically head respective teams in a company and answer directly to the board of directors. All listed companies and certain classes of public unlisted companies with a prescribed capital threshold are required to mandatorily appoint certain KMPs. Private companies and public companies falling below the stated financial thresholds are not subject these governance requirements and enjoy flexibility.

Other than legal requirements, one can observe a host of business and aspirational considerations in determining management structures. Investors or joint venture parties rely on a combination of having board representation and affirmative voting rights at shareholder level. Investors who are seeking these rights as investor protection tend to rely more on affirmative voting rights than a board seat. With the scaling of a business, particularly when raising substantial amounts of private capital and for companies going for listing, it is preferable to have professional senior management functioning under the board of directors. Founder's relevance, business continuity principles and succession planning are other relevant considerations.

3.5 Director, officer and shareholder liability

Indian law, based on common law principles, places a fiduciary duty on directors of a company to maintain the interests of the company and its stakeholders. In particular, the Companies Act codifies certain key duties of directors, including a duty to exercise their responsibilities with due and reasonable care, skill and diligence, and exercise independent judgement, as well as a duty not to become involved in a situation in which they may have a direct or indirect interest that conflicts with the interests of the company.

Where the Companies Act provides for offences by a company or an officer of the company who is in default, the executive directors, KMP or any other officer of the company who is charged with the concerned responsibility, or any other director who is aware of the contraventions or participated in the proceedings without objecting to the same, can be held liable. However, the Companies Act specifically provides for a safe harbour for independent directors or non-executive directors for any contravention by the company if it has occurred without their knowledge, consent or connivance, or where they have acted diligently. Similar principles are incorporated in other legislation, where the person in charge of and responsible to the company for the conduct of its business at the time of the commission of the offence, as well as other officers who are responsible for or aware of contraventions, may be held liable.

Indian companies generally do not ascribe liability on shareholders for the actions of a company, except in very limited circumstances where the piercing of the corporate veil is permitted. These are typically in cases involving fraud, evasion of tax or any other welfare benefits; setting up of a shell company as a subsidiary that has no independent existence; or if it is required in the public interest or to uphold public policy.

3.5.1 Recent developments

Amendments to the Companies Act

The MCA recently introduced amendments to the Companies Act whereby certain offences (eg, non-compliance with the filing requirement of annual returns/financials of a company and non-compliance with the requirements of the appointment of directors/number of directorships), which were earlier punishable with a fine and/or imprisonment, are now liable for a fine only. This implies that, where the fine amount was previously determined pursuant to adjudication by relevant company courts, the authorities (MCA/ROC) can now directly impose a fine, while imprisonment has been dropped. There are other proposed amendments pending before the Indian Parliament to decriminalise certain offences (eg, of provisions under the Companies Act relating to the transfer of securities, registration of charges/encumbrances created on assets and significant beneficial ownership) and reduce the amounts of penalties that may be imposed. These steps are being brought in to reduce the disproportionate exposure of directors/management and increase business confidence.

Penal proceedings

In view of recent insolvencies or financial distress, particularly in the financial sector, the government and law enforcement agencies (enforcement directorate and serious fraud investigation office) have, on several occasions, initiated penal proceedings against delinquent senior management. This has resulted in some clarity, streamlining and capacity building in the enforcement process, and has had an impact on overall enforcement risk analysis.

Insolvency and Bankruptcy Code, 2016

With the advent of the Insolvency and Bankruptcy Code, 2016 (IBC), investigations concerning financing irregularities are initiated as a matter of process, and are thereafter dealt with under relevant provisions of criminal law. To assist in the acquisition of insolvent companies, the IBC provides for a favourable concession that upon the change of control of the insolvent company, the liability of such a company for events prior to commencement of the corporate insolvency process ceases. However, any person who has been designated as 'officer-in-default' or was in any manner in charge of or responsible to the company for the conduct of its business shall continue to be liable.

Chapter 4: Takeovers (friendly M&A)

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Any investment in a listed company, including a transaction involving acquisition of control, is governed and regulated by the SEBI. The SEBI seeks to protect the interests of investors in securities and to regulate the securities market in India.

The SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 (the 'Takeover Regulations') regulate, inter alia, takeovers of listed Indian companies and open offer obligations. The Takeover Regulations seek to protect the interests of public shareholders and provide a transparent and equitable framework for the acquirer to acquire shares and public shareholders to exit the target company. The Takeover Regulations apply to any direct or indirect acquisition of shares, voting rights or control in a listed company. The Takeover Regulations provide for mandatory open offers, voluntary open offers and competing offers.

A mandatory open offer for 26 per cent of the shares of the target company is triggered in any acquisition resulting in the acquirer: (1) becoming entitled to 25 per cent of the voting rights in the target company; (2) already having acquired 25 per cent of the voting rights, acquiring a further five per cent of the shares or voting rights (creeping acquisition limit); (3) acquiring control of the target company; or (4) indirectly acquiring control over a holding company that effectively satisfies the foregoing thresholds. The creeping acquisition limit has been increased to ten per cent for the financial year 2020-21, in case of subscriptions by promoters.

Further, the Takeover Regulations lay down the parameters for determining the offer price and the process of understanding the open offer. The floor price of the open offer for an acquirer who has not bought any shares of the company previously, is higher than the negotiated price of volume weighted average market price for the previous 60 days from the trigger date (in case of frequently traded shares). To undertake an open offer, the acquirer is required to appoint a merchant banker, open an escrow account, prepare a draft letter of offer and seek in-principle approval from the SEBI, and advertise the schedule of activities in the open offer process through newspapers. The process starts with issuance of a public announcement in a prescribed format, followed by publication of a detailed public statement in the newspapers, and filing of the draft letter of offer with the SEBI. The tendering is initiated after dispatch of the letter of offer to the shareholders post-receipt of comments from the SEBI. In addition, the Takeover Regulations also provide for certain acquisitions that are exempt from the open offer obligation. These include, transfer between promoters, acquisitions through schemes of arrangement and the SEBI has recently issued an exemption for acquisition (through preferential allotment) of companies having stressed assets. The SEBI also has the power to give case-by-case exemptions. Further, there are certain reporting requirements under the Takeover Regulations, including, inter alia:

- for every acquirer, who by itself and through persons acting in concert acquires five per cent shares of the target listed company, to disclose the acquisition within two working days to the target listed company and all stock exchanges at which shares of the target listed company are listed;
- for every acquirer, who by itself and through persons acting in concent has already acquired five per cent shares of the target listed company, to disclose the acquisition of any further acquisitions amounting to two per cent of the shares of the target listed company; this disclosure must be made within two working days to the target listed company and all stock exchanges at which shares of the target listed company are listed;
- for every acquirer, who by itself and through persons acting in concent holds at least 25 per cent of the voting rights of the target listed company, to disclose its aggregate shareholding at the end of every financial year; and
- for the promoters of every listed company to disclose the details of shares of the listed company that have been encumbered, within seven days from the creation, invocation or release of the encumbrance to the listed company and all stock exchanges at which shares of the listed company are listed.

The SEBI has powers, inter alia, to investigate non-compliance; search and seize books, records, documents and registers; levy monetary penalties in specific instances; and direct the target company not to give effect to any transfer of shares acquired in violation of the Takeover Regulations.

In case of a primary investment into a listed company by preferential issuance of shares, in addition to the compliance for preferential allotment prescribed under the Companies Act, 2013, every listed company must comply with the requirements under Chapter V of the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018, inter alia, with respect to the eligibility criteria for the allottee, the pricing requirements and the lock-in period requirements.

In respect of mergers and acquisitions through stock transactions, the Companies Act, inter alia, provides for schemes of mergers or amalgamations ('Schemes') which require approval of the NCLT. The Companies Act also prescribes the steps to be taken by the NCLT for approving the Scheme. Once the NCLT passes an order approving the Scheme, the company must submit that order to the jurisdictional ROC. For regulating mergers and amalgamations of listed companies through Schemes in India, the SEBI has issued a circular dated 10 March 2017 on Schemes of Arrangement by Listed Entities (the 'SEBI Circular') to be read with provisions of the Companies Act. The SEBI Circular require inter alia (1) obtaining a no-objection certificate(s) of the relevant stock exchanges to the draft Scheme prior to submitting the Scheme to the NCLT; (2) a valuation report, if required; and (3) additional shareholders' approval for the certain Scheme.

Chapter 5: Foreign investment

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5.1 Foreign investment control/restriction

Foreign equity investment into an Indian company is regulated by the FDI policy issued by the government and exchange regulations issued by the RBI. The FDI Policy places limits for each sector, which is further categorised on the basis of the permissibility under the automatic route or the approval route. Investments falling under the automatic route can be made without the government's prior approval, whereas for investments under the approval route, prior approval of the relevant governmental/regulatory authority is required.

In India investments up to 100 per cent can be made under the automatic route in a majority of sectors, such as airports, assets reconstructions, cash and carry wholesale trading/wholesale trading, chemicals, coal and ignite, e-commerce (business-to-business), petroleum and natural gas, renewable energy, single brand product retail trading, power generation and hospitality.

In brownfield industries engaged in pharmaceuticals, healthcare or biotechnology, investments up to 74 per cent are permitted under the automatic route, while such investments are limited to up to 49 per cent in telecoms, defence and private sector banking. For investments beyond these limits, and in sectors such as multi-brand retail or print media, prior approval from the government is required. It is in such sectors that entering the Indian market by way of collaborations and joint ventures becomes a legal necessity.

While the government's approval is required only in limited cases, the process of seeking such approval has been significantly simplified by the setting-up of the foreign investment facilitation portal, which is a single point interface with the government that facilitates FDI approvals based on standard operating procedures.

Foreign investment is entirely prohibited in certain sectors. These include atomic energy, manufacturing of tobacco/tobacco products, chit funds, gambling, lottery, real estate business (except development of townships, construction of residential/commercial premises, roads or bridges, educational institutions, recreational facilities, city and regional level infrastructure, and real estate broking services).

The sector-wise categorisation is, in some cases, also supplemented with investment or performance-linked conditions. For example, foreign investments made for development of townships or real estate broking services are subject to a lock-in period of three years. Similarly, one of the conditions for investment in the cash and carry wholesale trading sector is that wholesale trading to companies that belong to the same group should be limited to 25 per cent of the total turnover of the wholesale venture with the group of companies taken together. Despite such conditions, India is an attractive destination for investors.

5.1.1 Tapping into the Indian market

Foreign investors can invest in equity or hybrid instruments that are compulsorily convertible into equity, such as preference shares, debentures and share warrants.

Investors looking to invest largely in listed Indian securities, government bonds, corporate bonds and units issued by investment vehicles can be registered with SEBI as foreign portfolio investors (FPIs). SEBI has put in place a consolidated framework setting out investment conditions and restrictions, general ongoing obligations, responsibilities and governance rules for FPIs.

There are individual and aggregate shareholding limits applicable to investments by FPIs in an Indian company. Investment by an FPI or its investor group is subject to a cap of ten per cent of the share capital or the value of any series of other instruments issued by the Indian company, as the case may be. Any investment above this threshold would result in the entire investment made by the FPI or the investor group being reclassified as FDI.

In addition to investing under the FDI and FPI regime, foreign investors can be registered with SEBI as a foreign venture capital investor (FVCI). However, FVCI's may only invest in securities issued by entities engaged in certain sectors, which include infrastructure (power generation and transmission), biotechnology, information technology-related hardware and software development, nanotechnology, seed R&D, R&D for new chemicals in the pharmaceuticals sector, dairy industry, poultry industry, production of bio-fuels and certain categories of hotel-cum-convention centres. In such permissible sectors, FVCI can invest by way of optionally convertible instruments.

In the recent past, the insolvency framework of India has created a stressed assets market. As lenders are looking to resolve non-performing assets, there is huge potential for foreign investors to acquire assets that have scope for revival at an attractive value. For this, collaborations, joint ventures and even investments through asset reconstruction companies or alternate investment funds (AIFs) have become relevant.

5.1.2 Recent developments

With the aim to making it easy to do business in the country, the government has removed several restrictions that inhibited growth and development of various sectors. Some important amendments recently made to the FDI Policy are discussed below.

Civil aviation

FDI up to 100 per cent is now allowed under an automatic route in the civil aviation sector.

Insurance intermediaries

To enable foreign brokerage firms to venture into the Indian insurance space, 100 per cent FDI in insurance intermediaries has been allowed. These intermediaries include insurance brokers, reinsurance brokers, insurance consultants, corporate agents, third-party administrators, surveyors and loss assessors.

As per the new policy, an insurance intermediary with a majority shareholding of foreign investors should have an Indian resident as its chair, CEO, principal officer or managing director. Such intermediaries are also required to acquire the prior permission of the authority concerned before repatriating dividends.

Single-brand retail trading

Previously, 30 per cent of the value of goods had to be procured from India if the single-brand retail trading entity had more than 51 per cent FDI. Further, as regards local sourcing requirement, the same could be met as an average during the first five years, and thereafter annually towards its India operations.

The new policy eases local sourcing norms and allows all procurements made from India by the single-brand retail trading entity for that single brand to be counted towards local sourcing, irrespective of whether the goods procured are sold in India or exported. Further, the cap of considering exports for five years has been removed to give an impetus to exports.

Until now, single-brand retail trading entities had to operate through bricks-and-mortar stores before retail trading their brand through e-commerce. To remove this artificial restriction, retail trading through online trade prior to opening physical stores has been allowed subject to the condition that such stores are opened within two years.

Mining

The government had permitted 100 per cent FDI under the automatic route for entities engaged in the sale of coal and coal mining activities. However, the relevant Indian laws imposed certain end-use restrictions on minerals extracted from a significant number of coal mines. In order to remedy this policy mismatch and provide operational flexibility, these domestic laws have been amended recently.

In the wake of the economic and financial crisis caused by the Covid-19 pandemic, India has revised its FDI policy, imposing stricter norms on foreign investments in Indian companies from an investor based out of bordering countries. Under the new rules, any foreign investment by a non-resident based out of a country that shares a land border with India will require the prior approval of the government irrespective of the sector into which the investment is being made. India shares a land border with Afghanistan (Restricted Country), Bangladesh, Bhutan, China, Myanmar, Nepal and Pakistan. This investment approval requirement also extends to: (1) those investments, where the beneficial owner (corporate or individual) is situated in the jurisdiction of a Restricted Country; or (2) a direct or indirect transfer of ownership of any existing or future investment, which results in the beneficial owner being from a Restricted Country.

5.2 Foreign exchange control

5.2.1 Pricing guidelines

One of the primary foreign exchange control norms governing foreign investments is the pricing guideline. Irrespective of the route or form of investment, pricing guidelines have to be abided by at the time of investment, as well as at the time of repatriation. Any investment coming into India must not be at a price lower than the fair market value. Similarly, any exit by a foreign investor should not be at a price higher than the fair market value. However, this pricing rule does not apply in the case of the transfer of investment between two foreign entities.

In the case of convertible instruments, the price or the formula pursuant to which the conversion would occur needs to be determined upfront; that is, at the time of issuing such instruments. This price/conversion formula cannot be lower than the prevailing fair market value.

5.2.2 Repatriation

All foreign investments are repatriable; although, in some cases, this may be subject to a certain lock-in period. For example, in construction-development projects that include the development of townships or construction of residential/commercial premises, a foreign investor's exit and repatriation of funds is subject to the completion of a lock-in period of three years. In any event, such lock-ins do not prevent a buy-back or dividend payout to the foreign investor, as long as applicable taxes are paid.

5.2.3 Reporting requirements

Reporting requirements in the case of foreign investments are fairly straightforward. In the case of an acquisition, the Indian company receiving foreign investment is required to report the same to the RBI in e-Form FC-TRS within 30 days. Similarly, in the case of the issuance of securities, a report in e-Form FC-GPR is required to be filed with the RBI within 30 days from the date of issue of shares. In addition to the above, the Indian company is required to report its foreign assets and liabilities in e-Form FLA on an annual basis.

The authorised dealer bank of the Indian company is authorised to process these forms, which further simplifies this process and prevents a bottleneck at the RBI.

5.3 Key tax incentives

Key tax incentives that are available to foreign investors under the tax regime are summarised below.

5.3.1 Exemption for the specified income of sovereign wealth funds

The Finance Act, 2020 provides for a 100 per cent tax exemption in respect of interest, dividend and capital gains income earned by sovereign wealth funds from any investment made in infrastructure and other notified sectors in India. In order to avail the exemption, the investment must be made on or before 31 March 2024 and held for at least three years. The sovereign wealth fund is required to comply with certain specified conditions.

5.3.2 Abolition of dividend distribution tax

Under Indian tax laws domestic companies were required to pay dividend distribution tax (DDT) at an effective rate of 20.56 per cent on dividend payments. Such a dividend was then exempt in the hands of shareholders. The Finance Act, 2020 has abolished DDT and instead taxes dividends in the hands of shareholders. Under the DDT regime foreign investors faced difficulty in claiming credit for DDT in their home jurisdictions. Further, they could not avail concessional tax rates on dividend income as provided in India's tax treaties (which typically vary between five and 15 per cent). Accordingly, this amendment is expected to benefit foreign investors as the return on equity in Indian companies should improve.

5.3.3 Favourable tax regime for FPIs

Indian tax laws provide for a favourable tax regime for FPIs:

- interest income earned by FPIs from investments in government securities and rupee-denominated bonds issued by Indian companies is taxed at a concessional rate of five per cent, subject to the fulfilment of certain conditions;
- dividend income earned by FPIs is taxable at the rate of 20 per cent; post the abolition of DDT, FPIs would be eligible to avail concessional tax rates on dividend income as provided in India's tax treaty with their home jurisdiction;
- long-term capital gains income earned by FPIs is taxable at the rate of ten per cent; and
- capital gains income arising from the transfer of interest in specified categories of FPIs is exempt from tax in India.

5.3.4 Concessional tax rate of five per cent on interest income of non-FPI foreign investors

Foreign investors (other than FPIs) are also entitled to avail of a concessional tax rate of five per cent in respect of interest income, subject to the fulfilment of certain conditions. On a general basis, the interest income should relate to a foreign currency loan extended to an Indian company or specified foreign currency/rupee denominated bonds issued by an Indian company. The rate of interest should not exceed the all-in-cost ceilings specified by the RBI under external commercial borrowings (ECB) regulations.

5.3.5 Comprehensive treaty network

India has a wide network of tax treaties. These treaties protect the income of foreign investors from double taxation and generally provide for concessional tax rates in respect of interest income and dividend income. Certain tax treaties also exempt capital gains income of foreign investors from Indian tax, subject to the fulfilment of certain conditions. Additionally, these treaties protect foreign investors from discriminatory taxation in India and contain measures for the initiation of a mutual agreement procedure between India and the home jurisdiction of the foreign investor in certain circumstances (eg, for the elimination of double taxation or for issues relating to the interpretation of the tax treaty).

5.3.6 Availability of concessional tax rates

Entities set up by foreign investors to undertake business activities in India may be entitled to avail of concessional tax rates/tax holidays provided under Indian tax laws. The tax laws were recently amended to allow new domestic manufacturing companies (set up and registered on or after 1 October 2019 and commencing manufacturing on or before 31 March 2023) to opt for a concessional tax rate of 15 per cent. Similarly, existing domestic companies have been allowed to opt for a concessional tax rate of 22 per cent. To avail the concessional tax rates, such companies are required to give up specified deductions, such as additional depreciation of 20 per cent on new plants and machinery available to manufacturing companies/companies engaged in the generation/distribution of power.

Companies not opting for concessional rates are entitled to avail of certain deductions/exemptions, for instance, additional depreciation as referred to above; deduction for investment in new plants and machinery in notified states; certain kinds of scientific research-related expenditure; expenditure on specified business; and expenditure on agricultural extension and skill development projects.

Chapter 6: Restructuring and insolvency

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6.1 Insolvency and Bankruptcy Code

In late 2016, the Indian corporate insolvency regime was repealed and replaced by the IBC, which provided for certain novel features such as a creditor-in-possession model, time-bound insolvency and mandatory reference to liquidation upon failure of insolvency resolution. The enactment of the new insolvency law was primarily driven by rising 'non-performing assets' in the Indian banking system, which had turned into a crisis.

A stressed company (the 'corporate debtor') may be placed under the corporate insolvency process prescribed under the IBC through an application filed by any creditor or by the corporate debtor itself in case of a default of INR 100,000 (approximately $1,300) or more. Once the insolvency application is admitted, an 'interim resolution professional' (akin to an administrator) is appointed and takes over the management of the corporate debtor; its board of directors is immediately suspended. The interim resolution professional issues a public notice and invites claims from the creditors of the corporate debtor. Once the claims are received, the interim resolution professional verifies and admits the claims, and constitutes the 'committee of creditors' of the corporate debtor. The committee of creditors, usually comprising the financial creditors (discussed below), oversees the key decisions of the interim resolution professional/resolution professional, including the process to invite bidders (known as resolution applicants) to place their bids (resolution plans) for the corporate debtor.

The IBC has divided creditors into two broad categories: (1) financial creditors, which include traditional lenders lending for time value of money; and (2) operational creditors, which include trade creditors, workers and government. While drafting the IBC, law-makers were of the view that the committee of creditors must consist of members with the capability to assess the viability and modify existing liabilities in negotiations. Typically, operational creditors are not in a position to do this. Hence, the law-makers felt that the committee of creditors should be restricted to financial creditors.[3] In view of this rationale, the Supreme Court has upheld the differential treatment accorded to financial creditors and operational creditors under the IBC.[4]

The differential treatment led to the National Company Law Appellate Tribunal, the appellate authority under IBC, to hold that operational creditors should be provided equitable treatment; that is, they should be required to take the same percentage haircut as the financial creditors under a resolution plan providing for the settlement of all creditor claims.[5] However, this principle was overturned by the Supreme Court, which allowed for differential treatment for different creditor classes and held that, ultimately, the wisdom of the committee of creditors must prevail.[6]

As aforementioned, the purpose of the corporate insolvency process is insolvency resolution of the corporate debtor through a resolution plan provided by a resolution applicant. The resolution plan must provide for the corporate debtor as a going concern. This 'going concern' condition has restricted transaction structures that may be employed by bidders and compels them to take on the corporate debtor's liabilities. This has naturally raised the question of the treatment of contingent liability under the resolution plan. The IBC requires creditors to file their claims with the interim resolution professional, but does not stipulate what happens to claims that are not filed with the interim resolution professional. The IBC further requires that claims be filed as of the 'insolvency commencement date'. Accordingly, it is (or was) not clear what should be done in respect of claims that may not be crystallised as of the insolvency commencement date. The resolution applicant requires a 'fresh slate' or a complete settlement of all such claims so as to be sure that the asset bought by it will be able to be revived and will not be subject to antecedent claims, even after coming out of insolvency. This issue was analysed by the Supreme Court in the case of the *Committee of Creditors*

3 The *Report of the Bankruptcy Law Reforms Committee Volume I: Rationale and Design*, p 84.

4 *Swiss Ribbons Private Limited v Union of India* (MANU/SC/0079/2019).

5 *Standard Chartered Bank v Satish Kumar Gupta, RP of Essar Steel Ltd & Ors* (Company Appeal (AT) (Ins) No 242 of 2019; Order dated 4 July 2019).

6 *Committee of Creditors of Essar Steel India Limited v Satish Kumar Gupta* (Civil Appeal No 8766-77 of 2019; Order dated 15 November 2019).

of Essar Steel India Limited v Satish Kumar Gupta,[7] where the Supreme Court agreed that the resolution applicant requires a fresh slate and therefore must know what payment is required. Accordingly, the resolution applicant must ascribe a value to contingent claims as well and admit the same so that they may be dealt with under the resolution plan.

Another unique requirement is section 29A, which prescribes certain eligibility criteria for prospective resolution applicants. These eligibility criteria are required to be met by the resolution applicant, persons acting jointly or in concert with the resolution applicant, 'connected persons' of the resolution applicant (which includes its promoters, management and their holding company, subsidiaries and related parties). Certain limited carve-outs are available for financial entities, the acquirer of a company under insolvency and so on. The eligibility criteria include not being an undischarged insolvency, not having or controlling a company that has an account declared a non-performing asset for more than one year, not being convicted of certain specified offences, not being prohibited from accessing the securities market and not being disqualified to act as a director. Section 29A has been a leading cause for litigation in IBC cases, and in many instances has led to protracted litigation leading to delay in insolvency resolution. The Supreme Court has attempted to rationalise the use of section 29A by: (1) streamlining its usage by bidders to maintain the time-bound nature of IBC transactions;[8] and (2) restricting the scope of 'related party' and 'relative' to parties connected with the business activity of the resolution applicant.[9] However, there is still ambiguity regarding the scope of section 29A due to its broad language.

The IBC was amended in August 2018 to provide for the withdrawal of corporate insolvency proceedings with the consent of 90 per cent of the financial creditors. The regulator stipulated that such a withdrawal may only occur prior to the issuance of an invitation to prospective bidders. However, subsequently, this timeline has also been held to be directory, and the withdrawal of IBC proceedings was recently allowed when a resolution plan approved by the committee of creditors was pending the approval of the adjudicating authority.[10]

There are numerous other aspects of the IBC from the perspective of various stakeholders (eg, the financial creditors, operational creditors, resolution applicants and erstwhile directors), which present their own intricacies.

6.2 Prudential Framework for Resolution of Stressed Assets

The regime for pre-IBC debt restructuring and resolution has also undergone a material change in recent times. Under the power granted to the RBI at the same time as the enactment of the IBC, the RBI issued a circular dated 12 February 2018 (the '12 Feb Circular') laying down a radically new framework for stressed assets resolution, and repealing all previously issued debt restructuring mechanisms, such as corporate debt restructuring, strategic debt restructuring and scheme for the sustainable structuring of stressed assets. However, the 12 Feb Circular was challenged by several industries, and, due to its features, such as

7 Order dated 15 November 2019 in Civil Appeal No 8766-77 of 2019.

8 *Arcelor Mittal India Private Limited v Satish Kumar Gupta and Ors*; Supreme Court Order dated 4 October 2018.

9 *Swiss Ribbons Private Limited v Union of India* (MANU/SC/0079/2019).

10 *Satyanarayan Malu v SBM Paper Mills Ltd* (MA 1396/2018,827/2018, 1142/2018 and 828/2018 in CP (IB)-1362(MB)/2017; Order dated 20 December 2018).

mandatory reference to the IBC in the case of failure to resolve stress, ultimately to be *ultra vires* the powers granted to RBI by the legislature.[11]

The RBI has now replaced the 12 Feb Circular with a new Prudential Framework for the Resolution of Stressed Assets issued pursuant to its circular dated 7 June 2019 (the '7 June Framework'). The 7 June Framework applies to banks and certain categories of financial institutions and non-banking financial institutions. Certain provisions also apply to asset reconstruction companies.

The 7 June Framework has attempted to rectify a number of pitfalls of the 12 Feb Circular, such as a lower consent threshold for approving a resolution plan and no mandatory reference to the IBC. The framework also provides for the mandatory execution of an inter-creditor agreement between all creditors of a debtor upon default in order to review the situation and arrive at a future course of action (whether it be resolution or recovery).

The framework provides for various means of implementing a resolution plan involving a change in ownership, restructuring, one-time settlement and so on. In this regard, it is pertinent to note that provisional norms may make it unattractive for lenders to approve a resolution plan that involves the continuation of the same promoter. However, in case of a resolution plan to qualify for 'change in ownership', the new acquirer must not be disqualified under section 29A of IBC nor be a person from the existing promoter group.

The framework also provides for measures such as increased provisioning in the case of failure to resolve stress within the stipulated timeline, the prudential norms or the pricing norms for the issuance of securities as part of the resolution plan.

All in all, the 7 June Framework provides a holistic paradigm for resolving stressed debt without resorting to IBC proceedings and a last resort to promoters to turn their companies around. Although resolutions under the 7 June Framework do not benefit from the numerous exemptions available to IBC resolutions, significant interest has been seen in pre-IBC resolutions under the 7 June Framework due to the flexibility it affords.

Chapter 7: Employment, industrial relations, and work health and safety

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7.1 Labour laws in India

Liberalisation has helped India to establish its identity on the world map in terms of business operations. While focusing on economic development and increasing job opportunities, it is essential to also consider the aspect of conditions of work. The increased production capacity of a nation is attributable to numerous factors, including investor-friendly policies, reduction of procedural

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11 *Dharani Sugars and Chemicals Limited v Union of India & Others* (Transferred Case (Civil) No 66 of 2018 in Transfer Petition (Civil) No 1399 of 2018; Order dated 2 April 2019).

hurdles, incentives and availability of labour. The industrial and other valuable output generated are the fruits of the efforts contributed by employees exercising their skills.

Coming from a socialist/mixed economy background, the Indian legislature has laid down a framework of labour regulations in order to ensure the social security of blue-collar employees in particular. The entities interested in doing business in India are required to abide by all the necessary compliance and directions issued under the provisions of the applicable labour laws, non-compliance with which may result in penal consequences.

7.1.1 Applicable labour and employment laws

Laws related to wages

Workers work to earn a livelihood for themselves in the form of salaries or wages, which are the amounts, in the form of emoluments, paid periodically to employees to compensate for their labour for the duration served. Indian legislature aims at ensuring the payment of wages to those who have expended their labour, energy and effort to contribute towards the business of their employers.

With a view to ensuring that wages are paid to workers, laws such as the Payment of Wages Act, 1936 append the responsibility of an employer to fix wage period, the time period for payment of wages, and deductions thereto in respect of their workers. In addition, laws such as the Minimum Wages Act, 1948 have been enforced to standardise minimum wages, which must be paid to skilled and unskilled workers. The law also mandates the payment of a bonus, which is 8.33 per cent of the salary or wage earned by the employee during a financial year, to the employee on the basis of production or productivity in every factory and to every other establishment where 20 or more workers are employed under the provisions of the Payment of Bonus Act, 1965.

Recently, the federal government has enacted a Code on Wages 2019, proposed to replace and consolidate the above laws. The code is expected to be notified once the minimum wages' calculations are arrived at, and the delegated legislation put in place.

Laws related to social security/statutory contributions

Owing to financial issues, workers are often faced with numerous challenges on account of the subsistence, health, education and wellbeing of themselves and their dependents.

In order to address such concerns Indian law has various provisions for social security cover to workers, such as workmen's compensation covered under the Workmen's Compensation Act, 1923 to help workers and/or their dependents in the case of accidents arising out of and in the course of employment; benefits to employees in the case of sickness, maternity and employment injury by establishments employing more than ten persons in the form of employees' state insurance covered under the Employees' State Insurance Act, 1948; provision of provident fund pension funds and a deposit linked insurance fund for employees in factories and other establishments employing 20 or more persons under the Employees' Provident Fund and Miscellaneous Provisions Act, 1952; and gratuity, which is a reward for long service, as a statutory retiral/exit benefit to workers who have rendered continuous service of five years or more.

Several laws, such as the provisions of the Factories Act, 1948, and state-specific shops and establishment acts, lay down guidelines for adequate safety measures, working hours, leave, holidays, hygienic work environment, permissible working hours for women and so on. The Contract Labour (Regulation and Abolition) Act, 1970 was promulgated to regulate the employment of workers by contractors in establishments, while the Building and Other Constructions Workers (Regulation of Employment and Conditions of Service) Act, 1996 controls the employment and conditions of service for workers engaged in the construction of buildings and other construction workers, focusing on their safety and health. The Child Labour (Prohibition and Regulation) Act, 1986 was enacted to prohibit the engagement of children below the age of 14 in factories, mines and hazardous employment, and to regulate their conditions of work.

With the objective of promoting the equality of women in all spheres of life, including employment, and to avoid discrimination against women, there are various laws to ensure equal pay to men and women for the same work (Equal Remuneration Act, 1976); to regulate the employment of women for a certain period before and after childbirth (Maternity Benefit Act, 1961); and to protect against sexual harassment of women at the workplace (Sexual Harassment of Women at Workplace (Prevention, Prohibition and Redressal) Act, 2013).

In order to secure industrial peace and harmony, the legislature has enforced laws such as the Industrial Disputes Act, 1947, with the objective of providing a procedure for the resolution and settlement of industrial disputes by negotiation; and the Industrial Employment Standing Order Act, 1946, with the aim of imposing a duty on employers to lay down the conditions of employment and communicate the same to workers in their employ.

7.2 Work permits

India has a complicated visa regime, which is approval-orientated.

The government issues an 'E' visa for foreigners seeking employment in the country. It is important to note that the individual applicant must have an employment contract directly with the Indian entity.

Categories of workers eligible for an 'E' visa include:

- consultants who are paid a fixed sum versus a monthly salary;
- independent consultants in highly skilled fields, such as engineering, accounting and medicine;
- individuals who provide training or knowledge transfer to an Indian company for which the company pays a fee or royalty to the employer of the individual; and
- senior management or specialists who are transferred to India for a specific project or management assignment.

Just because someone is able to work in one of these areas does not guarantee acceptance. Each applicant should also be able to prove:

- the worker is a highly skilled professional working under a contract in a technical job, managerial position or senior executive;
- the job offered to the foreign worker cannot be filled by a local worker; and
- the worker will make more than the threshold pay.

Chapter 8: Tax law

Ravi S Raghavan, Majmudar & Partners, Mumbai

8.1 Taxes applicable to individuals (employees)

Tax rates are applicable for the financial year 2020–2021 pertaining to the period 1 April 2020 to 31 March 2021:

Total income (INR)	Tax rates (%)
Up to 250,000**	Nil
250,001 to 500,000	5
500,001 to 1,000,000	20
1,000,001 and above	30

Alternatively, on the satisfaction of certain prescribed conditions, an individual may opt to compute tax in respect of total income (without considering prescribed exemptions/deductions), as per the following rates:

Total income (INR)	Tax rates (%)
Up to 250,000**	Nil
250,001 to 500,000	5
500,001 to 750,000	10
750,001 to 1,000,000	15
1,000,001 to 1,250,000	20
1,250,001 to 1,500,000	25
1,500,001 and above	30

**For a resident individual aged 60 or above, but less than 80, the basic exemption limit is INR 300,000.

A surcharge will be applicable at the following rates:

Sl No	Total income (INR)	Surcharge (%)
1	More than 5,000,000, but less than 10,000,000	10
2	More than 10,000,000, but less than 20,000,000	15
3	More than 20,000,000, but less than 50,000,000	25
4	More than 50,000,000	37
Health and education Cess at 4% will be applicable		

8.2 Taxes applicable to businesses

Resident Indian companies (RIC) that: (1) were set up after 1 October 2019; (2) are engaged only in the business of manufacture or production of articles or things (including generation of electricity); and (3) commenced manufacturing/production before 31 March 2023 have the option to be taxed at the rate of 15 per cent, provided they do not claim specified benefits or deductions. A surcharge of ten per cent and Cess at four per cent will be applicable.

RICs that were set up after 1 March 2016 and are engaged only in the business of manufacture or production have the option to be taxed at the rate of 25 per cent, provided they do not claim any specified benefits or deductions. A surcharge will be applicable at the following rates:

Sl No	Total income (INR)	Surcharge (%)
1	More than 10,000,000, but less than 100,000,000	7
2	More than 100,000,000	12
Cess at 4% will be applicable		

RICs not engaged in manufacturing or production have the option to be taxed at the rate of 22 per cent, provided they do not claim any specified benefits or deductions. A surcharge will be applicable at the rate of ten per cent on income tax. Cess will be applicable at the rate of four per cent.

RICs whose total turnover or gross receipts in the financial year 2018–2019 does not exceed INR 4,000m will be taxable at the rate of 25 per cent. A surcharge will be applicable at the rate of ten per cent. Cess will be applicable at the rate of four per cent.

RICs which are not covered under the previous paragraphs will be taxed at the rate of 30 per cent. Surcharge and cess will be applicable as above.

Foreign companies are taxable in India at the rate of 40 per cent. A surcharge is applicable at the following rates:

Sl No	Total income (INR)	Surcharge (%)
1	More than 10,000,000 but less than 100,000,000	2
2	More than 100,000,000	5
Cess at 4% will be applicable on income tax, inclusive of the surcharge		

Firms (including limited liability partnerships) will be taxable at a rate of 30 per cent. A surcharge is applicable at the rate of 12 per cent where the total income exceeds INR 10m. Cess at four per cent will be applicable on income tax, inclusive of the surcharge.

8.3 Other taxes

8.3.1 Royalties and fees for technical services

Under the IT Act, payments made by RICs to a non-resident that are in the nature of royalties and fees for technical services will be taxable in India at the rate of ten per cent (excluding the surcharge and education CESS) and the RIC is liable to withhold tax on such payments.

8.3.2 Dividends

With effect from 1 April 2020, RICs are not required to withhold dividend distribution tax prior to distributing profits. Such dividends will be taxed in the hands of shareholders at the applicable tax rates.

8.3.3 Income from capital gains

Income earned from the transfer of capital assets will be taxed under the head 'capital gains'. The tax rates depend on whether the gains are short-term and/or long-term capital gains. 'Short-term capital asset' means a capital asset held by a taxpayer for not more than 24 months immediately prior to its date of transfer. An asset other than a short-term capital asset is regarded as a long-term capital asset. The rate of long-term CGT is between ten and 20 per cent (excluding the surcharge and education CESS), and the rate of short-term CGT is between 15 and 30 per cent (for residents, excluding the surcharge and education CESS) and 40 per cent (for non-residents, excluding the surcharge and education CESS).

8.3.4 Minimum alternate tax

Minimum alternate tax (or an alternate minimum tax) will be applicable at the rate of 18.5 per cent (plus the applicable surcharge and CESS) on the adjusted book profits of RICs only when the tax payable under the normal income tax provisions is less than 18.5 per cent of their adjusted book profits.

8.3.5 Buy-back of shares

An additional tax of 20 per cent is payable by an RIC that is buying back shares from its shareholders. This tax is payable by the RIC on the difference between the amount paid for the buy-back and the issue price of the shares. The buy-back amount received is exempt from tax in the hands of the recipient.

8.3.6 Indirect transfer provisions

Under the IT Act, the income of a non-resident will be deemed to accrue or arise in India if it arises, directly or indirectly, through or from any business connection, property, asset or source of income or from a transfer of a capital asset (shares or other interest) situated in India. The indirect transfer provisions are triggered if the value of the assets located in India exceeds INR 100m and the assets in India represent at least 50 per cent of the value of all the assets owned by the offshore transferor company.

8.3.7 Income from other sources

Any income that is not covered under any of the specific heads of income will be liable to tax under the head income from other sources. Expenditure that is incurred wholly and exclusively for earning such income will be allowed as a deduction.

8.3.8 Thin capitalisation rules

Interest expenses paid to an associated enterprise shall be restricted to 30 per cent of its earnings before interest, taxes, depreciation and amortisation or to the actual amount of interest paid to an associated enterprise, whichever is less.

8.3.9 Equalisation levy

An equalisation levy of six per cent will be applicable on the total consideration received or receivable by a non-resident not having a permanent establishment in India for providing online advertising, digital advertising, or any other facility or service for online advertisements as may be specified by the government.

8.3.10 Permanent Account Number

Any person who makes a payment to a non-resident or a resident that is chargeable to tax in India will be liable to withhold taxes at source from such payments in accordance with the relevant provision of the IT Act. If the Permanent Account Number is not available, a higher tax withholding rate of 20 per cent will be applicable. However, this provision is relaxed if certain conditions are fulfilled.

8.3.11 Goods and services tax

The GST is a VAT ranging between five per cent and 28 per cent (on both goods and services) which is levied at all points in the supply chain, with an input tax credit allowed subject to the satisfaction of conditions.

Chapter 9: Intellectual property

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Innovation, manufacturing and the services industry are key drivers of the Indian economy and business ethos. International outbound investment from India has also increased, which has led to a significant amount of technology transfer through industrial acquisitions.

It is advisable for foreign companies doing business in India, as well as contemplating to do business in India, to register their intellectual property rights at the outset so as to enjoy unhindered protection and avoid any infringement issues at a later date. Indian law allows foreign companies to register all forms of intellectual property, including patents, trademarks, designs, copyrights, geographical indications, semiconductors and plant varieties. All forms of copyright, trademark, design and patent applications can be filed online. Applicants that do not have a registered place of business in India are required to file applications through an Indian attorney or agent.

India is a member of the following International Treaties and Conventions:

Sl no	Treaty	Signature	Signing of Indian Instrument of Accession	In force in India
1.	Paris Convention	20 March 1883	Accession: 7 September 1998	7 December 1998
2.	Berne Convention	9 September 1886	Declaration of Continued Application: 23 April 1928	1 April 1928
3.	Patent Cooperation Treaty	19 June 1970	Accession: 7 September 1998	7 December 1998
4.	Madrid Protocol	1 April 1996	Accession: 8 April 2013	8 July 2013
5.	Locarno Agreement	8 October 1968	Accession: 7 June 2019	7 September 2019
6.	Nice Agreement	17 June 1957	Accession: 7 June 2019	7 September 2019

9.1 Patents

In India the law relating to patents is governed by the Patents Act, 1970 as amended by the Patents (Amendment) Act, 2005 and the Patents Rules, 2003 (as amended in 2016). The term of every patent granted in India is 20 years from the date of filing the application. For the National Phase application under the Patent Cooperation Treaty (PCT), the term of a patent will be 20 years from the date of international filing.

A patent application can be filed by any person, either a citizen of India or not, either alone or jointly with any other person at the earliest possible date to register the priority of invention. For foreign companies or foreign nationals, the applicant must appoint a registered agent or representatives in order to be able to furnish an address for service in India.

The types of patent applications that can be filed under Indian patent law are the Provisional Application, Ordinary Application, Convention Application, PCT National Phase Application, PCT International Application, Application for Patent of Addition and Divisional Application. The priority of the filed application can be claimed within 12 months from the earliest corresponding application in the convention country/PCT. The minimum filing requirements for an applicant include names, addresses and nationalities (for PCT applicants) of all the inventors and applicants, and also of the applicants in the convention country.

After the grant of patent, every patentee must maintain the patent by paying annual renewal fees. For the first two years there are no renewal fees; renewal fees are payable only from the third year onwards. If not paid, the patent will cease. One exception is in the case of a patent of addition, where no annuities are payable. To provide an update on the working of patents, every patentee every licensee is required to furnish, at the end of the financial year, a statement as to the extent to which the invention has been worked on in India on a commercial basis. If the applicant/inventor is residing in India, and decides to directly file a patent application in a foreign country without first filing in India, then it is compulsory for the inventor to obtain a foreign filing licence from the Indian Patent Office (IPO).

9.2 Trade marks

The law governing trademarks in India is the Trade Marks Act, 1999 (as amended by the Trade Marks (Amendment) Act, 2010) and the Trade Marks Rules, 2017. The term of protection for a trademark application is ten years, which can be renewed for additional ten-year periods. Any person claiming to be a proprietor of a mark can file a trademark application with the Trade Marks Registry, and Foreign companies/nationals not living in India must appoint a registered agent or representative to furnish an address for service in India.

The kinds of trademarks that can be filed in India are the word mark, device mark, service mark, collective mark, certification mark, shape mark and sound mark. The international classification of goods is used, and separate applications must be filed for goods falling in different classes. Currently, the 11th edition of the Nice Classification passed by the WIPO is in force in India. Ownership of a trademark in India is determined on a first-to-use basis. Unlike the law on patents or designs, trademark law mandates the first-to-use rule over the first-to-file rule.

Once the application is filed and where all formalities are in order, the application will be examined. Once examined, the Trade Mark Office will either accept the application and publish it in the journal or issue an examination report citing the following:

- procedural objection, where power of attorney (POA) has not been filed; goods/service do not fall under the applied class and so on; and
- substantive objections, which are objections put forth in the light of absolute (section 9) and relative grounds (section 11) of refusal.

Applications that have been accepted are advertised in the Trade Marks Journal, and opposition may be filed within four months of the date of advertisement.

The exclusive rights obtained by registration cannot operate against the rights of the prior user of the same or similar trademarks in respect of goods in relation to which the impugned mark has continuously been used for dates prior to the use of registered mark or date of the registration of the registered mark. However, section 12 of the act provides for the registration of a trademark in the case of its honest concurrent use by providing that

> 'in the case of honest concurrent use or of other special circumstances which in the opinion of the Registrar, make it proper so to do, he may permit the registration by more than one proprietor of the trade marks which are identical or similar (whether any such trade mark is already registered or not) in respect of the same or similar goods or services, subject to such conditions and limitations, if any, as the Registrar may think fit to impose'.

Thus, the Registrar is not obliged to register such an honest concurrent user; it depends upon his/her discretion.

A registered trade mark can be assigned with or without the goodwill of the business concerned, and the registered trade mark may be rectified (removal of mark) from the register on the ground of wrongly remaining on the register, or non-use of a mark for a continuous period exceeding five years and three months before the filing of the rectification application from the date of registration unless there are special circumstances excusing non-use.

9.3 Copyright

In India the law governing copyright is the Copyright Act, 1957 and the Copyright Rules, 2013. The term of protection for a copyright is the life of the author plus 60 years from the beginning of the calendar year following the year in which the author dies. Any individual who is an author, rights owner, assignee or legal heir may file a copyright application and foreign companies/nationals not living in India must appoint a resident agent or representative in order to be able to furnish an address for service in India.

However, it should be noted that copyright protects expressions, not ideas. There is no copyright protection for ideas, procedures and methods of operation or mathematical concepts as such, and the registration of a copyright is not mandatory in India. The acquisition of copyright is automatic; it does not require any formality. Copyright comes into existence as soon as a work is created, and no formality is required to be completed for acquiring copyright. However, a certificate of registration of copyright and the entries made therein serve as *prima facie* evidence in a court of law with reference to a dispute relating to the ownership of copyright. However, in 2012, in the case of *Dhiraj Dharamdas Dewani v Sonal Info Systems Pvt Ltd and Ors,* the Bombay High Court held that

> 'in the absence of registration under section 44 of the Act by the owner of the copyright it would be impossible to enforce the remedies under the provisions of the Act against the infringer for any infringement under section 51 of the Act. Hence registration of copyright was compulsory or mandatory for taking recourse to the provisions of the Act'.

The author of a work has the moral right to claim authorship of the work and to restrain or claim damages in respect of any distortion, mutilation, modification or other acts in relation to the said work that is done before the expiration of the term of copyright if such distortion, mutilation, modification or other act would be prejudicial to his/her honour or reputation. Moral rights are available to the authors even after the economic rights are assigned.

The author of a work is usually the 'first owner' of the work. In certain circumstances, section 17 of the Copyright Act determines who may be regarded as the 'first owner' of a copyrighted work.

The provisions of section 52 of the Copyright Act provide for certain acts that would not constitute an infringement of copyright, namely fair dealing with a literary, dramatic, musical or artistic work not being a computer program for the purposes of:

- private use, including research;
- criticism or review;
- reporting current events in any print media or by broadcast or in a cinematographic film or by means of photographs;
- a judicial proceeding or report of a judicial proceeding;

- reproduction or publication of a literary, dramatic, musical or artistic work in any work prepared by the Secretariat of a legislature or, where the legislature consists of two Houses, by the Secretariat of either House of the Legislature, exclusively for the use of the members of that legislature;
- reproduction of any literary, dramatic or musical work in a certified copy made or supplied in accordance with any law for the time being in force;
- the reading or recitation in public of any reasonable extract from a published literary or dramatic work;
- the publication in a collection, mainly composed of non-copyright matter, bona fide intended for the use of educational institutions; and
- the making of sound if made by or with the licence or consent of the owner of the right in the work.

9.4 Designs

In India the Designs Act, 2000 and the Designs Rules, 2001 govern the law relating to industrial designs. The term of protection is ten years from the priority date, which can be renewed (once) for a period of five years. Any person claiming to be the proprietor of a design, whether Indian or a foreign national, can file a design application in India. Foreign companies/nationals not living in India must appoint a resident agent or representative to furnish an address for service in India. It is mandatory to provide an address for service, or else the IPO shall not proceed with the application.

Prior publication, registration or public use anywhere in the world destroys the novelty of a design. This affects the registrability and is a ground for rectification of the registered design. A design is capable of being registered only if it is new or original and the proprietor of a new design should not make the design public/publicise by any means anywhere in the world, or monetise the design/article, before having design protection granted for any particular product. However, the proprietor may sell his/her design after filing a design application with the IPO.

Articles sought for design registration are categorised according to an International Classification System (known as the Locarno Classification) mentioned in the Third Schedule of Designs Rules, 2001, and only one class number is to be mentioned in one particular application, which is mandatory under the rules. This classification is for articles upon which the design is applied. Examination is conducted with a view to determine whether the application is anticipated by designs already registered in India or worldwide. An examination report issued by the IPO contains both technical objections (related to the novelty of the design), as well as formal requirements. A reply to the objections raised in the examination report has to be filed with the IPO within six months from the date of filing the design application with the IPO.

It is pertinent to note that before delivery on the sale of any article(s) to which a registered design is applied, the proprietor shall cause each such article to be marked with the prescribed mark; prescribed words REGISTERED/REGD/RD; or figures denoting that the design is registered and the corresponding registration number. If the proprietor fails to do so, then he/she shall not be entitled to recover any penalty or damages in respect of any infringement of his/her copyright in the design, unless he/she shows that he/she took all proper steps to ensure the marking of the article, or unless he/she shows that the infringement took place after the person guilty thereof knew or had received notice of the existence of the copyright in the design.

It is mandatory to record, by means of an entry in the Designs Register, the assignment of any registered design, and if any assignment has been made for a foreign design application prior to filing its reciprocity application with IPO, the applicant must furnish the certified copy of the assignment from the patent office (of the country where the first application has been filed) to claim priority and proprietorship in India.

The registration of a design may be cancelled at any time after the registration of design on a petition for cancellation, along with the prescribed fee, to the Controller of Designs (at the IPO) on the following grounds:

- the design has been previously registered in India;
- the design has been published in India or elsewhere prior to the date of registration;
- the design is not new or original;
- the design is not registrable; or
- the design is not a design under the definition of ‘design’ in the Designs Act, 2000.

Chapter 10: Financing

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10.1 Market panorama

The Indian loan market is a milieu of a diverse range of credit providers, ranging from traditional banks, non-banking finance companies (NBFCs), debt funds, portfolio investors, small finance banks (SFBs) and startup lending platforms. These creditors cater to a variety of customers, ranging from deeply leveraged heavy industries, infrastructure projects, medium and small enterprises to the retail segments covering personal and business loans.

Lending in India operates largely in a regulated environment, primarily governed by the Banking Regulation Act, 1949 and supervised by the RBI. Where it involves retail investors or debt capital markets, SEBI in collaboration with the RBI provides additional regulation.

Traditionally, the main source of credit in India has been commercial banks, but over the last decade NBFCs have been increasingly active and have occupied lending spaces where regulated banks cannot operate or find it too risky to operate. This has resulted in the ‘shadow’ banking infrastructure mushrooming rapidly.

Banks in India operate under a heavily regulated regime. In order to start banking operations, companies are required to obtain a banking licence from the RBI under the provisions of the Banking Regulation Act, 1949. Banks are also subject to heavy regulation in the form of requirements on maintaining capital adequacy ratios, exposure norms, provisioning norms and end-use restrictions on loan proceeds.

NBFCs, while regulated by the RBI and operating under a licence regime prescribed by it, are subject to lighter regulations. In particular, NBFCs are exempt from lending restrictions on pricing and end use, providing greater flexibility to reach some of the underserved sectors and offering more innovative products. Also, depending on the sector and nature of facilities offered by NBFCs, different regulations apply. For instance, NBFCs allowed to accept deposits from the public under their licensing terms are subject to bank-type regulations, while non-deposit taking NBFCs operate under a fairly relaxed regime. Another prominent type of NBFCs are microfinance institutions, which have done tremendously well in boosting access to credit for medium, small and micro enterprises in India.

Other sources of traditional credit include international financial institutions, such as the World Bank Group and other multilateral development finance institutions, but their lending range is limited in light of their specific lending criteria.

Outside traditional credit providers, FPIs, venture debt providers, AIFs, retail lending platforms and SFBs have emerged as alternate sources of credit in the Indian markets. Considering the temporary liquidity stress in the NBFC market and conservative approach of banks, these sources have been progressively increasing their market share in the Indian lending landscape.

Lending by FPIs, venture debt providers and AIFs generally occurs by way of listed and unlisted debt instruments. Given that they operate in debt capital markets, they are regulated by SEBI. These regulations primarily relate to registration with SEBI, minimum eligibility requirements, and restrictions on entry and exit.

SFBs, on the other hand, are more akin to a traditional bank, but set up with the objective of financial inclusion for under-served sections of society. SFBs are also regulated by the RBI and require an SFB licence for providing the basic banking service of the acceptance of deposits and lending.

More recent additions in the retail lending space are platform lending entities and specialised Fintech companies. These entities provide technology-driven platform services for institutional and retail lenders. Platform entities providing services to institutional lenders are vicariously regulated through the regulation of institutional lenders by the RBI and/or SEBI. Platform entities providing services to retail lenders require a NBFC peer-to-peer licence from the RBI and are subject to certain other restrictions, including prohibition on lending on the platform.

10.2 Borrowing by Indian companies

Domestic borrowings from local sources such as banks, NBFCs and SFBs can be in any form depending on the requirement of the borrowers; that is, term loans, non-convertible debentures (NCDs), demand loans, discounting facilities and so on. For availing any of these financings, Indian companies typically need to comply with the requirements of the Companies Act, 2013, primarily comprising various approvals from their shareholders and board of directors, along with general authorisation under their constitutional documents for borrowing.

The RBI regulates loans extended by foreign entities to Indian entities, and such lending is classified as an ECB. Eligible borrowers may raise ECBs for up to $750m in a single financial year from eligible lenders, which must have a maturity period of at least three years. Eligible borrowers include all entities eligible to receive FDI, which excludes individuals. Recognised classes of foreign lenders include international banks and financial institutions, international capital markets, export credit agencies, suppliers of equipment, foreign collaborators and foreign equity holders. Money raised through ECBs cannot be used for on-lending for investment in equity or real estate purposes, acquisition financing or the borrower's general corporate or working capital purposes (unless an ECB for such a general or working capital purpose has a maturity of more than ten years). All eligible ECBs can be availed through an automatic route and, in some cases, require confirmation from the borrower's local AD bank. It is possible to get around some of these restrictions at times by going under the approval route by applying for the upfront permission of the RBI for the transaction after making a full disclosure, but the exercise of this authority by the RBI is entirely discretionary and all such requests are evaluated on a case-by-case basis.

Another route for availing foreign debt by Indian companies is from FPIs by way of the issuance of rupee denominated NCDs. FPIs can invest in NCDs under the following routes: (1) the voluntary retention route with on-tap limits, voluntary maturity thresholds for NCDs and exemption from concentration norms; and (2) the regular FPI route with the minimum short-term maturity of one year for NCDs subject to the monitoring of caps on total annual redemption at a portfolio level. Investment in listed NCDs by FPIs does not have any end-use restrictions. However, proceeds of unlisted NCDs cannot be utilised by the borrower for investment in capital markets, dealing in real estate business or purchase of immovable properties.

Indian companies can also borrow from AIFs and venture debt funds in the form of the issuance of listed or unlisted NCDs. This route is virtually without any material restrictions on maturity and end use, and can be structured as 'short-term' or 'long-term' investment subject to compliance with general requirements for such investments prescribed by the RBI and SEBI from time to time. Venture debt funds usually provide short-term debt funding because their objective is to provide bridge financing for the interim requirement of startups without the founders diluting their ownership and control in their companies. AIFs, on the other hand, have been capturing the void created due to the liquidity crunch faced by NBFCs and are active in infrastructure, real estate and the distressed assets space.

10.3 Security and guarantee

Typically, the most common forms of security are in the form of a mortgage over immovable properties, hypothecation of movable properties (including fixed and current assets) or a pledge over shares. All types of security creation over the assets of any company require the registration of the charge to be made with the ROC within 30 days of the creation of the charge. If this does not occur, the charge will not be taken into consideration if the company goes into liquidation. A mortgage of immovable properties must be registered with the concerned local Sub-Registrar of Assurances for the area where the mortgaged property is situated within four months of security creation. The mortgage is not enforceable until the registration has been made. However, this is not compulsory in some states if the mortgage is in the form of an equitable mortgage effected through the deposit of title deeds.

In respect of a pledge of shares, if the shares are in dematerialised form, a pledge creation form must be filed with the depository before the pledge will be effective. If the shares are in physical form, the pledge is created with the delivery of share certificates along with signed blank transfer forms.

There are no significant costs involved in relation to form filings with the ROC; a very small amount is charged as a nominal fee. However, there is stamp duty payable to the government at the time of the execution of any instrument and as registration fees post-execution in respect of mortgages. The rates of payment differ from state to state. In some states these duties are capped, while in others they are charged as an *ad valorem* percentage on the amount of debt secured without an upper limit, thereby pushing up transaction costs significantly.

It is possible for Indian companies to give downstream, upstream and cross-stream guarantees, provided they relate to the obligations of domestic entities and the passing of some corporate benefit can be demonstrated.

From a foreign debt perspective, the creation of security over the assets of the borrower or pledge over shares of the borrower and guarantees by third parties for securing and guaranteeing ECBs and NCDs subscribed by FPIs is generally permitted. However, obtaining a no-objection certificate from the AD bank of the borrower is a procedural requirement in certain cases.

Security over assets of third parties (promoters, shareholders and group companies of the borrower other than financial securities of the promoter) for securing ECBs may require approval from the RBI, although the RBI occasionally issues directions permitting/restricting such security creations. While structuring a security package for foreign debt, the prevailing foreign exchange directions issued by the RBI should be thoroughly reviewed.

Additionally, pursuant to the Companies Act, 2013, an Indian company cannot issue guarantees or provide any security on behalf of any other company if: (1) the respective boards of the two companies have any directors in common; (2) the directors of the guarantor company can jointly exercise at least 25 per cent of the total voting power available to the shareholders of the borrower company; or (3) the borrower company, its board or managing director is accustomed to acting according to the instructions of the guarantor company or any of its directors (individually or collectively). However, the above three restrictions will not apply if: (1) the borrower company is the wholly owned subsidiary of the guarantor company; or (2) the guarantor company is acting in the ordinary course of its business in giving such a guarantee or providing security; and (3) the shareholders of the guarantor company have approved the provision of such a guarantee or security by 75 per cent majority and the loan for which such a guarantee or security is being provided will be utilised for the principal business of the borrower company.

In India it is only possible contractually to determine the order of priority in conflicting security interests among secured creditors. While there is a statutory order of priority to be followed in the event of liquidation of the company that cannot be contractually overturned, the terms of the contract determine what will ordinarily be the order of priority in which secured creditors are repaid. All creditors of the same rank receive payment on a basis proportionate to their exposure only after the dues of all higher-ranked creditors have been completely discharged.

Chapter 11: Privacy laws and data protection

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The present regulatory framework governing data protection is archaic, with information technology laws primarily outlining basic data protection requirements. A comprehensive law dealing with data protection and privacy modelled on the lines of the European Union's General Data Protection Regulation (GDPR) is presently in the works and expected to pass later this year.

11.1 A fundamental right to privacy

In a landmark judgment (*Justice K S Puttaswamy (Retd) and Another v Union of India and Others*) rendered in August 2017, the Supreme Court of India ruled that the right to privacy is a fundamental right and can only be subject to reasonable restrictions under the law. The Supreme Court further recognised that informational privacy in the digital era is a facet of the right to privacy and highlighted the need for a robust data protection law to control the actions of the state as well as non-state actors.

11.2 Present regulatory framework

The Information Technology Act, 2000 as amended by the Information Technology Amendment Act, 2008 (the 'IT Act') is the principal legislation governing electronic transactions and data protection in India. The IT Act has extraterritorial jurisdiction and covers contraventions committed outside India if such a contravention involves an Indian computer, computer system or network. While there is no data protection regulator, the Department of Information Technology under the Ministry of Electronics and Information Technology (MeitY) is the nodal agency for all information technology matters.

11.3 Intermediary regulations

The Information Technology (Intermediary Guidelines) Rules, 2011 framed under the IT Act (the 'Intermediary Rules') specifies the duties of intermediaries in India.

An intermediary is an entity that provides storage, transmission and any other service related to third-party electronic data. It includes telecom service providers, network service providers, internet service providers, web hosting service providers, search engines, online payment sites, online-auction sites, online marketplaces and cyber cafes. An intermediary must comply with the Intermediary Rules, which mandate the intermediary to: (1) publish a 'User Agreement' or 'Terms and Conditions' and a 'Privacy Policy' on the intermediary's website accessible in India; (2) prohibit its users from hosting, publishing, transmitting or sharing any information that belongs to someone else, obtained without his/her authorisation or is misleading, defamatory, obscene, pornographic, paedophilic, libellous, hateful, harms minors or violates any applicable law in India; (3) appoint a 'Grievance Officer' and have a grievance redressal mechanism in place; and (4) report cybersecurity incidents to the Computer Emergency Response Team under the MeitY as soon as possible.

An intermediary is exempt from liability for any third-party information hosted on its website, as long as the intermediary observes due diligence while discharging its duties and does not initiate the transmission of such information or modify the information being transmitted through the intermediary. This safe harbour provision will not apply if the intermediary is involved in the commission of an unlawful act or fails to take down unlawful content upon receiving actual knowledge or on being notified by the appropriate government or its agency.

11.4 Regulations relating to personal and sensitive personal data

The Information Technology (Reasonable Security Practices and Procedures and Sensitive Personal Data or Information) Rules, 2011 (the 'SPDI Rules') set out the safeguards to be implemented by an entity for the collection, storage, use and transfer of personal information and sensitive personal data or information. Under the SPDI Rules, personal information is broadly defined to include any information regarding a natural person that is directly or indirectly capable of identifying such a person, such as an individual's name, telephone number or address. A subset of personal information, sensitive personal data, consists of, inter alia, passwords, biometric information, sexual orientation, physical, physiological and mental health condition and so on, and excludes information that is freely available in the public domain.

An entity dealing with sensitive personal data is considered to be a data controller and must have a privacy policy disclosing its data handling and disclosure practices, type of information collected, purpose of such a collection, intended usage of the information collected and reasonable security practice followed by the data controller. Sensitive personal data must be collected/processed only for a lawful purpose and not be retained for longer than necessary. Specific written consent of the information provider who 'opts-in' (or 'opts-out') to share his/her sensitive personal data is mandatory and third-party disclosure is permissible provided prior consent is obtained from the information provider. Similarly, an entity may freely transfer sensitive personal data outside India, as long as the same level of data protection is adhered to in the recipient country. Barring specific sectoral regulations (eg, data storage on local servers for Fintech firms mandated by India's central bank), there are no explicit requirements on the data hosting location or jurisdiction under the SPDI Rules. These rules are applicable only to corporate entities and leave government bodies outside their ambit.

11.5 Penalty for breach of data protection obligations

Under the IT Act, it is a criminal offence punishable with a monetary fine as well as imprisonment for a person to fraudulently or dishonestly carry out any act that results in the failure to protect data, or for an intermediary to disclose personal information in breach of a lawful contract.

11.6 Sectoral regulations

Apart from the IT Act, multiple sectoral regulations address various aspects of data privacy and data protection in India. For instance, medical regulations in India mandate patient–physician confidentiality. Similarly, the RBI and the Telecom Regulatory Authority of India provide for privacy and confidentiality obligations that must be adhered to by business entities in the financial and telecom sectors, respectively.

Chapter 12: Competition law

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12.1 Introduction

Ever since the merger control-related provisions under the Competition Act, 2002 were enforced eight years ago, the Competition Commission of India (the 'Commission') has been tasked with balancing the growth of a robust competition regime in India while safeguarding the interests of the industry to enable ease of doing business in India.

Recent noteworthy developments under the Indian merger control regime include the introduction of a green channel clearance regime, acceptance of purely behavioural remedies in horizontal mergers and increased scrutiny of vertical mergers.

Indian competition law, including merger control provisions, is proposed to be amended to bring it in line with global best practice. In 2018 the central government constituted a Competition Law Review Committee (CLRC)[12] to recommend changes to the existing law (ie, the Competition Act) and the CLRC submitted its report in August 2019. Following the CLRC recommendations, in February 2020 the central government invited public comments on the Competition (Amendment) Bill, 2020 (the 'Bill').[13]

12.2 Recent developments in the Indian scenario

12.2.1 Introduction of the 'green channel' route

The automatic approval route, or the 'green channel', was introduced by the Commission with effect from 15 August 2019. Under the 'green channel' route, notifiable transactions wherein the parties do not have any horizontal and/or vertical overlaps in any of the plausible markets nor have any presence in complementary markets can obtain 'near simultaneous' or same-day clearance from the Commission. This makes India the only jurisdiction with a mandatory notification regime to enable the notifying party/parties to obtain same-day approval from the Commission, in certain specified scenarios.

As of February 2020, nine transactions had been approved under the 'green channel' route.

12.2.2 Increase of behavioural remedies

Over the last eight years of merger control, in the assessment of complex horizontal mergers the Commission has shown a preference for structural divestments in seven out of its eight Phase II reviews, with behavioural remedies being more commonly accepted in Phase I reviews.

However, in the past year, while assessing the transaction involving Schneider Electric India Private Limited and Temasek Holdings (Private) Limited's proposed acquisition of the electrical and

12 By way of full disclosure, Uberoi was part of the working group of the CLRC.

13 See http://feedapp.mca.gov.in//pdf/Draft-Competition-Amendment-Bill-2020.pdf accessed 13 May 2020.

automation business of Larsen & Toubro Limited,[14] the Commission for the first time approved a notifiable transaction subject to purely novel behavioural remedies in a Phase II review.

In doing so, the Commission has acknowledged that: (1) the 'one-size-fits-all' approach is not effective in addressing concerns on the appreciable adverse effect on competition; and (2) behavioural remedies are capable of addressing appreciable adverse effect on competition concerns just as effectively as structural ones.

12.2.3 Increased scrutiny of vertical mergers

In 2019 the Commission increased its scrutiny of vertical mergers, requiring Form II notifications in at least two vertical mergers involving: (1) acquisition of equity stake in a cab aggregator by a car manufacturer (ie, acquisition of equity stake in ANI Technologies Pvt Ltd, which runs the online ride sharing platform 'Ola', by Hyundai Motor Company and Kia Motor Company);[15] and (2) acquisition of equity stake in an airport operator by a corporate group with a majority stake in two airlines (ie, the acquisition of shares of GMR Airports Limited by TRIL Urban Transport Private Limited, Valkyrie Investment Pte Limited and Solis Capital (Singapore) Pte Limited).[16]

However, it is pertinent to note that in both these vertical mergers the Commission accepted the behavioural remedies offered by the parties, given that such remedies effectively addressed the vertical foreclosure harms.

This trend of increased scrutiny of vertical mergers by the Commission is in line with the practices of other mature jurisdictions such as the US,[17] and is expected to increase given that vertical integration will be commonplace for digital platforms.

12.3 Key changes proposed: Competition Amendment Bill

12.3.1 Reduced timelines

In a bid to 'fast-track' merger clearances, the Bill seeks to reduce the timeline for Phase I reviews from 30 working days to 20 calendar days, and to reduce the outer limit timelines from 210 days to 150 (+30) calendar days.[18] This time limit is subject to clock-stops, such as when the Commission requests more information.

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14 C-2018/07/586; by way of full disclosure, Uberoi advised Schneider Electric India Private Limited and Temasek Holdings (Private) Limited.

15 C-2019/09/682.

16 C-2019/07/676.

17 Jenner & Block, Increased Scrutiny for Vertical Mergers on the Horizon, https://jenner.com/system/assets/publications/18871/original/Increased%20Scrutiny%20for%20Vertical%20Mergers%20on%20the%20Horizon%20-%20ATTORNEY%20ADVERTISING.pdf?1557244521 accessed 13 May 2020.

18 '7. In section 6 of the principal Act, —

…

(c) in sub-section (2A), for the words "two hundred and ten", the words "one hundred and fifty calendar" shall be substituted.

(d) after sub-section (2A), the following proviso shall be inserted, namely: —

"Provided that the Commission may by order extend the period under sub-section (2A) beyond one hundred and fifty calendar days by such further period as it thinks fit, but not exceeding thirty calendar days in case parties to the combination request for additional time to furnish relevant information or remove defects to the notice filed under sub- section (2) of section 6 as may be requested by the Commission."'

http://feedapp.mca.gov.in//pdf/Draft-Competition-Amendment-Bill-2020.pdf accessed 13 May 2020.

12.3.2 *Size of transaction test*

The Bill suggests an amendment to the Competition Act that enables the government to prescribe any criteria that shall cause an acquisition, merger or amalgamation deemed to be a combination, and require the prior approval of the Commission.[19] This amendment, although quite open-ended, is expected to bring in a 'size of transaction' or 'deal value' threshold in addition to the asset and turnover thresholds currently in place under the Indian competition regime.

12.3.3 *Material influence standard*

The standard for control used by the Commission has an important impact on the nature of transactions that are required to be notified with and assessed by the Commission. To date, the Commission has predominantly used the 'decisive influence' test to determine control, and has used the 'material influence' in only two cases.[20] However, the Bill has now sought to bring in a 'material influence' threshold under the act.[21]

Chapter 13: Dispute resolution

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13.1 Structure of the courts

The ease of doing business is largely dependent on the legal and regulatory framework of a country. An effective judiciary enabling timely adjudication of disputes, coupled with recognition of the importance of enforcement of contractual obligations is a key factor contributing towards building investor confidence in a country.

A key factor that contributes to boosting investor confidence, as recognised by the World Bank is the enforcement of contracts supported by timely adjudication of commercial disputes. The judiciary in India, like most countries, has a hierarchical structure, comprising the Supreme Court as the apex court of the country, High Courts as the highest courts in states and subordinate courts in various districts supervised by the High Courts.

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19 '6. In section 5 of the principal Act,
(a) after clause (c), the following provisos shall be inserted, namely: —
"Provided that the Central Government may in public interest and in consultation with the Commission prescribe any criteria other than those prescribed in clauses (a), (b) and (c), the fulfilment of which shall cause any acquisition of control, shares, voting rights or assets, merger or amalgamation to be deemed to be a combination under this section and a notice for any acquisition of control, shares, voting rights or assets, merger or amalgamation fulfilling such criteria shall be given to the Commission under section 6."'
http://feedapp.mca.gov.in//pdf/Draft-Competition-Amendment-Bill-2020.pdf accessed 13 May 2020.

20 (1) C-2015/02/246, which involved the transfer of business, assets and operations of two cement plants owned by Jaiprakash Associates Limited to UltraTech Cement Limited; and (2) C-2016/10/443, which involved the amalgamation of Agrium Inc and Potash Corporation of Saskatchewan, Inc.

21 '6. In section 5 of the principal Act, —
…
(b) for clause (a) of the Explanation, the following clause shall be substituted, namely: —
"(a) "control" means the ability to exercise material influence, in any manner whatsoever, over the management or affairs or strategic commercial decisions by—
(i) one or more enterprises, either jointly or singly, over another enterprise or group; or
(ii) one or more groups, either jointly or singly, over another group or enterprise;"'
http://feedapp.mca.gov.in//pdf/Draft-Competition-Amendment-Bill-2020.pdf accessed 13 May 2020.

Further, to ensure the timely, efficient and effective resolution of commercial disputes, the Commercial Courts Act, 2015, as amended by the Commercial Courts, Commercial Division and Commercial Appellate Division of High Courts (Amendment) Act, 2018 (the '2018 Amendment'), was enacted. The Commercial Courts Act is primarily aimed at expediting commercial disputes at the original and appellate levels, by way of, inter alia, specialised fora, Commercial Courts at the district level and Commercial Divisions in all High Courts, ordinary original civil jurisdiction, and Commercial Appellate Divisions in the High Court so as to bring about a time-bound adjudication of commercial disputes. The specialised Commercial Courts have jurisdiction to try all suits and applications relating to a commercial dispute of a specified value.[22] The pecuniary jurisdiction of Commercial Courts has been brought down to INR 300,000 from the earlier specified value of INR 10m by way of the 2018 Amendment.

The Commercial Courts Act provides that any person aggrieved by the judgment or order of a Commercial Court below the level of a District Judge may appeal to the Commercial Appellate Court within a period of 60 days from the date of judgment or order. Further, any person aggrieved by the judgment or order of a Commercial Court at the level of a District Judge exercising original civil jurisdiction or, as the case may be, the Commercial Division of a High Court may appeal to the Commercial Appellate Division of that High Court within a period of 60 days from the date of the judgment or order. [23]

13.2 Use of arbitration

Arbitration has emerged as a popular and effective means of dispute resolution in India, governed by the Arbitration and Conciliation Act, 1996 (the '1996 Act'). The government has made concerted efforts to introduce global best practice into the arbitration regime with the intention to make India a global arbitration hub. For instance, key amendments have been brought about by the Arbitration and Conciliation (Amendment) Act, 2015 (the '2015 Amendment') and the Arbitration and Conciliation (Amendment) Act, 2019 (the '2019 Amendment'). These amendments are designed to improve the perception of India as an international arbitration jurisdiction by attempting to strengthen institutional arbitration, reduce judicial interference and empower arbitral tribunals, so as to build confidence in arbitration as an effective mechanism of adjudication of commercial disputes. As far as adjudication of challenges to arbitral awards are concerned, the Indian judiciary is increasingly taking a non-interventionist approach. Arbitrations are now characterised by limited interference of courts from the stage of referral of disputes to arbitration until proceedings to set aside/challenge an arbitral award. Some of the key changes to the 1996 Act in this regard are:

13.2.1 Interim relief

Prior to the 2015 Amendment parties could seek interim relief from courts prior to the commencement of arbitration, but were under no compulsion to commence arbitral proceedings in a timely manner. Therefore, parties enjoyed the benefit of interim orders from courts for extended periods of time. To address this anomaly, the 2015 Amendment mandated that arbitration must commence within 90 days from the date of the interim order. Moreover, the courts are not

22 The Commercial Courts Act 2015, s 6.

23 *Ibid*, s 13.

to entertain any application under section 9 of the 1996 Act, unless they find that circumstances exist that may not render the remedy under section 17 (ie, seeking interim relief from the arbitral tribunal) efficacious.

Under section 17 of the 1996 Act, which is applicable to India-seated arbitrations, interim measures of protection may be passed by the arbitral tribunal during the arbitral proceedings. Now, by virtue of the 2015 Amendment, the arbitral tribunal has same power for making orders under section 17 of the 1996 Act as the court has for the purpose of, and in relation to, any proceedings before it under section 9, and any such order passed by the arbitral tribunal is enforceable under the Code of Civil Procedure 1908 (CPC) in the same manner as if it were an order of the court.

13.2.2 Proceedings to set aside or challenge the enforcement of an award

The 2015 Amendment brought much needed clarity to the ambit of the term 'public policy' in section 34(2)(b) of the 1996 Act, which is applicable for proceedings to set aside an arbitral award rendered in an India-seated arbitration. By way of this amendment, two explanations were added to section 34(2)(b) specifying that an award may be set aside on this ground only if the award: (1) is vitiated by fraud or corruption; (2) is in contravention with the fundamental policy of Indian law; or (3) is in conflict with the most basic notions of morality or justice. The additional ground of 'patent illegality appearing on the face of the award' remains available as an independent ground for setting aside an arbitral award only for India-seated arbitrations other than international commercial arbitrations. The 2015 Amendment has, however, clarified that an award shall not be set aside merely on the ground of an erroneous application of the law or by reappreciation of evidence.

Further, the 2019 Amendment clarified that the scope of challenge to an arbitral award under section 34 is limited to a challenge based upon the record of the arbitral tribunal. Therefore, wide-ranging challenges based on evidence not led before the arbitral tribunal – which create uncertainty and increase time and cost related to the ultimate enforcement of the arbitral award – has been restricted, providing an impetus for the swift enforcement of awards. As regards the enforcement of foreign awards under section 48, all grounds for challenge except 'patent illegality' are available.

Indian courts have increasingly adopted a pro-arbitration approach and even staved off challenges to awards on the ground of breach of public policy for alleged violation of foreign exchange regulations. One of the key decisions in this regard was that of the Delhi High Court in *NTT Docomo Inc v Tata Sons Ltd, 2017 SCC OnLine Del 8078,* wherein the Delhi High Court noted that:

> 'The issue of an Indian entity honouring its commitment under a contract with a foreign entity which was not entered into under any duress or coercion will have a bearing on its goodwill and reputation in the international arena. It will indubitably have an impact on the foreign direct investment inflows and the strategic relationship between the countries where the parties to a contract are located. These too are factors that have to be kept in view when examining whether the enforcement of the Award would be consistent with the public policy of India.'

Prior to the 2015 Amendment a mere admission of a challenge to an India-seated award meant that the award could not be enforced. Such a grant of an automatic stay on the mere admission of a challenge to an award led to a lot of frivolous challenges to arbitral awards. Thus, to encourage a pro-enforcement environment, the 2015 Amendment introduced changes to section 36 of the 1996 Act mandating that:

- a separate application be made by an award debtor seeking stay over enforcement of the award; and
- while considering the application for grant of stay in the case of an arbitral award for payment of money, the court should have due regard to the provisions for grant of stay of a financial decree under the provisions of the CPC, that is, typically for the deposit of security for costs. Practically, commercial courts in India have directed the party challenging the award to deposit security in the range of 50–100 per cent of the award amount.

13.2.3 Thrust towards institutional arbitration

The government is proactively investing in building infrastructure for arbitral institutions, such as the setting up of the New Delhi International Arbitration Centre and Mumbai Centre for International Arbitration, to bring India on a par with jurisdictions such as Singapore and London, which boast of pre-eminent arbitral institutions such as the Singapore International Arbitration Centre (SIAC) and London Court of International Arbitration, respectively.

There is a thrust towards the development of an arbitration bar and expertise. The 2019 Amendment is clear in its intention to encourage institutional arbitration in India and regulate the development of an arbitration bar, including by way of proposing setting up the Arbitration Council of India (ACI), specifying qualifications for arbitrators and tasking the arbitral institutions rather than courts with the functions of the appointment of arbitrators under the amended section 11. However, these provisions are yet to be notified for enforcement.

13.2.4 Other important reforms to the 1996 Act

Apart from the above amendments, there are other noteworthy amendments brought about by the 2015 and 2019 Amendments.

Mandatory disclosure of impartiality

Under section 12, the 2015 Amendment has made it mandatory for an arbitrator to make a declaration of independence and impartiality. The Fifth Schedule lists the grounds that would give rise to justifiable doubts as to the independence or impartiality of the arbitrator. The Seventh Schedule sets out the conditionalities under which an arbitrator is ineligible to act as such unless, subsequent to disputes having arisen, parties have waived this disqualification by way of an express agreement in writing. Further, section 14 provides for the substitution of an arbitrator in the event of the termination of his/her mandate. This is intended to encourage greater transparency and accountability in the process.

Extension of the time by consent of parties

The 2015 Amendment introduced section 29A into the 1996 Act with the aim of effective and time-bound disposal of India-seated arbitrations. This section provided that an arbitral award must be rendered within 12 months from the date on which the arbitral tribunal enters reference, and such a time period may be extended by a period of six months by the mutual consent of parties. A further extension of this period could only be made by judicial order and would invite scrutiny into the conduct of the arbitral proceeding and potential cost consequences to the parties or tribunal. However, this provision has been further amended by the 2019 Amendment to provide that in the case of non-international commercial arbitrations, the award must be passed within 12 months from the date of completion of pleadings. Further, pleadings are to be completed within six months from the date upon which the arbitrator receives notice of his/her appointment in writing, whereas there is no mandated timeline for India-seated international commercial arbitrations, which are expected to meet these timelines on a best endeavours basis.

Fast-track procedure

Section 29B was introduced in the 2015 Amendment for the purpose of the completion of arbitrations involving small claims through a fast-track procedure. Such arbitrations are to be conducted through documentary evidence and must be completed within six months.

Costs

Section 31A was introduced in the 2015 Amendment to bring the concept of the 'costs follow events' regime to India and discourage frivolous claims.

Confidentiality

The 2019 Amendment introduced section 42A, which obligates the arbitrator, arbitral institution and parties to the arbitration to maintain confidentiality of arbitral proceedings, except where the disclosure of an award is necessary for its implementation and enforcement.

All the above amendments to the 1996 Act have opened up a gamut of options for parties seeking to resolve disputes through arbitration to find timely, efficient and cost-effective dispute resolution through arbitration.

13.3 Other forms of dispute resolution

Apart from litigation and arbitration, other ADR mechanisms in India include mediation and conciliation. While they are effective mechanisms to resolve the pendency of litigation in India, they are less popular in India as a matter of practice. In fact, the CPC encourages ADR. Section 89 of the CPC stipulates that where it appears to the court that there exist elements of settlement that may be acceptable to the parties, the court may formulate the terms of the settlement, subject to input from the parties, and refer them for resolution by means of arbitration, conciliation, mediation or judicial settlement through the Lok Adalat. However, this provision is severely underutilised in India.

Further, the 2018 Amendment has added section 12A to the Commercial Courts Act 2015, which introduced the concept of pre-institution mediation. Essentially, this contemplates mediation of commercial disputes prior to the institution of a suit in the case of suits that do not contain a plea for urgent interim relief. It also provides for the enforcement of settlement terms arrived at between parties. In this regard, the amendment provides that the written settlement between the parties would have the same status as that of an arbitral award under section 30 of the 1996 Act. However, pre-institution mediation is still at a nascent stage in India and has not yet emerged as an effective means of resolution of disputes between parties.

Further, under the Commercial Courts (Pre-institution Mediation and Settlement) Rules 2018, it is only where both parties to the commercial dispute appear before the concerned authority and give consent to participate in the mediation process that the authority may refer the matter to a mediator. However, the reality is that the average commercial litigant in India, does not, to date, view mediation as an effective means for binding dispute resolution. This is further augmented by the lack of adequate infrastructure for training mediators and the consequent non-availability of a skilled pool of mediators who can effectively resolve disputes through a non-adversarial process, such as mediation.

Interestingly, the 2019 Amendment mandates the ACI to take all such measures as may be necessary to promote and encourage arbitration, mediation, conciliation or other ADR mechanisms and, for that purpose, to frame policy and guidelines for the establishment, operation and maintenance of uniform professional standards in respect of all matters relating to arbitration. However, the relevant provision has not yet been notified for enforcement, and given the existing lack of infrastructure, the functions of the ACI pertaining to the promotion of mediation remain unclear. Therefore, cultivating a skilled pool of mediators through concerted efforts at training and developing adequate infrastructure to support and promote mediation and conciliation as an effective dispute resolution mechanism is critical for the growth of these ADR mechanisms as effective tools for commercial dispute resolution in India.

Chapter 14: Other

Priya Adlakha, SS Rana & Co, New Delhi

Depending upon the specific industry/requirement, foreign entities may be required to comply with the following illustrative laws.

14.1 Food laws

Food safety laws in India fall under the purview of the Food Safety and Standards Act, 2006 and subsequent rules framed thereunder. The standard body regulating food safety in India is the Food Safety and Standards Authority of India (FSSAI). Any person carrying out food business in India has to ensure compliance with the aforementioned laws.

The main objective of the Food Safety and Standards Act, 2006 is to ensure that the consumable items available in the market are healthy, safe to eat and not adulterated. To ensure that these consumable products are safe, the FSSAI has introduced regulations wherein it restricts certain products and ingredients from being sold.

Every food business operator, whether a manufacturer, retailer or any person dealing in the sale of food products, must mandatorily obtain an FSSAI licence/registration from the FSSAI department. The application for a FSSAI licence can be made on the FSSAI website by submitting the required documents along with the prescribed fees. A FSSAI licence is valid from one to five years, depending on the nature of the fee paid.

There are two kinds of FSSAI licence in India: the state licence and central licence. For a state licence the food business should have an annual turnover of up to INR 200m, and for a central licence the annual turnover should be more than INR 200m. Small business owners with an annual turnover of less than INR 200m do not require a licence; however, they need an FSSAI registration for operating their food business.

Food packaging and labelling laws are regulated under the Food Safety and Standards (Packaging and Labelling) Regulations, 2011. The above rules list the precautions to be taken by every food business operator while packaging products. They further mention the mandatory declarations that must be affixed on the food packaging, along with the manner in which the declarations are required to be mentioned.

Wrongful branding, sale of substandard food, operating without a licence/registration and misleading advertisements are some of the recognised offences under the food safety laws in India. These offences can either be punishable with imprisonment or a fine, or both.

14.2 Cosmetics

The cosmetics market in India is growing at a significant rate, with an increased percentage of users every year. As cosmetics have properties that can directly or indirectly influence human health, their manufacture/sale/distribution is regulated under the Drugs and Cosmetics Act, 1940 and subsequent Drugs and Cosmetics Rules, 1945. The said laws have been enforced to protect the interests of consumers, who can be deceived by substandard products, fake products or products having less net weight than fixed by the authorities.

The aforementioned laws provide for mandatory registrations and compliance required by enterprises or proprietors engaged in the business of drugs and cosmetics. The government continues to modify the enactments by issuing notifications or orders when required. India also allows the import of cosmetics, which are regulated under the guidelines provided for the registration of imported cosmetics.

The labelling of cosmetics is regulated under the Drugs and Cosmetics Rules, along with the Legal Metrology (Packaged Commodities) Rules, 2011. Some of the mandatory labelling requirements include the name of the product, manufacturing site address, directions for use, net contents, ingredients and any caution, if necessary.

Additionally, the Bureau of Indian Standards (BIS), which is the statutory body for standards in India, sets the standards for cosmetics for the products listed under Schedule 'S' of the Drugs and Cosmetics Rules, 1945. Schedule 'S' comprises products such as skin powders, and creams, hair oils and shampoos. The standards published by BIS must be adhered to for manufacturing cosmetics in India.

The Drugs and Cosmetics Rules, 1945 restrict the use of cosmetics containing dyes, colours and pigments, other than those specified by the BIS. Further, the above rules prohibit the use/import of lead and arsenic compounds in cosmetics for the purpose of colouring. The rules also prohibit the manufacture and import of cosmetics containing mercury compounds.

The application has to be made under the method mentioned in the Drugs and Cosmetics Rules, 1945. The rules classify cosmetics into different categories; that is, powders, creams, lipsticks, hair dyes and so on, according to which their application can be made. To manufacture any of the products as specified in these categories, a licence has to be obtained from a Licensing Authority appointed by the federal government.

Before granting or refusing the licence, the Licensing Authority must order an inspection of the whole premises where the operations of manufacturing are being carried out. A detailed report must be submitted to the Licensing Authority, which then decides whether to grant the licence.

After the government notification introduced in 2011, all cosmetic products imported for sale in India need to be registered with the Central Drugs Standard Control Organization (CDSCO). CDSCO is the licensing authority for the purpose of import according to the 1945 Rules. This new 'registration' requirement is primarily to regulate the import of beauty and personal care products by traders with no accountability for contents and no mechanism to fix responsibility in case a consumer is not satisfied with the quality. The new regulation is an attempt to check the sale of substandard cosmetic products and harmonise import requirements with products manufactured in India.

A trademark owner without a manufacturing unit in India to sell cosmetics is now required to obtain a registration certificate to continue marketing activities in India. An application for the registration of import must be made along with the requisite documents and submitted to the Drug Controller General at the CDSCO office in New Delhi.

The Drugs and Cosmetics Act, 1940 is a punitive act. If any of the provisions or rules under the act with respect to cosmetics is not complied with, it can attract a fine or imprisonment, or both, depending on the gravity of non-compliance.

14.3 Legal metrology laws

The Legal Metrology Act, 2009 deals with the units and methods of weighment and measurement in relation to mandatory technical and legal compliance in order to ensure public guarantee of security and accuracy. The act was introduced to replace the Standard of Weights and Measures Act, 1976 and the Standards of Weights and Measures (Enforcement) Act, 1985. The provisions of the act came into force on 1 April 2011.

The aim of the act is to set and enforce the standards of weight and measures; to regulate the trade and commerce in weights, measures and other goods sold or distributed by weight, measure or number; and to regulate other connected matters. The Legal Metrology (Packaged Commodities) Rules, 2011 pertain to goods that are packaged and provide the manner in which declarations are to be made and what declarations a packaged commodity meant for sale must contain.

The major stakeholders under the Legal Metrology Act are listed below:

Packers

A packer is defined under Regulation 2(g) as a person who pre-packs any commodity in any bottle, tin, wrapper or otherwise in units suitable for sale, whether wholesale or retail.

Manufacturers

Under section 2(i) of the act, 'manufacturer', in relation to any weight or measure, means a person who: (1) manufactures a weight or measure; (2) manufactures one or more parts, and acquires other parts, of such a weight or measure and, after assembling those parts, claims the end product to be a weight or measure manufactured by itself; (3) does not manufacture any part of such a weight or measure, but assembles parts thereof manufactured by others and claims the end product to be a weight or measure manufactured by itself; and (4) puts, or causes to be put, its own mark on any complete weight or measure made or manufactured by any other person and claims such a product to be a weight or measure made or manufactured by itself.

Dealer

Under section 2(b) of the act, 'dealer', in relation to any weight or measure, means a person who carries on, directly or otherwise, the business of buying, selling, supplying or distributing any such weight or measure, whether for cash or deferred payment, or for commission, remuneration or other valuable consideration, and includes a commission agent, importer and manufacturer, who sells, supplies, distributes or otherwise delivers any weight or measure manufactured by it to any person other than a dealer.

Importer

An 'importer' is the individual, firm or legal entity that brings goods or causes goods to be brought from a foreign country into a customs territory.

Repairer

Under section 2(p) of the Act, 'repairer' means a person who repairs a weight or measure, and includes a person who adjusts, cleans, lubricates or paints any weight or measure, or renders any other service to such a weight or measure to ensure that such a weight or measure conforms to the standards established by or under this act.

Every manufacturer, packer or importer of commodities is required to obtain a registration by filing an application with the Director or Controller, along with submission of its particulars, including, but not limited to, its name, complete address of the premises and name of the commodity, along with the payment of the requisite fees (Regulation 27).

Mandatory Declarations need to be made under the provisions of the act.

The rules mandate for the making of declarations on every package intended to be commercialised in the Indian market (Regulation 6 of the rules), namely:

- name and address of the manufacturer, packer, importer;
- common or generic names of the commodity;
- net quantity in terms of the standard unit of weight or measure of the commodity;
- month and year in which the commodity was manufactured, pre-packed or imported;
- retail sale price of the package; and
- size/dimensions of the commodity wherever relevant.

Offences and penalties under the act are specified in chapter V:

- Section 27 of the act provides a penalty for the manufacture or sale of a non-standard weight or measure that shall be punishable with a fine, which may be extended to INR 20,000, and for the second or subsequent offence with a fine or imprisonment for a term that may extend to three years, or both.
- Section 36(1) of the act provides a penalty for the manufacturing, packaging, selling, distributing, importing and so on of non-standard packages that shall be punished with a fine, which may extend to INR 25,000; for the second offence, with a fine, which may extend to INR 50,000; and for the subsequent offence, with a fine that shall not be less than INR 50,000, but which may extend to INR 100,000, or imprisonment for a term that may extend to one year, or both.
- Section 36(2) of the act provides punishment for manufacturing, packing or importing any pre-packaged commodity with an error in the net quantity as may be prescribed. The punishment may be a fine of not less than INR 10,000, but may extend to INR 100,000, or imprisonment for a term that may extend to one year, or both.
- Section 38 of the act provides a penalty for the non-registration by the importer of the weight or measure. The offence is punishable with a fine, which may extend to INR 25,000; and for the second subsequent offence with a fine or imprisonment for a term that may be extended to six months, or both.
- Regulation 32 of the rules imposes a penalty on the manufacturer, packer or importer of the commodities for non-registration under the provisions of the rules or contravention of any other rules.

Section 48 of the act provides that some offences may be compounded either before or after a prosecution upon payment of a prescribed sum. However, no offence can be compounded if the person has committed the same offence or a similar offence earlier within three years of date of the first offence, which was compounded. Companies must nominate a person who will be held responsible for the conduct of the company, and communicate the same to the Director of Legal Metrology or the concerned controller. When no person is nominated, then the person in charge or responsible for the operations of the company is held responsible. The company may be directed by the court to publish its name along with the offence committed in a newspaper at its own cost.

Appeals can be filed to the next highest authority against all decisions or orders of an officer in charge of legal metrology within 60 days from the day of the passing of the order or decision.

Indonesia

Chapter 1: Introduction

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Indonesia is an archipelagic nation consisting of more than 17,500 islands, and is home to more than 260 million people. It is a resource-rich country and a major exporter of minerals and agricultural products (including palm oil and rubber). It has a dynamic and growing middle class and a relatively young population (median age of 29).

On a nominal basis, its GDP is more than $1tn. Prior to the Covid-19 outbreak, the economy was growing at a relatively healthy rate of five per cent. Household consumption represents approximately 60 per cent of overall GDP.

The current Widodo administration has prioritised infrastructure development. The 2020 infrastructure-related budget amount is IDR 419tn (approximately US$26bn at the post-Covid-19 depressed exchange rate). The government will also focus on developing manufacturing capability and the tourism industry, as well as encouraging FDI in the country.

Chapter 2: The business environment

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2.1 Government structure

Indonesia has a centralised system of government, with regional governments exercising a degree of autonomy. The power of the executive is vested in the Office of the President. The President, who is elected, is empowered to manage national affairs and relations with foreign powers. The legislative power is held by the House of Representatives (Dewan Perwakilan Rakyat or DPR) and the Regional Representatives (Dewan Perwakilan Rakyat Daerah – DPRD), the members of which are elected every five years. The judiciary consists of the Supreme Court and the Constitutional Court.

2.1.1 The executive

The Indonesian President is elected nationally by popular vote. In exercising its power, the President is assisted by government ministers, each of which is responsible for a particular area of government activity.

2.1.1 The legislature

Indonesia's legislative power is vested jointly in Parliament, called the DPR, and the President. Each has rights to propose legislative bills and approve laws.

The President may also issue Government Regulations (Peraturan Pemerintah) as required to implement laws. In urgent circumstances, the President may issue Government Regulations in Lieu of Law (Perpu), which must be ratified by the DPR at the next sitting, failing which they are deemed to be revoked. A Perpu becomes law upon ratification by the DPR.

At the regional level the authority to draft regulation is vested in both the regional parliament, called the DPRD, and the regional government (both at the provincial or municipal level, which includes the governor or mayor/regent).

Draft legislation becomes a regional regulation when jointly approved by the DPRD and the regional government.

2.1.3 The judiciary

The highest judicial power in Indonesia is vested in the Supreme Court. In addition to the Supreme Court, the Constitutional Court also holds an important role in upholding law and justice. Both institutions are designed to be independent agencies.

THE SUPREME COURT

The Supreme Court has the authority to review any regulation or order made under law.

Indonesia adopts a three-tiered court system consisting of the Supreme Court, the High Courts and the district courts. The Supreme Court supervises the district courts and the High Courts, and hears appeals originating from the High Courts. District courts' decisions are appealed to the High Courts. Commercial Court judgments on bankruptcy and intellectual property are appealed directly to the Supreme Court.

In addition to High Courts and district courts, which are courts of general matters (having jurisdiction in both civil and criminal cases), there are also courts dealing with particular subject matter. Courts dealing with particular subject matter include the Commercial Court (dealing with bankruptcy and intellectual property matters), industrial relation court, administrative courts, military courts, religious courts and tax courts.

THE CONSTITUTIONAL COURT

The Constitutional Court has the authority to review laws for compliance and consistency with the Constitution and to rule on: (1) disputes concerning the authority of state institutions and agencies as provided for in the Constitution; (2) dissolution of a political party; and (3) the results of general elections.

2.2 Legal system

The country is organised as a constitutional democracy and its supreme legal norms are set forth in the Constitution of the Republic of Indonesia of 1945. It is a civil law country and does not apply the doctrine of binding precedent, although judgments of the High Courts and the Supreme Court are generally persuasive. The source of its law consists of a mixture of Roman-Dutch tradition, indigenous traditional law (known as *adat* law) and Islamic law, as well as laws and regulations promulgated by the legislature (at the central and regional level) and the President, as well as the administrative rules and guidance issued by the governmental ministries and agencies. The hierarchical ordering of the recognised statutory laws in Indonesia is governed in Law No 12 of 2011, as follows:

- the Constitution;
- Decree of the People's Consultative Assembly (Ketetapan Majelis Permusyawaratan Rakyat;
- laws made by Parliament signed by the President, or Perpu;
- Government Regulation, promulgated by the President to implement a law, and can include penalties for breach only if those penalties are provided for in the relevant law;
- Presidential Regulation or Presidential Decrees issued as a public rule by the President;
- Provincial Regulation, Ministerial Regulations and Director General Regulations; and
- Regency/Municipal Regulation.

International treaties or agreements entered into by Indonesia with another country become part of the Indonesian legal system only after their ratification following a procedure prescribed by law; that is, Law No 37 on Foreign Affairs and Law No 24 of 2000 on International Treaty (as amended).

Chapter 3: Business and corporate structures

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3.1 Common forms of legal entities

Business activity in Indonesia may be conducted through incorporated or unincorporated entities. Examples of unincorporated entities include professional partnerships, *firma* partnerships and limited partnerships. Incorporated entities include limited liability companies, cooperatives, associations, foundations, higher-education institutions and churches. Additionally, Indonesian law recognises special entities performing certain functions that do not fall neatly within the aforementioned forms.

These include the Indonesian Red Cross (Palang Merah Indonesia), the Indonesia Deposit Insurance Corporation, Bank Indonesia and other institutions established based on law.

Business activity performed by foreign investors in Indonesia is generally conducted through a limited liability (non-public) foreign investment company (*penanaman modal asing* – PMA) established under Indonesian laws and domiciled within the territory of Indonesia.

Prior to incorporating a company in Indonesia, a foreign investor may choose to establish a representative office in Indonesia for the purposes of safeguarding its business interests and overseeing business development in Indonesia in anticipation of establishing a more permanent presence locally.

A representative office is not a legal entity in the eyes of Indonesian law. It exists under a licence from the Investment Coordination Board (Badan Koordinasi Penanaman Modal – BKPM). The licence is valid if the representative office continues to operate; however, it can be revoked at any time by the BKPM due to non-compliance.

A representative office's permissible scope of activity is quite narrow and may not seek earnings from sources in Indonesia or conduct trading activity.

3.2 Incorporation process

Although not specifically mandated under law, the establishment process usually begins with founders or shareholders jointly directing a notary public to reserve a company name with the Ministry of Law and Human Rights (MOLHR). The notary will electronically submit an application to MOLHR through a legal entity administration system (*sisminbakum*). The MOLHR will notify its approval or rejection (ie, another company has already registered the proposed name in the system).

The founders then need to appear in person to sign a deed of establishment (which contains the articles of the company) before the notary or appoint representing attorneys by virtue of POAs.

It is important to note that a limited liability company in Indonesia requires at least two founders and two shareholders. Founders and shareholders can either be natural persons or legal entities.

The deed of establishment then needs to be submitted (along with supporting documentation, including proof of capital injection) to the MOLHR for approval within 60 days of the signing date. This submission process will be administered by the relevant notary.

The company will obtain the legal entity status on the date of issuance of the MOLHR approval.

Subsequently, the newly established company needs to obtain a tax number, access to the government's Online Single Submission system and a company number (Nomor Induk Berusaha), as well as the relevant business licences.

3.3 Ongoing reporting and disclosure obligations

A PMA company is generally required to file the following (in addition to other disclosure obligations that may be applicable to its sector):

- a quarterly report on its capital investment activity to BKPM;
- an annual mandatory employment report to the Ministry of Manpower (MOM); and
- an annual financial report to the Ministry of Trade (Kementerian Perdagangan).

3.4 Management structures

Law No 40 of 2007 (the 'Company Law') provides for a mandatory two-tier management system consisting of a board of directors and board of commissioners.

The board of directors is responsible for the management of the company; is authorised to represent the company in its affairs; and is able to make policies and perform the day-to-day management of the company.

The board of commissioners exercises an oversight function vis-à-vis the board of directors, as well as providing the board of directors with 'advice'. The board of commissioners does not have an executive function, although it may take over the management of the company for a limited time if no board of director members are available.

3.5 Director, officer and shareholder liability

Under the Company Law, members of the board of directors and board of commissioners can be held personally liable for the company's losses if they are 'at fault' or 'negligent' in the performance of their duties in managing the company (if they are board of director members) or discharging their oversight function (if they are board of commissioner members) with the requisite good faith and responsibility.

Chapter 4: Takeovers

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There is no dedicated and comprehensive 'takeover code' under Indonesian law. Instead, additional formalities and requirements that may arise in connection with a 'change of control' are found principally in the Indonesian Company Law, supplemented by additional provisions in the Labor Law and Competition Law.

From the perspective of the Company Law, the following requirements generally apply if there is a change in the holder of more than 50 per cent of the shares in a non-public company (in addition to the regular administrative requirements vis-à-vis shareholding change):

- announcement of the shareholding change in an Indonesian newspaper with nationwide circulation (30 days prior to the shareholder resolution approving the change);
- employee notification of the shareholding change (30 days prior to the shareholder resolution approving the change); and
- ensuring that no creditors object to the shareholding change.

From the Labor Law perspective, the occurrence of a 'change of control' in the relevant company triggers certain rights to employees. Specifically, employees may decide not to continue their employment with the company post-completion, and in this context severance is payable. Therefore, in practice, the following step also needs to be considered during the documentation process and properly executed subsequently:

- settling any outstanding severance payment to employees who wish to terminate their employment contract due to shareholding change (if any).

In a public company setting, in addition to the public disclosure requirement (by way of a newspaper announcement) and Financial Services Authority (Otoritas Jasa Keuangan – OJK)/stock exchange notification rule, a change of 'controller' in a Indonesian public company triggers the general offer requirement pursuant to OJK Regulation No 9/2018 ('POJK 18'). A controller is any party:
(1) owning more than 50 per cent of the voting shares of an Indonesian public company; or
(2) with the ability to determine, directly or indirectly by any means, the management and/or policy of an Indonesian public company.

If there is an element of 'conflict' or if the transaction is performed between affiliates, additional disclosure and valuation steps need to be complied with.

Chapter 5: Foreign investment

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Law No 25 of 2007 concerning Investment (the 'Investment Law') regulates FDI by granting a right of entry to foreign businesses through licensing procedures principally controlled by the BKPM. The entity through which business activity is conducted generally takes the form of a (non-public) limited liability PMA under Indonesian law and domiciled within the territory of the Republic of Indonesia. Foreign investors' maximum ownership interest in a PMA is limited in certain industries, depending upon the targeted investment sectors or fields. The list of business sectors that are restricted or 'closed' from foreign ownership is contained in the Regulation of the President of the Republic of Indonesia No 44 of 2016 concerning the Lists of Business Fields that are Closed/Conditionally Open to Investments (commonly known as the 'Negative List').

Certain industries are overseen by their respective ministries or regulatory authorities, with the BKPM exercising a more limited role. These industries include oil and gas (managed through the Ministry of Energy and Mineral Resources and its agencies including SKKMigas), banking (regulated by the Central Bank of Indonesia), mining (managed through the Ministry of Mining and Mineral Resources), insurance (regulated by the Ministry of Finance and its agencies) and several others (including forestry, shipping, seaports and telecommunication).

All investors, regardless of nationality, are given several rights/protection under the Investment Law, inter alia, as follows:

- The government shall treat all investors, either foreign or domestic, equally.
- The government shall take no measures of nationalisation or expropriation against the proprietary rights of investors, unless provided by law. In the event that the government takes measures to nationalise, expropriate or otherwise infringe investors' rights, the government is required to pay a compensation amount established by market value.
- Investors are entitled to move their assets freely in accordance with the prevailing laws and regulations.
- Investors are entitled to transfer and repatriate in foreign currency, inter alia, capital, profits, bank interest, dividends, other income and so on.
- Investors are entitled to employ expatriates for certain positions, subject to laws and regulations.

Additionally, investors are also entitled to: (1) certainty of right, law and protection; (2) transparent information on their business sector; and (3) rights to services and various forms of facilities in accordance with the prevailing laws and regulations.

Chapter 6: Restructuring and insolvency

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6.1 Introduction

In practice, restructuring in Indonesia can be done either out of court, which is not formally regulated, or under court-supervised proceedings, regulated under Law No 37 of 2004 on Bankruptcy and Suspension of Payments (Penundaan Kewajiban Pembayaran Utang – PKPU) (the 'Bankruptcy Law').

Insolvency in Indonesia, on the other hand, commonly refers to court-supervised bankruptcy proceedings, which are regulated by the Bankruptcy Law, and dissolution and liquidation, which are regulated by Law No 40 of 2007 on Limited Liability Companies (the 'Company Law') and do not constitute court-supervised proceedings. For an entity operating in certain sectors, such as banking, insurance, pension funds and other financial activity, there are specific sets of regulations that regulate the dissolution and liquidation of such an entity, as well as an earlier supervision phase prior to entering into such an entity dissolution, in addition to the Company Law.

The term 'insolvency' as used in the Bankruptcy Law has a different meaning to many other legal systems. It does not constitute a test for bankruptcy declaration, but refers to the specific concept of 'the state of being insolvent at law', which occurs during bankruptcy or PKPU proceedings.

Under the Bankruptcy Law, there are two types of court-supervised proceedings applicable to Indonesian individuals, limited liability companies and limited partnerships: (1) bankruptcy proceedings that aim at liquidation; and (2) PKPU proceedings for the continuation of the business. Nevertheless, both are intertwined as restructuring can emerge from bankruptcy proceedings and liquidation can be the result of PKPU proceedings. In both, a debtor can submit a composition plan to its creditors to restructure its debts, which in practice may comprise a haircut, instalments, extension of maturity (ie, grace period), debt-to-equity conversion, potential investment plan from the investor or any combination of these.

The use of court-supervised proceedings for restructuring grants a debtor the ability to take the benefit of, among others, the following features: (1) automatic stay (ie, the secured creditors are unable to enforce their collateral during the stay period); and (2) cramdown (ie, the restructuring will bind all creditors except for the dissenting secured creditors in the PKPU proceedings or the secured creditors in the bankruptcy proceedings). However, if restructuring under court-supervised proceedings is not successful, the debtor's estate will be liquidated.

6.2 Court-supervised proceedings (applicable to bankruptcy and Penundaan Kewajiban Pembayaran Utang proceedings)

6.2.1 Pre-bankruptcy/PKPU

The Bankruptcy Law provides that a bankruptcy and Penundaan Kewajiban Pembayaran Utang – PKPU petition may be filed by: (1) one or more creditors; (2) the debtor; (3) the public prosecutor, if it is in the public interest; and (4) particular institutions for certain debtors: (i) banks, securities companies, stock exchanges, clearing and guarantee institutions, depository and settlement institutions, insurance and reinsurance companies, pension funds by the OJK; and (ii) state-owned companies operating in the public interest, by the Minister of Finance (MoF).

The pre-conditions for a bankruptcy/PKPU declaration to be granted are: (1) the debtor has at least two creditors; (2) the debtor has failed to pay at least one of its debts that is due and payable; and (3) the conditions above can be summarily proven. In this regard, any dispute on the amount of debt being claimed does not mean the debt's existence cannot be summarily proven.

The petition must be filed with the Commercial Court that has jurisdiction over the legal domicile of the debtor. Currently, there are five Commercial Courts in Indonesia, which are the Commercial Courts at the District Courts of: (1) Central Jakarta; (2) Medan; (3) Semarang; (4) Surabaya; and (5) Makassar.

With respect to a bankruptcy petition, the Commercial Court must make a decision within 60 days of the petition being filed. The decision can be appealed to the Supreme Court in cassation within eight days of the court's decision. The Commercial Court Registrar must deliver the cassation petition dossiers to the Supreme Court within 14 days of registration of the petition. Within 60 calendar days of the cassation petition being received by the Supreme Court,[1] it must decide whether to affirm or overturn the Commercial Court decision. In certain cases, a case review (*peninjauan kembali*) can be made against a final and binding Commercial Court decision (not appealed within the cassation filing period) or a Supreme Court decision in cassation.

With respect to a PKPU petition, the Commercial Court must make a decision either: (1) three days from the filing of a voluntary PKPU petition filed by the debtor; or (2) 20 days from the filing of an involuntary PKPU petition filed by a party other than the debtor. No cassation can be submitted against a Commercial Court decision on a PKPU petition, except by the Attorney-General for legal reasons (*kepentingan hukum*).

6.2.2 Post-bankruptcy/PKPU declaration

Bankruptcy proceedings

With respect to bankruptcy proceedings, the Bankruptcy Law provides that if the Commercial Court approves the petition, it is required to render a bankruptcy declaration and appoint one or more receiver(s) (*kurator*) and a supervisory judge (*hakim pengawas*). In bankruptcy proceedings, after the bankruptcy declaration is rendered by the Commercial Court, the affairs of the bankrupt debtor are handled and managed by one or more court-appointed receivers. The directors of the debtor (in the form of a legal entity) lose their power to manage the bankrupt debtor's affairs and estate as that power is given to the receiver. The receiver is subject to the supervision of the court-appointed supervisory judge. On the issuance of the Commercial Court decision declaring the bankruptcy of the debtor, an automatic stay or moratorium of the bankrupt debtor's estate will be triggered. The rights of secured creditors to enforce security (and the rights of any third parties to claim assets that are under the control of the bankrupt debtor or the receiver) are subject to an automatic stay for a maximum of 90 days in the bankruptcy proceedings. Under the proceedings, the automatic stay may be less than 90 days if the bankruptcy proceedings are terminated earlier or if the debtor enters a state of insolvency.

Based on the Bankruptcy Law and practice, the timeline following the bankruptcy declaration can be summarised as follows:

Table 1

Bankruptcy timeline	Schedule
Within 14 days of bankruptcy declaration	Supervisory judge to render a decision on: (1) the first creditors meeting; (2) deadline for the creditors to submit claims; and (3) claim verification meetings.
Within 5 days of the supervisory judge's decision	Receiver to announce such dates to all known creditors by letter and publication in at least two daily newspapers.
Within 1–2 weeks of bankruptcy declaration	First creditors meeting to be held.
Within 2.5–3.5 weeks of bankruptcy declaration	Deadline for the creditors to submit claims.
Within 5–7 weeks of bankruptcy declaration	Claim verification meeting is to be held.

1 According to Supreme Court Decree No 109/MA/SK/IV/2020 on the Application of Bankruptcy and PKPU Cases Operation Guidance Book dated 29 April 2020, the Supreme Court decision in cassation must be read out in a public hearing within 60 calendar days as of the date of the Panel of Supreme Court Judges appointment order.

Scenario A: The bankrupt debtor submits a composition plan at the claim verification meeting.	
A few months thereafter (could last five months or more)	• Composition plan discussions (if the bankrupt debtor offers a composition plan). • Voting on the composition plan by unsecured creditors held. • Decision to approve the composition plan requires the affirmative votes of: (1) more than half of the unsecured creditors present or represented at the meeting, whose rights are acknowledged or provisionally acknowledged; and (2) who represent at least two-thirds of the total amount of the unsecured claims of the unsecured creditors present or represented at the meeting, whose rights are acknowledged or provisionally acknowledged ('Bankruptcy Voting Quorum Requirements').
Two possible outcome scenarios:	1. Composition plan is approved by the creditors under the Bankruptcy Voting Quorum Requirements and ratified by the Commercial Court: bankruptcy proceedings are terminated and bankruptcy proceedings timeline is completed (as debtor's debts are restructured under the terms and conditions of the ratified composition plan). 2. Composition plan is rejected by the creditors (as it does not meet the Bankruptcy Voting Quorum Requirements) or is approved by the creditors but not ratified by the Commercial Court: the bankruptcy estate is declared to be in a state of insolvency and the bankruptcy proceedings timeline continues (see Scenario B).
Scenario B: The bankrupt debtor does not submit a composition plan at the claim verification meeting or Scenario A 2. occurs: the bankruptcy estate is in a state of insolvency.	
Within 1–5+ years of the state of insolvency, depending upon the complexities of the bankruptcy assets to be liquidated, such as challenges from a third party and so on.	Process to liquidate the bankruptcy estate and distribute the liquidation proceeds to the creditors in line with the prevailing laws and regulations up to completion.

PKPU proceedings

With respect to PKPU proceedings, the Bankruptcy Law provides that if the Commercial Court approves the petition, the Commercial Court is required by law to grant the debtor a provisional PKPU for up to 45 days and appoint one or more administrator(s) (*pengurus*) and a supervisory judge. The 45-day provisional PKPU may be extended up to a maximum of 270 days from the date the provisional PKPU is granted (and becomes a permanent PKPU).

After the PKPU declaration is rendered by the Commercial Court, the affairs and estate of a corporate debtor in PKPU proceedings are handled and managed jointly by the director(s) of the company and one or more court-appointed administrators. The administrator is subject to the supervision of the court-appointed supervisory judge. In this regard, the debtor will still be entitled to manage and dispose of its assets, but only jointly with the administrator. The debtor cannot engage in any management or ownership action over all or part of its assets without the approval of the administrator. Any violation of this provision will entitle the administrator to take whatever action is required to ensure that the debtor's assets are not jeopardised by the debtor's action. Performance by the debtor, without the administrator's consent, of the debtor's obligation arising after the commencement of the PKPU proceedings, can only be imposed on the debtor's assets to the extent that the debtor's assets gain advantage/benefit from this performance.

Upon the issuance of the Commercial Court decision granting the provisional PKPU, an automatic stay or moratorium of the debtor's estate will be triggered. The rights of secured creditors to enforce security (and the rights of a third party to claim its assets that are under the control of the debtor under the PKPU or the administrator) are subject to an automatic stay for the entire duration of the PKPU proceedings.

Based on the Bankruptcy Law and practice, the timeline that follows the provisional PKPU declaration can be summarised as follows:

Table 2

Provisional PKPU timeline	Schedule
Within 1–5 days of PKPU declaration	Supervisory judge to render a decision on: (1) the first creditors meeting; (2) the deadline for the creditors to submit claims; (3) the claim verification meetings; and (4) the judge deliberation hearing.
Within 1–5 days of the supervisory judge decision	Administrator to announce such dates to all known creditors by letter and publication in at least two daily newspapers.
Within 1–2 weeks of PKPU declaration	First creditors meeting held.
Within 2–3.5 weeks of PKPU declaration	Deadline for creditors to submit claims.
Within 3.5–5.5 weeks of PKPU declaration	Claim verification meeting held.
Within 4–6 weeks of PKPU declaration	Composition plan discussions/voting meeting or PKPU extension voting meeting held. In the voting process at the creditors' meeting, the decision to approve the composition plan or to extend the PKPU period or to grant a permanent PKPU requires the affirmative cumulative votes of ('PKPU Voting Quorum Requirements'): 1. (i) more than half of the unsecured creditors, who are present or represented at the meeting, whose rights are acknowledged or provisionally acknowledged; and (ii) who represent at least two-thirds of the total amount of the unsecured claims of the unsecured creditors present or represented at the meeting, whose rights are acknowledged or provisionally acknowledged; and 2. (i) more than half of the secured creditors, who are present or represented at the meeting; and (ii) who represent at least two-thirds of the total amount of secured claims of the secured creditors present or represented at the meeting.
Within 29–44 days of the PKPU declaration	Judge deliberation hearing.
Three possible scenarios:	1. (i) Debtor's request to extend the PKPU proceedings and convert the Provisional PKPU into a Permanent PKPU; or (ii) composition plan (a) is rejected by the creditors (as it does not meet the PKPU Voting Quorum Requirements); or (b) is approved by the creditors but not ratified by the Commercial Court: the PKPU proceedings are terminated and the debtor is declared bankrupt and the bankruptcy estate is automatically declared to be in a state of insolvency (see the Bankruptcy timeline for Scenario B in table one). 2. Composition plan approved by the creditors under the PKPU Voting Quorum Requirements and ratified by the Commercial Court in the judge deliberation hearing: the PKPU proceedings terminated and PKPU proceedings timeline completed (as the debtor's debts are restructured under the terms and conditions of the ratified composition plan). 3. Debtor's request to extend provisional PKPU proceedings approved by creditors either unanimously or under the PKPU Voting Quorum Requirements and ratified by the Commercial Court: PKPU proceedings timeline continues for a maximum of 270 days: see Permanent PKPU timeline below.

Table 3

Permanent PKPU timeline	
The Permanent PKPU can be granted for 15–90 days (or any other number of days decided by the Commercial Court) following the Provisional PKPU and can be extended several times. The total PKPU proceedings (which include the Provisional PKPU and the Permanent PKPU (and its extension(s)) can be granted for a maximum of 270 days.	• Composition plan discussions. • Claim verification process continues (if not already completed). • Voting on the composition plan or debtor's request to extend the Permanent PKPU. • Judge deliberation hearing with three possible scenarios in the Provisional PKPU timeline as mentioned above.
Last Permanent PKPU Extension (reaching the maximum 270-day period – if the composition plan cannot be approved by the creditors earlier) Scenario 1 (ii) a or Scenario 1 (ii) b, or Scenario 2 in the Provisional PKPU timeline mentioned above are applicable for the final outcome.	• Composition plan discussions. • Voting for the composition plan. – If the composition plan is approved, the dissenting secured creditors must be compensated with the lower value of either: the collateral (selected from the collateral value determined by the collateral documents or collateral value determined by appraiser appointed by the supervisory judge); or the actual claim directly secured by *in rem* security rights. • Judge deliberation hearing with either Scenario 1 (ii) a or Scenario 1 (ii) b, or Scenario 2 in the Provisional PKPU timeline.

6.3 Dissolution and liquidation process

According to the Company Law, a company may be dissolved due to/based on the following:

- a resolution of the general meeting of shareholders (GMS);
- the duration of the company stipulated in the articles of association has expired (and the dissolution occurs by law);
- a court order;
- upon termination of bankruptcy (proceedings) by a final and binding decision of the Commercial Court, as the bankruptcy estate of the company is insufficient to cover the costs of the bankruptcy;
- the bankruptcy estate of the company is declared to be in a state of insolvency as governed by the Bankruptcy Law; or
- the company's business permit has been revoked, thus requiring the company to implement liquidation under the laws and regulations.

Any of the above will constitute a milestone for the commencement of the dissolution and liquidation process.

With respect to the dissolution of a company that is started on the basis of a court order, the District Court (Pengadilan Negeri) may dissolve a company (and will appoint a liquidator if it declares the company dissolved) based upon the following:

- a request of the public prosecutor on the grounds that the company has violated the public interest or the company has committed an act that violates laws and regulations;
- a request from an interested party on the grounds that there is a legal defect in the deed of establishment; or
- a request from the shareholders, the board of directors or board of commissioners on the grounds that the company can no longer continue.

The criteria that mean a company 'can no longer continue' include:

- a company does not perform any business activity (is inactive/dormant) for three years or more, as substantiated by a letter of notification delivered to the tax authority;
- the addresses or whereabouts of the majority of the shareholders are no longer known, despite a notice published in newspaper advertisements, so that a GMS cannot be held;
- where the proportion of the ownership of shares in a company is such that the GMS is unable to adopt a valid resolution, for example, two groups of shareholders each own 50 per cent of the shares; or
- the assets of the company have decreased/depreciated such that, with the existing assets, the company is no longer able to continue its business activity.

The dissolution of a company must be followed by liquidation performed by a liquidator. After its dissolution, the company may not undertake any legal act unless it is required to settle its assets as part of the liquidation. The obligations of the liquidator in settling the company's assets in liquidation must include the following:

- the recording and gathering together of the company's assets and liabilities;
- an announcement of the plan for the distribution of assets/proceeds resulting from the liquidation process in a daily newspaper and State Gazette of the Republic of Indonesia;
- payment of its creditors;
- payment of the remaining balance of the assets resulting from liquidation to the shareholders; and
- other actions required to be undertaken to implement the settlement of the company's assets, including the termination of outstanding contracts and employees, tax settlement and revocation of the tax identification number, revocation of licence(s), collection of receivables, sale of assets and voluntary filing of a bankruptcy petition if the dissolved company is insolvent.

The Company Law does not prescribe a strict timeline for a dissolution and liquidation process to be completed.

Chapter 7: Employment law

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7.1 Employee rights and protections

7.1.1 Industrial relations

Employment relationships in Indonesia are regulated by Law No 13 of 2003 regarding Manpower (the 'Manpower Law') and the policies of the MOM. Any individual employment relationship is also likely to be governed by a company regulation or collective labour agreement and an individual employment agreement.

The Manpower Law requires any employer with more than ten employees to have a company regulation, which must be approved by the local Manpower Services Office. A company regulation generally repeats relevant provisions of the Manpower Law, which are mandatory in nature, while adding any matters the employer wishes to apply to its employees generally.

An employment agreement usually contains further details beyond the company regulation, as the employer may agree to for the benefit of any individual employee.

The employees of any employer with more than ten employees can unionise. Unions are enterprise-based in Indonesia. If employees choose to unionise, the union and the employer may agree to a collective labour agreement. The collective labour agreement will replace the company regulation.

Where any provisions governing an employment relationship are contradictory, the order of precedence, from highest to lowest, is: (1) the Manpower Law; (2) company regulation/collective labour agreement; and (3) employment agreement.

7.1.2 Permanent employment versus fixed-term employment

There are two main types of employment under the Manpower Law: permanent employment and fixed-term employment. These two types of employment are regulated differently.

Permanent employees are employed for an indefinite period. An employer may impose a maximum three-month probationary period on new permanent employment hires. If the probationary period was agreed in writing in an employment agreement, the employer may terminate the employment without notice, reason or obligation at any time during the probationary period.

Fixed-term employees are employed for a fixed period. A fixed-term employment agreement is only permitted for work that is temporary, completed in a short period of time, seasonal or related to a new product, a new activity or a supplemental product that is still experimental or in the exploration stage. Unlike in the case of permanent employees, an employer cannot impose a probationary period on fixed-term employees.

7.1.3 Termination

In Indonesia an employer may not generally unilaterally terminate an employee. There are a limited number of exceptions, which are termination during probation, the voluntary written resignation by the employee, retirement, expiration of the employee's fixed-term employment contract and the death of the employee.

If an employer wishes to terminate an employee and none of the above circumstances apply, the employer may either:

- negotiate and settle a separation benefits package with the employee, leading to the employee voluntarily signing a mutual termination agreement; or
- suspend the employee on full salary and follow the formal termination process mandated by law, namely mandatory non-binding mediation through the local Manpower Services Office followed by labour court proceedings to obtain court approval for the proposed termination.

The former option is generally much faster and less costly than the latter.

7.1.4 Employee statutory rights

Indonesian laws and regulations provide employees with statutory rights governing working hours, overtime payments, religious holiday allowances, leaves of absence and social security.

The Manpower Law stipulates normal working hours of not more than eight hours per day and 40 hours per week based on a five-day workweek, or seven hours per day and 40 hours per week based on a six-day workweek. These statutory working hours do not apply to certain sectors, such as the offshore oil and gas sector.

Any overtime of more than three hours per day and/or 14 hours per week requires the employer to pay for overtime rates using the formula set forth in MOM Decree No KEP.102/MEN/VII/2004 regarding Overtime Work and Overtime Pay.

7.1.5 Religious holiday allowance

Employees receive a religious holiday allowance as regulated by MOM Reg No 6 of 2016 regarding Religious Holiday Allowance for Workers/Laborers in Companies. The religious holiday allowance is paid to workers who have been employed for at least one full month prior to the relevant religious holiday (in Indonesia, Idul Fitri or Christmas), whether based on a fixed-term or permanent employment contract.

Employees who have been employed for at least 12 consecutive months are entitled to a minimum religious holiday allowance equal to one month's salary. Employees who have worked for one month but less than 12 months will receive a religious holiday allowance on a prorated basis, using the following formula: (working period/12) × one month's salary.

The religious holiday allowance is provided once a year, at the latest seven days before the particular religious holiday (again, Idul Fitri or Christmas) applicable to a given worker.

7.1.6 Leaves of absence

Employees are entitled to a minimum of 12 days of annual leave per year. In addition to annual leave, employees are entitled to paid sick leave, family and other medical leave, and pregnancy/paternal leave.

In the event of any sick leave, full wages must be paid for the first four months of sick leave; 75 per cent of full wages for the second four months; 50 per cent for the third four months; and 25 per cent thereafter until the employer terminates the employee.

The Manpower Law also allows leave for family and other medical purposes, during which the employee is entitled to his/her salary, as follows:

- the employee's wedding (three days);
- circumcision of the employee's child (two days);
- baptism of the employee's child (two days);
- marriage of a son or daughter (two days);
- death of a spouse, parent, parent-in-law, or child or son/daughter-in-law (two days);
- birth of a child or the miscarriage of the employee's wife (two days); and
- death of a family member living in the same house as the employee (one day).

Additionally, a pregnant employee is entitled to three months of maternity leave with full pay. In the event of a miscarriage, a female employee will be entitled to six weeks of paid leave. Paternity leave of two days is given to the father upon the birth of a child.

7.1.7 Social security

Pursuant to Law No 24 of 2011 regarding the Social Security Organizing Body (Badan Penyelenggara Jaminan Sosial – BPJS) (Law No 24), employers must enrol their employees working in Indonesia for a period of at least six months in BPJS social security programmes.

There are two kinds of BPJS social security programmes: BPJS Health and BPJS Employment. BJPS Health manages the health security programme and BPJS Employment oversees work accident security, old age security, pension security and death security.

Indonesian employers must make financial contributions to the BPJS social security system on the employees' behalf.

7.2 Statutory contributions and minimum wage

7.2.1 Statutory BPJS contributions

There are different contributions for the different types of BPJS programmes as discussed in section 7.1.7.

7.2.2 BPJS Health

The health security contribution, according to Presidential Regulation No 82 of 2018 regarding Health Security, as amended by Presidential Regulation No 75 of 2019, is five per cent of the employee's monthly salary. The employer pays four per cent of the contribution and the remaining one per cent is paid by deduction from the employee's salary. The maximum monthly salary for calculating the BPJS Health contribution is IDR 12m.

7.2.3 BPJS Employment: Work Accident Security

The Work Accident Security contribution is stipulated in Government Regulation No 44 of 2015 regarding the Implementation of Work Accident Security and Death Security Programmes, as amended by Government Regulation No 82 of 2019 (GR 44/2015). The amount depends on the work environment risk level, as follows:

- lowest risk: 0.24 per cent of the employee's monthly salary;
- low risk: 0.54 per cent of the employee's monthly salary;
- middle risk: 0.89 per cent of the employee's monthly salary;
- high risk: 1.27 per cent of the employee's monthly salary; and
- highest risk: 1.74 per cent of the employee's monthly salary.

7.2.4 BPJS Employment: Death Security

Pursuant to GR 44/2015, the contribution for the Death Security Program is 0.30 per cent of the employee's monthly salary.

7.2.5 BPJS Employment: Pension Security

Government Regulation No 45 of 2015 regarding the Implementation of Pension Security sets the Pension Security contribution at two per cent of the monthly salary of the relevant employee. The employer or the company is to pay two per cent of that amount and the remaining one per cent is paid by deduction from the employee's salary.

7.2.6 BPJS Employment: Old Age Security

The contribution to the Old Age Security Program is stipulated in Government Regulation No 46 of 2015 regarding the Implementation of the Old Age Security Program, as amended by Government Regulation No 60 of 2015. The amount is 5.7 per cent of the monthly salary of the employee, with 3.7 per cent paid by the employer or the company and two per cent paid by deduction from the employee's salary.

7.2.7 Minimum wage

Minimum wage is generally regulated under MOM Regulation No 15 of 2018 regarding Minimum Wage. Wages are defined as basic earnings (salary) plus regular allowances. Each province can set its own minimum wage each year, which must be complied with by employers in that province.

For example, the 2020 monthly minimum wage in Daerah Khusus Ibukota Jakarta was set at IDR 4,267,349.906, pursuant to Governor of Jakarta Regulation No 121 of 2020 regarding Provincial Minimum Wage for 2020.

Under the Manpower Law, any company paying a salary lower than the applicable minimum without MOM approval may be subject to criminal sanctions in the form of one to four years imprisonment and/or a fine of IDR 100m to IDR 400m, unless it has been given approval to do so.

An employer that is unable to meet the regional minimum wage requirement may ask the MOM or other appointed official, directly or through a business association, to suspend the application of the applicable minimum wage for that employer.

7.3 Work permits and visas

As a basic rule, the government has specified the sectors and positions in Indonesia that are open to expatriate employees. MOM Decree No 228 of 2019 regarding Certain Positions Permissible for Expatriates stipulates that 18 sectors are open to expatriate employees. These sectors include construction, real estate, education, processing industry, and information and telecommunications, among others. The same regulation stipulates 187 positions open to expatriates, for example, country manager, financial manager and business development manager.

The MOM has also provided a negative list of positions closed to expatriates, under MOM Decree No 349 of 2019 regarding Certain Positions that Are Not Permissible for Expatriates. The negative list consists of 18 positions related to human resources, including but not limited to human resources manager, career adviser, employee mediator and occupational safety specialist.

Expatriates who intend to work in Indonesia require a work permit, which the employer is required to obtain on the expatriate's behalf. Employers obtain the work permit through an online system known as the TKA Online System, which is managed by the MOM.

7.3.1 Rencana Penggunaan Tenaga Kerja Asing and notification

A work permit for an expatriate employee is comprised of two parts: (1) an Expatriate Manpower Utilisation Plan (Rencana Penggunaan Tenaga Kerja Asing – RPTKA): and (2) a Notification. Both the RPTKA and the Notification are issued by the MOM.

The RPTKA constitutes MOM approval for an employer to open a job position to expatriate hiring generally, while the Notification constitutes MOM approval to fill that position with an identified expatriate employee.

Any expatriate entering Indonesia to engage in work activity without a work permit, even if only temporarily, may be detained and deported. Since there is no legal definition of 'work', any activity apart from business negotiations leading to a trade or investment transaction must be carefully considered before being undertaken by expatriates in Indonesia.

7.3.2 Visas and stay permits

Minister of Law and Human Rights Regulation No 16 of 2018 regarding Procedures for the Issuance of Visas and Stay Permits for Expatriates requires that any expatriate intending to reside in Indonesia obtain a limited stay permit (*visa izin tinggal terbatas* – VITAS) from the Immigration Office. Any expatriate residing in Indonesia for work, together with his/her family members, must hold a VITAS in addition to the work permit.

Expatriates entering Indonesia for brief periods to engage in business meetings or negotiations do not require a VITAS, but may instead do so on a visitor visa. There are three types of visitor visa: single-entry visitor visa, multiple-entry visitor visa and visa on arrival.

In practice, a visitor visa used for business purposes is often referred to, including by Indonesian embassies or consular offices, as a 'business visa'. However, the actual wording in the regulations is 'visitor visa' (*visa kunjungan*), based on Law No 6 of 2011 regarding Immigration (Immigration Law) and Government Regulation No 31 of 2013 regarding the Implementing Regulation for the Immigration Law, as amended by Government Regulation No 26 of 2016.

Chapter 8: Tax law

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Tax law regimes in Indonesia are spread out across a number of laws. This includes corporate income tax, IIT, VAT, and/or land and building tax. The focus of this chapter is the general law on tax regimes in Indonesia which in turn comprise tax disputes and tax issues.

8.1 Overview of the law and regulatory framework

The general rules that regulate how Indonesia runs its tax regimes are based on Law No 6 of 1983 as most recently amended by Law No 16 of 2009 concerning General Terms and Procedure for Taxation (Ketentuan Umum dan Tata Cara Perpajakan – KUP). KUP regulates, among others, the tax identity number (Nomor Pokok Wajib Pajak), confirmation and revocation as a taxable company (Pengusaha Kena Pajak), tax payment procedure and/or general rules about the taxable object, which are ruled by the prevailing laws. KUP also regulates the general rule of the tax dispute procedure concerning tax objections, tax appeals and the reconsideration process. KUP regulates a general term for any tax procedure in Indonesia, except where it is regulated separately in other laws.

Under Indonesian law, tax regimes are considered as administrative law; therefore, they will generally regulate the procedure of reporting, filing a complaint, calculating tax, among others, but the violation of any tax obligation is regulated by another specific law. For example, if there is any indication of criminal activity, the case will be subject to a district court should any criminal proceeding be needed.

In general terms, tax law in Indonesia consists of several important laws, as outlined below:

8.1.1 Law No 36 of 2008 concerning Income Tax Law

Under the Income Tax Law, the tax subject consists of individual/undivided inheritance as a unit in lieu of the beneficiaries, entity and permanent establishment. For taxation purposes, a permanent establishment will be treated as a corporate taxpayer. Indonesia also recognises the WHT system for income tax (*pajak penghasilan*).

Taxation in Indonesia is determined on the basis of residency, that is, a resident and non-resident taxpayer. The Indonesian taxation system is also based on the self-assessment system, where the taxpayer will be entrusted to complete a self-assessment to calculate its tax obligation.

‘Resident taxpayer’ means: (1) an individual who resides in Indonesia and has been present in Indonesia for more than 183 days within any 12-month period, or an individual who has been residing in Indonesia within a particular taxable year and intends to reside in Indonesia; (2) an entity established or domiciled in Indonesia, except for a part of a government body that fulfils required criteria, such as its establishment is pursuant to laws, it is financed by a state budget or local government budget, its revenues are included in a state budget or local government budget and its bookkeeping is audited by a government auditor; or (3) any undivided inheritance as a unit in lieu of beneficiaries.

‘Non-resident taxpayer’ means: (1) an individual who does not reside in Indonesia and has been present in Indonesia for no more than 183 days within any 12-month period, or an entity that is not established and is not domiciled in Indonesia conducting business or carrying out activity through a permanent establishment in Indonesia; and (2) any individual who does not reside in Indonesia and has been present in Indonesia for no more than 183 days within any 12-month period, or an entity that is established outside of Indonesia and is not domiciled in Indonesia, which may receive or accrue activity through a permanent establishment.

There are two categories of income tax law: IIT and corporate income tax.

Individual income tax

IIT will be charged using progressive rates over the taxable annual income, which range from five per cent to 30 per cent. The following progressive rates are charged to taxable annual individual income:

- up to IDR 50m will charged at five per cent;
- above IDR 50m will be charged at 15 per cent;
- above IDR 250m will be charged at 25 per cent rate;
- above IDR 500m will be charged at 30 per cent.

The tax rates above apply to an Indonesian resident taxpayer. For non-residents, a tax rate of 20 per cent of the gross amount is applied. However, the tax rate may vary depending on the tax treaty between Indonesia and the country of origin of the non-resident.

Corporate income tax

Corporate income tax applies to companies domiciled in Indonesia and foreign companies that have a permanent establishment in Indonesia and carry on their business activity through a local entity. Corporate income tax will be charged at 25 per cent, with exemptions as follows:

- companies listed on the Indonesia Stock Exchange with at least 40 per cent of shares offered to the public will be charged at 20 per cent;
- SMEs with an annual gross turnover below IDR 50 bn will be charged at the 12.5 per cent rate;
- companies with an annual gross turnover below IDR 4.8bn will be charged at one per cent.

Companies investing in certain business sectors and/or certain less developed regions can also be granted tax facilities in the form of an additional net income tax reduction, accelerated depreciation and amortisation, with the period of loss carry forward extended up to ten years (certain additions might apply for certain requirements) and/or income tax on dividends at a ten per cent rate unless the tax treaty regulates a lower rate. Also, a taxpayer making a new investment in a pioneer industry but not entitled to any tax facilities under Article 31A of the Income Tax Law can also obtain an exemption or reduction of income tax based on Indonesia’s Investment Law No 25 of 2007.

8.1.2 Law No 42 of 2009 concerning Value Added Tax and Luxury Goods Sales Tax – the third and latest Amendment of Law No 8 of 1983

VAT

VAT (*pajak pertambahan nilai*) is tax charged for any taxable goods or services in their circulation from the producer to the consumer. Indonesia imposes a single VAT rate of ten per cent. However, VAT as low as zero per cent will be applied for the export of tangible taxable goods, intangible taxable goods and taxable services.

Under this law, goods shall be tangible goods that due to their nature and legal status could be chattels, real property and intangible goods. A taxable entrepreneur performs the delivery of taxable goods/a taxable service that is taxed under this law.

Under Law No 42 of 2009 Article 4 section (1), VAT shall be imposed on:

- delivery of taxable goods inside the custom area by the entrepreneur;
- import of taxable goods;
- utilisation of taxable services from outside the customs area by the entrepreneur;
- utilisation of intangible taxable goods from outside the custom area inside the custom area;
- utilisation of intangible taxable services from outside or inside the custom area;
- export of tangible taxable goods by the taxable entrepreneur;
- export of intangible taxable goods by the taxable entrepreneur; and
- export of intangible taxable services by the taxable entrepreneur.

The type of goods subject to VAT shall be certain goods within the following groups:

- mining and drilling products taken directly from their sources;
- staple goods mostly required by people;
- food and beverages served in a hotel, restaurant, food shop or shop, or similar, including dine-in and take-out food, and food and beverages presented by a catering company; and
- money, gold bullion and securities.

In addition, VAT law adopts a negative list approach. Services on which VAT is not imposed include medical services, social services, courier services with stamps, financial services, insurance services, religious services, education services, art and entertainment services, non-advertisement broadcasting services, land and water transportation services, as well as domestic air transport services that are an integral part of international air transport services, employment services, hospitality services, services that are provided by the government in the framework of the implementation of general administration, parking services, public telephone services that use coins, remittance services by postal money orders and catering services.

Luxury Goods Sales Tax

Luxury Goods Sales Tax (LGST) shall be imposed on the delivery of taxable goods categorised as luxury goods by the entrepreneur inside the custom area of its business activity, or the work and import of taxable goods categorised as luxury goods.

The tariff of LGST is at least ten per cent and no more than 200 per cent. Further, the export of taxable goods categorised as luxury goods shall be subject to ten per cent tax.

VAT or VAT and LGST on returned taxable goods may be deducted from the payable VAT or VAT and LGST within the tax period in which the taxable goods are returned.

8.1.3 Law No 12 of 1994 concerning Land and Building Tax as the Latest Amendment of Law No 12 of 1985

The subject of Land and Building Tax is any individual or entity that owns a right upon a land, and/or benefits from it, and/or owns, controls and/or benefits from the building. Land and Building Tax applies to the taxable object, such as rice fields, plantations, mining or residential and business buildings.

The basis for Land and Building Tax is the sales value of the taxable object (*Nilai Jual Objek Pajak* – NJOP). NJOP is the average price or market price of the taxable object. NJOP for land is calculated based on location, utilisation, zone allotment and environmental condition. NJOP for buildings is calculated based on the building construction material, engineering, location and environmental condition.

The tax rate for a taxable object of land and buildings amounts to 0.5 per cent. The tax rate is charged based on the sales price of the taxable price (*Nilai Jual Kena Pajak* – NJKP). NJKP is calculated from 20 per cent of the NJOP. However, under MoF Decree No 201/KMK.04/2000, a certain percentage is applied for a certain taxable object (eg, NJKP for plantations, mining and forests is 40 per cent).

8.2 Tax disputes and tax issues

Tax disputes arise between a taxpayer and authorised authority upon a decision made by the respective tax authority.[2] There are four stages that could be pursued by the taxpayer concerning tax disputes: (1) tax objection; (2) tax appeal; (3) tax lawsuits; and (4) judicial review by the Supreme Court.[3]

Under Indonesian law, a taxpayer may file a tax objection with the Directorate General of Tax (Direktorat Jenderal Pajak – DJP) against any tax assessment through the tax office. In the case that such an objection is approved or rejected in part by the DJP, the taxpayer will be subject to an administrative sanction in the form of a penalty amounting to 50 per cent of the tax assessment unpaid at the time the objection was submitted, except if the taxpayer continues the process by filing a tax appeal.

2 Directorate General of Tax, Tax Disputes Settlement (Penyelesaian Sengketa Pajak) www.pajak.go.id/id/penyelesaian-sengketa-pajak accessed 12 June 2020.

3 *Ibid*.

In the appeal process the taxpayer may appeal to the tax court within three months from the date the DJP decision is received by the taxpayer. In this case the taxpayer is required to pay a minimum of 50 per cent of the tax payable before submitting the letter of appeal. If the appeal is approved or rejected in part by the tax court, the taxpayer must pay the unpaid tax in the tax assessment, including a 100 per cent penalty of the tax assessment unpaid at the time the appeal was submitted. The taxpayer may submit a lawsuit against the authority over a dispute concerning, among others, tax collection and/or decision. Tax lawsuits must be lodged within 14 days after the tax collection or within 30 days after the tax decision is released.

The taxpayer may also challenge the tax court decision in an appeal by filing a request to the Supreme Court for judicial review. The request for judicial review can only be filed once. However, judicial review will not hinder the implementation of the tax court decision. The request for judicial review must be filed within three months after the deceit is known after the verdict or there is new written evidence, or some other prevailing reason, such as the court verdict does not correspond to the matter being claimed or if part of the claim has been decided without any consideration of the reason, or where the verdict issued is not in accordance with the prevailing laws. In this case, the Supreme Court shall investigate and decide the case within six months after the request for review is submitted.

8.3 Double tax avoidance agreement

Indonesia has a signed double tax avoidance agreement (the 'Tax Treaty') with around 67 countries. In order to claim relief under the Tax Treaty, a foreign taxpayer must complete and submit specific documents issued by the DJP. The documents are divided into two forms: DGT-1 and DGT-2. DGT-2 is applied for a company that is a banking institution or earns income from bonds or stock listed on the Indonesia Stock Exchange. Form DGT-1 is applied for other types of company excluded from DGT-2. These documents contain a certificate of domicile, which must be endorsed by the tax authority in the partner country.

Generally, the Tax Treaty will regulate tax on income imposed on behalf of each of the two states, or of their political subdivision or local authorities, and shall apply for any identical or similar taxes. For the purpose of the Tax Treaty, the resident of the contracting states will be defined according to the law of the respective state.

8.4 Tax issues

In Indonesia there are two common issues concerning tax: tax pricing and tax avoidance or evasion. Tax pricing is where the related party conducts a transaction with a price below the market price. Meanwhile, tax avoidance is where a taxpayer avoids paying tax or pays tax below the means required by the prevailing regulation.

8.4.1 Tax pricing

Regarding tax pricing, the Indonesian government has issued, through the DJP, a Guidelines and Mutual Agreement Procedure, which regulates the updated transfer pricing documentation for transfer pricing to provide greater certainty to a business subject to transfer pricing rules. Under Indonesian tax law, the DJP is authorised to adjust a taxpayer's income or costs, where the transaction between related parties is not in accordance with fair and common business practices.

Related parties are deemed to have a special relationship under the following circumstances:

- a taxpayer directly or indirectly holds 25 per cent or more of the capital of another taxpayer, or a company holds 25 per cent or more of the capital of the two taxpayers, in which case these two taxpayers are also considered to be related parties; or
- there is control through management or the use of technology, although ownership relations are not present; or
- there is a family relationship, biological or by marriage, in vertical and/or horizontal lineage of the first degree.

Further, the MoF has issued Regulation No 213/PMK.03/2016 regarding the implementation of the three-tiered documentation requirement. Under the MoF regulation, the taxpayer is required to submit a summary of the master file and local file as an attachment to the corporate return. The summary requires the taxpayer to declare that the master file and local file contain the minimum content as per the requirement and to provide the date on which the master file and local file became available as an addition to the special attachment form of the related party transaction in the annual income tax return. There is no specific deadline for the submission of the transfer pricing documentation, but such a document must be presented when requested by the tax office.

8.4.2 Tax avoidance and tax evasion

Tax avoidance is used to describe the legal arrangement of a taxpayer's business so as to reduce its tax liability. This issue circles around the existence of deficiencies or loopholes in the prevailing laws. Therefore, to minimise such an act, the Indonesian government has applied several anti-tax avoidance measures, such as: (1) Anti-Thin Capitalization regulation; (2) Controlled Foreign Corporation Rules; (3) Transfer Pricing Rule, as mentioned above; (4) Anti-Treaty Shopping; and (5) fair rules principles.

Tax evasion is the illegal act of minimising the amount of tax payment (eg, non-reporting of income or a fictive entity). The Indonesian government's approach regarding tax evasion varies in accordance with how big or small the respective case is. A small case will usually be charged with an administrative sanction; for a big case, the approach will range from an administrative sanction to criminal sanction. The procedure for any criminal charged upon taxation is regulated under MoF Regulation No 18/PMK.03/2013, which is also subject to KUP regulation.

Chapter 9: Intellectual property rights laws

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This chapter considers, at a high level, intellectual property rights (IPR) laws in Indonesia.

9.1 Regulatory framework

The intellectual property rights regime in Indonesia is regulated under several regulations, which are adjusted in accordance with the Trade Related Aspects of Intellectual Property Rights (TRIPs), as follows:

- Law No 28 of 2014 concerning Copyright;
- Law No 13 of 2016 concerning Patent;
- Law No 20 of 2016 concerning Trademarks and Geographical Indications;
- Law No 31 of 2000 concerning Industrial Design;
- Law No 32 of 2000 concerning Integrated Circuit Layout Design;
- Law No 30 of 2000 concerning Trade Secrets; and
- Law No 29 of 2000 concerning Protection of Varieties of Plants.

Generally, intellectual property rights regulation is administered by the Directorate General of Intellectual Property Rights of the Ministry of Laws and Human Rights (DGIP), excluding Plant and Variety Protection Rights, which are regulated under the Ministry of Agriculture.

9.1.1 Copyright

Under Indonesian regulations, copyright is an exclusive right of the creator automatically given under declarative principle upon realisation of a creation.[4] Copyright is an exclusive right that consists of moral rights and economic rights. Moral rights are attached to the author and cannot be transferred, while economics rights are transferable.[5] Further, the regulations also extend their protection to copyright-related rights, which relate to copyright as an exclusive right for the performer, phonogram producer or broadcasting company to produce, reproduce or broadcast its works. Although copyright protection is automatic, the copyright creator also has an option to record its right with the DGIP.

Generally, copyright protection lasts for a lifetime and continues for 70 years after the author is deceased. In this case, the holder of the copyright is a legal entity; therefore, copyright protection lasts for 50 years from publication.[6] In addition, copyright protection lasts for 50 years for the

4 Directorate General of Intellectual Property Rights, Ministry of Laws and Human Rights, definition of copyright www.dgip.go.id/pengenalan-hak-cipta accessed 5 April 2020.

5 Indonesian Law, Law No 28 of 2014 concerning Copyright, s 2.

6 *Ibid*, S IX, Art 60.

performer and phonogram producer, while it lasts for 20 years for the broadcasting company from the first time it is broadcast.[7]

9.1.2 Patent

A patent is defined as the exclusive rights granted by the state to inventors on the basis of their technological invention.[8] There are two types of patent under Indonesian law: patent and simple patent.

A patent is defined as an invention that fulfils the patent requirements, as follows:

- novelty/new;
- inventive step; and
- industrial applicability.

On the other hand, in the case of a simple patent, it is only required that the invention is novel, has industry applicability and is an improvement on an existing product/process. A simple patent does not need to have an inventive step.

Under Indonesian law patent protection lasts for 20 years and a simple patent lasts for ten years from the filing date.

Currently, Indonesian law has an integrated electronic system for intellectual property rights applications. A patent must be recorded at an intellectual property office, such as the DGIP, for protection. If there is no record of registration of the respective patent, there will be no effect on the third party for enforcement.

Patent law also prescribes rules in relation to an invention that cannot be protected under a patent, such as::

- a process or product for which its publication and use or implementation is contrary to a regulation, religious value, public order or morality;
- a diagnostic method, treatment and/or surgery applied to humans and/or animals;
- scientific theories or methods and mathematical formula; and
- living things, except micro-organisms or biological processes that are essential for producing plants or animals, non-biological processes or microbiological processes.

A patent holder may grant a licence agreement to another party. The patent must be implemented in Indonesia within 36 months of the patent rights protection being granted to support technology transfer, the absorption of the investment and/or job opportunities. Failure to conduct such support will lead to a compulsory licence and invalidation of the patent registration. Further, patent holders also have the ability to sue anyone who makes, uses, rents, delivers or infringes their patent without their consent under criminal charge.

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7 *Ibid*, Art 3.

8 Indonesian Law, Law No 13 of 2016 concerning Patent.

9.1.3 *Trademarks and geographical indications*

A trademark is defined as a distinguishable and unique sign used in industry for the trade of goods and/or services in order to indicate the origin of the goods and/or services. A trademark is an exclusive right granted by the state to the registered trademark holder for a certain period to use its own trademark or permit another party to use such a right.[9]

Under Indonesian law a trademark should be registered in order to enjoy protection. In the case of registration, the Indonesian jurisdiction upholds the principle of first to file; consequently, in the case of a dispute, the party who registered the trademark first will prevail. It is therefore vital for trademark owners proactively to register their trademarks.

The Indonesian jurisdiction also recognises the trademark application with a priority right under the Paris Convention for the Protection of Industrial Property.[10] Further, as a member of the Paris Convention, Indonesia is obligated to provide protection for well-known trademarks. Additionally, Indonesian trademark law also extends its application to cover international trademark applications under the Protocol Relating to the Madrid Agreement concerning International Registration of Marks.

Trademark protection in Indonesia lasts for ten years from the filing date and may be extended for a further ten years.[11] Trademark registration in Indonesia should be filed with the DGIP.

In the case of rights enforcement, the holder of a registered trademark can enforce its rights through the Commercial Court against any party who is using the registered trademark without a permit or through the criminal court for criminal charges against anyone for infringement.

Similar to trademark rights, geographical indications in Indonesia are also protected after their registration with the Ministry of Laws and Human Rights.[12] Without any registration, protection for geographical indication will be fragile, even though the product has been circulated among the public.

The application of geographical indication can be filed by the institution that represents society in a particular geographical region that produces products/goods, as well as by the regional government.[13] Further, geographical indications can be registered based on an international agreement. Protection for geographical indications will be given as long as it maintains the goods' reputation, quality and characteristics.[14] Under law the holder of a geographical indication right must prohibit anyone from exploiting the right without the consent of the rights holder.

9.1.4 *Industrial design*

Under Indonesian law industrial design rights are given to new industrial designs without any prior similar publication. Prior similar publication means before the filing date or the priority date for the application for priority rights for the design, or the design has been used inside or outside Indonesian

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9 Indonesian Law, Law No 20 of 2016 concerning Trademark and Geography Indication, s 1, Art 1.

10 *Ibid*, Art 9.

11 *Ibid*, Art 35.

12 *Ibid*, Art 53.

13 *Ibid*.

14 Ibid, Art 61.

territory.[15] Protection of industrial designs will not be given for any industrial design that contravenes the prevailing regulation, public policy, religion or ethics.

Industrial design rights protection is given for a ten-year period from the filing date recorded in the Design Industry Log Book and published in the Design Industry Official Publication.[16] An industrial design application originating from any Paris Convention member may claim priority rights within six months from the filing date.

Further, based on the prevailing law, the holder of industrial design rights has the exclusive right to use the industrial design and prohibit anyone from making, using, selling, importing, exporting and/or circulating the design without consent, except for certain exceptions regulated under law.

9.1.5 Trade secrets

Under Law No 30 of 2007 concerning Trade Secrets, a trade secret is defined as classified information unknown to the public in the technology and/or business field that has economic value for the business owner and is protected by the owner of the trade secret.

Protection for a trade secret right under law covers the production method, processing method, selling method or other information in the technology and/or business field that has economic value.

Further, the owner of a trade secret has the right to use the trade secret or transfer the right to another party by licensing it. Any use of a trade secret without consent is subject to criminal charges.

9.1.6 Integrated circuit layout design

Layout design refers to a three-dimensional layout design formed by various elements, with at least one active element, of which parts of or all the interconnections are an integrated circuit, and such a three-dimensional layout is meant for preparation for creating an integrated circuit. Further, under prevailing law an integrated circuit is defined as a finished or semi-finished product that contains various elements, with at least one active element, which are partly or entirely interconnected and integrated to form a semiconductor for producing electronic functions.

The integrated circuit layout design right is an exclusive right granted by the government to designers to exploit their creation. Protection for an integrated circuit layout design will be given to the original design created by the designer for ten years.[17]

The holder of an integrated circuit layout design right has a right to prohibit anyone, without consent, from creating, using, importing, exporting and/or circulating the respective integrated circuit layout design, except for research and educational purposes.[18]

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15 Indonesian Law, Law No 31 of 2000 concerning Industrial Design.

16 *Ibid*, Art 5.

17 Indonesian Law, Law No 32 of 2000 concerning Integrated Circuit Layout Design, Art1.

18 *Ibid*, Art 8.

9.1.7 *Protection of plant varieties*

Protection of plant varieties is a special protection given by the government through the Office for the Protection of Varieties of Plants for any kind of plants and varieties produced by plant breeders.[19] The protection of plant varieties is given for 20 years for seasonal types and 25 years for perennial types.

Indonesian law recognises the transfer of title in regard to the protection of plant varieties. However, such an assignment shall be recorded at the Office for the Protection of Varieties of Plants.[20] Indonesian law also regulates compulsory licensing for every person after 36 months from the date that rights are granted, to any right holders who do not implement their rights in Indonesia or implement their rights but harm public interest. Compulsory licensing is granted by a court hearing process.[21]

9.2 Current developments in Indonesian intellectual property rights law

The Indonesian government has started implementing an online integrated system for intellectual property rights registration to encourage e-filing. The government has also introduced an integrated intellectual property rights database, which escalates the process for checking the status of intellectual property rights registration and information access.[22]

Further, to accommodate national integrated services for every region concerning intellectual property rights, the integrated system also provides regional office information. Additionally, the government also aims to enhance Indonesian intellectual property rights protection by providing an online reporting system for any violation through the DGIP website.

In addition, to improve the current intellectual property rights protection law regime, the government plans to amend current intellectual property rights law to be more in line with technology trends and compliant with the international legal regime on intellectual property rights protection.

Chapter 10: Financing

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This chapter focuses on banking business in general and debt financing through bank and non-bank lending.

10.1 Banking licensing

In order to establish a bank in Indonesia and provide banking services, a party is required to obtain in-principle approval and an operating licence as a commercial or rural credit bank from the OJK.

19 Indonesian Law, Law No 29 of 2000, Art 1.

20 *Ibid*, Art 40 (3).

21 *Ibid*, Art 45.

22 Directorate General of Intellectual Property website http://en.dgip.go.id accessed 8 June 2020.

A commercial bank may engage in other activity, such as handling foreign currency, or the interim placement of capital in banks or other companies in the field of finance. The latter could include leasing, venture capital, securities companies, insurance and a central securities depository under the provisions of BI, which is the central bank, to the extent it has obtained relevant approval from OJK.

In addition to OJK, BI regulates the macroeconomic system and governs monetary policy and the payments system. These two institutions are the main regulators for the banking and financing industry in Indonesia.

The steps and procedures for obtaining the necessary banking licences are outlined below:

10.1.2 In-principle approval

In-principle approval is a preparatory licence for a bank establishment. An application for in-principle approval must be submitted by at least one of the prospective owners, along with the required supporting documents, including details of the ownership of the bank, candidates for membership of the board of commissioners and board of directors, structure of the organisation and personnel, business plan for the first three years, corporate plan, details on the operation of the bank (risk management, internal control system, good corporate governance and work system) and so on.

10.2.2 Operating licence

A business licence is granted upon completion of the preparation phase and incorporation of the legal entity. An application for a business licence must be submitted to OJK by a party that has already obtained in-principle approval together with the supporting documentation required, such as corporate documents, data on ownership, evidence of payment of paid-up capital or operational readiness and so on.

Capital injected by the shareholders cannot be a loan or financing facility in any form from a bank or other party in Indonesia, or for/from money laundering. The shareholders are required to provide a written statement to confirm the foregoing.

The members of the board of commissioners and board of directors are also required to provide a written statement confirming compliance with certain provisions stipulated in the BI regulation on the implementation of good corporate governance for banks. These include constraints on holding concurrent positions in other banks, holding stocks or shares in other companies and so on

A party that wishes to establish a bank must make a presentation to OJK on the entirety of the plan.

By regulation, the approval or rejection of in-principle approval, as well as the business licence, must be given within 60 working days of the application documents being received. During that 60-day timeline, OJK must carry out a fit and proper test for prospective controlling shareholders and candidates for membership of the board of commissioners and board of directors.

The bank must commence its operational activity within 60 working days of the business licence being obtained and must report to OJK within ten working days of the commencement of its activity.

10.2 Foreign investment restriction

Pursuant to Regulation OJK No 56/POJK.03/2016 on Share Ownership in Commercial Banks ('Reg 56/2016'), the maximum foreign shareholding in a bank is determined by the following criteria:

1. shareholder category:
   - 40 per cent of the bank's capital, for a bank financial institution and non-bank financial institution;
   - 30 per cent for a non-financial institution; and
   - 20 per cent and 25 per cent (Sharia); for individual shareholders;
2. relationship between shareholders:
   - i. any shareholder having the following relationship will be regarded as one party:
     - ownership relation;
     - family relationship up to second degree; and/or
     - any cooperation or action to achieve the same purpose in controlling the bank (acting in concert) with or without written agreement such that such an action or cooperation creates an option right to hold the shares;
   - ii. for a foreign controlling shareholder, Reg 56/2016 stipulates the following requirements:
     - commitment to support economic development in Indonesia;
     - obtaining a recommendation from the relevant financial supervisory authority;
     - a minimum rating of:
       - one rung above the lowest rating of investment for a bank financial institution;
       - two rungs above the lowest rating of investment for a non-bank financial institution; and
       - three rungs above the lowest rating of investment for a non-financial institution;
   - iii. shareholders (including foreign shareholders) may have a shareholding of more than the above limitation if they purchase the shares of:
     - (a) a bank in the handling or salvage of the Indonesia Depository Insurance Corporation; and (b) a bank with special supervision, in which within 20 years of the purchase the shareholders will adjust the shareholding threshold pursuant to Reg 56/2016;
     - a bank with intensive supervision, in which within 15 years of the purchase the shareholders will adjust the shareholding threshold pursuant to Reg 56/2016;
     - a bank that is the result of merger or amalgamation from the original bank with a good governance level at rating 1 or 2 experiences the following:

- decrease of Bank Soundness Level to rating 3, 4 or 5 within three consecutive years; or
- sale of shares at the initiative of the shareholders, the relevant controlling shareholders shall adjust their threshold pursuant to Reg 56/2016 within ten years of the merger or amalgamation;

- a bank the result of a merger or amalgamation from the original bank with a good governance level at rating 3, 4 or 5, whose shareholders must adjust their shareholding threshold pursuant to Reg 56/2016 within 20 years of the merger or amalgamation.

Notwithstanding the above, a shareholder may hold shares at more than the maximum limitation as provided in Reg 56/2016 subject to OJK discretion.[23]

10.3 Liquidity and capital adequacy

Indonesia is a member of the Basel Committee on Banking Supervision, and is therefore committed to implementing the Committee's standards for the national banking industry, including minimum capital requirements, a supervisory review process, market discipline (regulations on credit risk, market risk and Minimum Capital Provision Requirement (Kewajiban Penyediaan Modal Minimum)).

10.3.1 Liquidity requirements under Indonesian banking regulations

A bank in Indonesia must maintain minimum capital funds in rupiah (mandatory minimum deposit (*giro wajib minimum* – GWM)), which includes:

- primary GWM: minimum deposit maintained by the bank in a deposit account of BI, at approximately 6.5 per cent of the total of third-party funds; and
- secondary GWM: minimum reserves in the form of a Certificate of BI, and/or other state commercial paper, at approximately four per cent of total third-party funds.

10.3.2 Capital adequacy

Indonesia has set out obligations on minimum capital requirements for the risk profile grades of different banks, calculated on the basis of the banks' risk-weighted assets. The obligations are:

- eight per cent of a bank's risk-weighted assets for banks with grade 1 risk profile;
- nine up to ten per cent of a bank's risk-weighted assets for banks with grade 2;
- ten to 11 per cent of a bank's risk-weighted assets for banks with grade 3; and
- 11 to 14 per cent of a bank's risk-weighted assets for banks with grade 4 or 5.

Indonesian commercial banks must meet the minimum threshold for tier-1 and tier-2 capital, where common equity tier-1 (paid-up capital and disclosed reserves) is 4.5 per cent of a bank's risk-weighted

23 Art 19 of Reg 56/2016.

assets and tier-1 capital is six per cent of a bank's risk-weighted assets. Tier-2 capital is a maximum of 100 per cent of tier-1 capital, either individually or consolidated with the banks' subsidiaries.

Further, banks must set aside additional capital as a buffer against varying economic and financial risks:

- a capital conservation buffer of 2.5 per cent of the banks' risk-weighted assets, which applies to commercial banks classified as 'BUKU 3' and 'BUKU 4'. BUKU 3 is applied to banks with core capital of IDR 5tn to IDR 30tn, while BUKU 4 is for banks with core capital of more than IDR 30tn;
- a countercyclical buffer of zero per cent to 2.5 per cent of the banks' risk-weighted assets (applies to all banks); or
- capital surcharge for systemic banks of one per cent to 2.5 per cent of the banks' risk-weighted assets, which applies to systemic banks. Systemic banks are defined as those that may have a systematic financial impact on various aspects, including the amount of owned assets, capital levels and the obligations that they hold, a bank's network or relationships with other sectors, and the complexity of the bank's transactions or services. OJK has used the term Domestic Systemically Important Bank, but has replaced it with 'systemic bank' in the current regulation.

10.4 Bank and non-bank financing

10.4.1 Bank financing

Banks must have a credit or financing policy approved by their BOC to provide financing to third parties. The credit or financing policy must contain a complete and detailed procedure for providing financing for third parties, including the implementation of prudential principles and risk management, approval procedure, documentation required, supervision of financing and settlement of non-performing or bad financing. Banks must also comply with the maximum legal lending limit (*batas maksimum pemberian kredit*).

10.4.2 Non-bank financing

A non-bank institution must have an annual business plan that contains a financing plan along with a policy and procedure for providing financing to third parties. There must be a specific working unit within the non-bank institution responsible for administering and implementing the financing plan, policy and procedure. This working unit must consist of people who have knowledge and experience in the financing sector.

A non-bank institution, when providing financing to third parties, must also take into consideration financing risk and mitigate such risk by way of, among others, the implementation of a risk transfer mechanism, having the necessary insurance in place and creating securities over the assets of the debtors.

10.4.3 Offshore financing

In addition to financing from Indonesian banks and non-bank institutions, foreign banks and non-bank institutions may directly provide financing to Indonesian companies, except for microfinance institutions. Financing from foreign banks and non-bank institutions will be subject to certain requirements, such as:

- obtaining approval from the Team for Supervision of Offshore Commercial Loans ('Pinjaman Komersial Luar Negeri Team') if the loan is for the construction or development of projects with the following nature/characteristics: (1) financing must be provided on the basis of 'non-recourse', 'limited-recourse', 'advance payments', 'trustee borrowings', 'leasing' and so on; and (2) developed on the basis of build–operate–transfer, build and transfer and so on; and
- loan proceeds must be disbursed to the debtor through a Domestic Foreign Exchange Bank, a bank specifically appointed by BI by way of a letter of appointment to conduct banking activity using foreign currencies, including an Indonesian subsidiary or branch of a foreign bank, but not an overseas branch office of a bank headquartered in Indonesia.

10.4.4 Security and guarantees

Types of security interest

Lenders can take security over all present and future movable, immovable, tangible and intangible assets of the debtor. Security interests in Indonesia are limited to those prescribed by Indonesian law, namely: (1) mortgage, fiduciary security and pledge for *in rem* security interests; and (2) (corporate and personal) guarantees for personal security interests. However, in practice, lenders and debtors also enter into a contractual arrangement that can function as security and create a step-in right for the lenders (eg, a conditional assignment or novation of contractual rights and obligations or powers of attorney) despite the risk that these 'contractual securities' be deemed invalid by Indonesian courts in that they may be considered a circumvention of Indonesian security laws. It is to be noted that only the *in rem* security interest holder has preferential rights. The *in rem* security interest holder is not only entitled to foreclose on the mortgaged, pledged or fiduciary transferred property but may also satisfy its claim out of the proceeds ahead of most other creditors seeking recourse against the mortgaged, pledged or fiduciary transferred property, except for those whose claims are preferred by law (eg, claims for costs of foreclosure, costs incurred to protect the mortgaged, pledged or fiduciary transferred property from loss, and preferential claims of tax authorities).

The bankruptcy of the mortgagor, pledgor and fiduciary transferor does not, in principle, affect the security right of the mortgagee, pledgee and transferee in that the assets in question are not regarded as being part of the bankruptcy estate.

The following chart summarises the assets of an Indonesian debtor typically requested by lenders to be part of the security package and the respective security interest (both *in rem* security and contractual security) that can and would normally be taken over each asset.

Asset	Security taken
Land, plant and other fixtures	Mortgage: provided that the land has a specific land title permitted to be subject to mortgage; otherwise, these assets may be subject to a fiduciary transfer security
Movable and immovable tangible assets	Not able to be subject to mortgage: therefore, secured by a fiduciary security
Receivables and insurance proceeds	Fiduciary security
Intellectual property	Fiduciary security and POA to exercise intellectual property
Bank accounts	Pledge of bank accounts and POA to manage bank accounts
Shares	Pledge of shares, POA to sell shares and POA to vote
Contractual arrangements	Conditional assignment and POA to exercise contractual rights
Licences	POA to manage business

Guarantees in general

Under Indonesian law, the proper and timely performance by a borrower of his/her contractual obligations may be guaranteed by corporate and non-corporate third parties. Under such guarantees, upon default by the borrower, the guarantor is liable to perform the obligations that have been breached, liable to compensate the creditor for losses and damages resulting from such a breach, or both, depending on the wording of the guarantee.

Guarantees may be unlimited or the liability of the guarantor may be limited to an amount specified in the guarantee instrument. If unlimited, the guarantee will cover not only the principal amount of the loan and accrued interest, but also any and all costs and expenses incurred by the creditor in the course of attempting to collect the debt from the borrower and to enforce the guarantee against the guarantor.[24]

Under a guarantee, the guarantor cannot assume any obligations in excess of the obligations of the borrower; if and to the extent that they do, the guarantee is void.[25]

Corporate guarantees

In respect of corporate guarantees, it must be noted that Indonesian law recognises the *ultra vires* principle. This principle is not explicitly provided for in Indonesian company law, but has been developed by legal doctrine.

The existence of this principle could well entail that corporate guarantors may, under certain circumstances, maintain that guarantees issued by them are void or unenforceable on the grounds, for instance, that the objects and purposes of the guarantor's articles of association do not state that the subject company may issue guarantees, and that the subject company concerned has no commercial interest in issuing the guarantee concerned. In accepting corporate guarantees, lenders

24 Arts 1825 and 1839, Indonesian Civil Code.

25 Art 1822, Indonesian Civil Code

will be wise to examine whether there are possibilities of such instruments being contested in the future by the guarantors concerned.

Most articles of association of companies provide that the board of directors of the company must obtain the prior approval for the issue of guarantees from either the board of commissioners or the GMS. Lenders should always have to double-check whether such a requirement exists, and if so, whether the guarantor has complied with the requirement under its articles of association. Non-compliance will mean the non-enforceability of the guarantee.

Chapter 11: Privacy laws and data protection

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11.1 Legal framework

Privacy and personal data protection in Indonesia are grounded in Article 28(G) of Indonesia's Constitution, which provides that every person has the right to the protection of themselves, their families, respect, dignity and the possessions under their control. Article 28(G) also provides for security and protection from threat of fear for doing, or not doing, something that constitutes a human right.

To date there is no law or regulation in Indonesia that specifically regulates the protection of privacy. The provisions most relevant to personal data protection are set forth in the following:

- Law No 11 of 2008 regarding Electronic Information and Transactions, as amended by Law No 19 of 2016 (the 'EIT Law');
- Government Regulation No 82 of 2012 regarding the Implementation of Electronic Systems and Transactions, which was issued as procedural guidelines for the EIT Law ('GR 82');
- Government Regulation No 71 of 2019 regarding the Implementation of Electronic Systems and Transactions ('GR 71/2019'), which revoked GR 82; and
- Ministry of Communication and Informatics (MOCI) Regulation No 20 of 2016 regarding Personal Data Protection in Electronic Systems ('MOCI Reg 20/2016').

11.1.1 Consent

Essentially, consent is the core principle of data privacy protection under Indonesian data protection laws and regulations. Any process involving the collection, use or transfer of personal data can be performed only after obtaining the consent of the owner of the personal data.

Article 26(1) of the EIT Law stipulates that, unless otherwise determined by laws and regulations, the use of any information relevant to an individual's personal data through electronic means must be based on that individual's consent. Article 26(2) of the EIT Law provides that if this right is violated, the individual can file a claim for damages caused by the violation of his/her rights.

MOCI Reg 20/2016 further stipulates that displaying, announcing, sending, disseminating and/or providing access to personal data in an electronic system can only be done based on the approval of the owner of the personal data, and such consent must be 'accurate and suitable to the purpose of acquiring and collecting said data'.

11.1.2 Sanctions

As defined in MOCI Reg 20/2016, the consent of the personal data owner must be provided in writing, whether manually or electronically. Non-compliance in this respect could render an electronic system provider (ESP) subject to administrative sanctions provided under MOCI Reg 20/2016.

11.1.3 Personal data owner versus personal data controller

Although the current data protection legal framework in Indonesia is less developed than in other jurisdictions, there have been improvements as the authorities make efforts to keep pace with the country's embrace of the digital economy. For example, mirroring the EU's GDPR, GR 71/2019 recognises and makes a distinction between a personal data owner and personal data controller, although it does not provide a definition for either term.

11.2 Privacy laws and data protection in specific sectors

Aside from the personal data protection provisions discussed above, there are laws in specific sectors that require a certain degree of data protection or refer to privacy rights.

11.2.1 Health sector

Article 57 of Law No 36 of 2009 regarding Health provides that any person is entitled to the confidentiality of his/her personal health information disclosed to healthcare providers, unless disclosure is required.

11.2.2 Financial sector

Article 31(1) of the Financial Services Authority (OJK) Regulation No 1/POJK.07/2013 regarding Financial Consumer Protection expressly prohibits the disclosure of customer data and/or information by financial service providers to third parties without the prior written consent of the customer or if such disclosure is required by a lawful authority.

Article 31(3) further provides that if a financial service provider obtains the personal data and/or information of a person and/or a group of persons from a third party, it must obtain written confirmation from the third party that it obtained the consent of the personal data owner(s) for the disclosure of their personal data to the financial service provider.

11.2.3 Payment system sector

Article 14(1) of BI Regulation No 16/1/PBI/2014 regarding Protection of Payment System Service Consumers ('BI Reg 16/1/2014') requires payment system service providers to protect the confidentiality of consumers' data and/or information by way of having and implementing a consumer data and/or information protection policy. Article 15 of BI Reg 16/1/2014 prohibits payment system service providers from giving the data and/or information of consumers to another party without the prior written consent of the consumers or if such action is required under the prevailing regulations.

11.3 Data transfer

Indonesian laws and regulations do not expressly regulate the handling and transfer of non-personal data. However, any and all actions taken with respect to personal data, including cross-border data transfers, must be based on the consent of the data subject.

11.3.1 Obligations of ESPs

GR 71/2019 provides that ESPs that process personal data, which includes acquisition and collection, processing and analysis, storage, repairs and updates, appearance, announcement, transfer, dissemination or disclosure, and/or deletion or destruction, must fulfil the following obligations:

- personal data collection shall be carried out in a limited and specific manner, be legally valid and just, and be performed with the knowledge and consent of the owner of the personal data;
- personal data processing shall be carried out in accordance with its purpose;
- personal data processing shall be carried out with a guarantee for the rights of the personal data owner;
- personal data processing shall be accurate, complete, not misleading, up to date and accountable, and shall pay due regard to the purpose for processing such personal data;
- during processing personal data shall be protected against loss, misuse, illegal access, disclosure, modification or destruction.
- Personal data processing is carried out with notification to the personal data owner regarding the purpose of the collection and/or processing, and notification of any failure to protect the personal data; and
- Processed personal data shall be destroyed and/or deleted once the retention period based on the provisions of laws and regulations has ended.

11.3.2 Consent

The consent of the data owner for the use and handling of his/her personal data should be as specific as possible, covering, among other things, the transfer of the collected data to a foreign server via the internet and/or the transfer of the collected data to a foreign server after the collected data has been stored in Indonesia, if these actions are intended.

‘Consent’ is defined in Article 1(4) of MOCI Reg 20/2016 as ‘a written manual and/or electronic statement given by a personal data owner after receiving complete disclosure of the obtainment, collection, processing, analysis, storage, display, announcement, transfer and disclosure, as well as the confidentiality or non-confidentiality of, the personal data’.

Article 2(4) of MOCI Reg 20/2016 provides that consent may be given only after the owner of the personal data confirms the veracity, confidentiality or non-confidentiality, and purpose of the personal data. Article 6 of MOCI Reg 20/2016 provides that consent must be given in the Indonesian language.

11.3.3 Use of personal data

Article 14(4) of GR 71/2019 provides that in addition to the consent of the personal data owner, another person’s personal data may be used if such use satisfies one of the following requirements:

- processing an individual’s personal data in order to satisfy a contractual obligation or to satisfy the request of the personal data owner pursuant to an agreement;
- the satisfaction of a legal obligation of the personal data controller in line with applicable laws and regulations;
- guarding a vital interest of the personal data owner;
- performing a legal obligation of the personal data controller;
- performing an obligation of the personal data controller concerning public service in the public interest; and
- satisfying other lawful interests of the personal data controller and/or personal data owner.

11.3.4 Cross-border data transfer

Specifically with regard to the cross-border transfer of data, Article 22 of MOCI Reg 20/2016 provides that any ‘transfer of personal data managed by an Electronic Service Provider at a public or private institution domiciled in Indonesia to outside of Indonesia’ must comply with the following requirements:

- coordinated with the MOCI or officials/agencies authorised to handle such cross-border data transfer (the ‘Coordination Requirement’); and
- conducted according to the provisions of laws and regulations regarding the cross-border exchange of data.

At the time of writing Indonesia does not have any specific law or regulation on cross-border data exchanges as discussed above.

Article 22(2) of MOCI Reg 20/2016 provides that implementing the Coordination Requirement encompasses the following:

- reporting the planned transfer of personal data to the MOCI, with the report to include at least the names of the receiving state and the receiver, the frequency of such transfer and the reason or purpose of the transfer;
- requesting advocacy, if necessary; and
- reporting the result of the transfer.

There is no regulation to date clarifying the process or form by which parties can satisfy the Coordination Requirement.

11.4 Data onshoring

Some ESPs may be required to store their electronic data onshore in Indonesia. GR 71/2019 classifies ESPs as public scope ESPs or private scope ESPs.

11.4.1 Public scope versus private scope ESPs

Public scope ESPs are state administrative agencies (as defined therein) and institutions appointed by state administrative agencies, while private scope ESPs are individuals, business entities and the public.

GR 71/2019 requires public scope ESPs to manage, process and/or store electronic systems and electronic data in Indonesia, unless the storage technology is not available in Indonesia. Private scope ESPs are allowed to manage, process and/or store electronic systems and electronic data outside Indonesia, on the condition that they provide access to Indonesian authorities for regulatory supervision and law enforcement purposes.

11.4.2 Onshore data and disaster recovery centres

Article 99 of GR 71/2019 stipulates strategic sectors for which the government may, by separate regulation, require onshore data and disaster recovery centres. These strategic sectors include: government administration; energy and mineral resources; transportation; finance; healthcare; information technology and communications; food; defence; and other sectors determined by the President.

11.4.3 Data onshoring for the financial sector

The OJK has enacted various regulations on data onshoring requirements for the financial sector, although the requirements set out are quite general. The exception is regulations applicable to banks, namely OJK Regulation No 28/POJK.04/2016 regarding Integrated Investment Management System and OJK Circular Letter No 21/SEOJK.03/2017 regarding Implementation of Risk Management in the Utilisation of Information and Technology by Public Banks (the 'OJK Circular Letter 21/2017').

Section 3.2.1 of the Annex to OJK Circular Letter 21/2017 in particular sets out technical requirements applicable to the providers of data centres for public banks. These requirements include control over physical access to the data centre (ie, the installation of biometric devices), control over an uninterruptible power supply, and reliable fire and smoke detectors. Data centre providers are further required by section 9.2.2 (16) of the Annex to OJK Circular Letter 21/2017 to submit an annual audited financial report and audited information technology report to the OJK through its bank customers.

11.5 Looking ahead

Privacy and data protection in Indonesia are loosely regulated at the moment under the EIT Law, GR 71/2019 and MOCI Reg 20/2016. That could soon change. A law on data protection is included in the Prioritized National Legislation Program (Program Legislasi Nasional Prioritas or 'Prolegnas') of the House of Representatives, accessible at www.dpr.go.id/uu/prolegnas. So while it appears that the new law could be here sooner rather than later, an MOCI official was unable to provide a timeframe for when the new data protection law will be enacted.

News reports also indicate that a number of government officials have expressed interest in reviewing and revising the EIT Law and the Telecommunications Law. However, the current Prolegnas does not include any planned amendments to these laws.

Lastly, based on discussions with another MOCI official, there are ongoing talks about enacting a new MOCI regulation in response to GR 71/2019 that will regulate the implementation and enforcement of the ESP registration requirement. However, the official was unable to say when the new regulation might be enacted, and there is no draft of the proposed regulation currently available to the public.

Chapter 12: Competition law

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Law No 5 of 1999 concerning the Prohibition of Monopolistic Practices and Unfair Business Competition (the 'Competition Law') prohibits any agreement or conduct that can cause monopolistic practices or unfair business competition, including: (1) anti-competitive horizontal agreements; (2) abuse of dominance; and (3) anti-competitive mergers.

Komisi Pengawasan Persaingan Usaha is an independent agency established in 2000 to enforce the Competition Law.

12.1 Anti-competitive agreements

The following agreements are per se prohibited (ie, no demonstration of anti-competitive effect is required) under the Competition Law:

- a price-fixing arrangement among producers in the same relevant market;
- an arrangement to price discriminate among consumers;

- an arrangement to boycott other enterprises from engaging in the same type of business or access to sell or buy goods and services; and
- an exclusive arrangement restricting resale and supply.

The following are examples of agreements that are prohibited to the extent that they can be demonstrated to result in an anti-competitive effect or unfair business practices:

- an arrangement to jointly control production or the market (oligopoly);
- an arrangement between competitors to fix a price below the market (predatory pricing);
- an arrangement to support the resale price;
- an arrangement that will lead to market partitioning or allocation;
- an arrangement between competitors to influence the price by determining production (cartels);
- an arrangement to establish a joint or large company by keeping and maintaining the continuity of each respective company or its members, with the aim of controlling production (trust);
- an arrangement to jointly control the purchase or acquisition of supplies to control prices (oligopsony);
- an arrangement to control the production of goods included in the production chain (vertical integration); and
- an arrangement with foreign parties setting forth conditions that may cause monopolistic practices or unfair business competition.

12.2 Abuse of dominance

An enterprise with a dominant position is prohibited from:

- imposing trade terms with the intention of preventing and/or hampering the consumers acquisition of goods and/or services competitively, in respect of price or quality;
- restricting the market and technology development;
- hampering other entrepreneurs from potentially becoming a competitor in the relevant market; or
- engaging in price discrimination, predatory pricing, interlocking management in competing companies, or owning or creating a majority shareholding in several companies in the same market.

12.3 Anti-competitive merger

Article 28 of the Competition Law prohibits a business from conducting mergers, dissolving companies or acquiring shares of other enterprises if doing so causes monopolistic practices and/or unfair business competition.

Chapter 13: Dispute resolution

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13.1 Structure of the courts

The 1945 Constitution of the Republic of Indonesia granted independent judicial power in Indonesia to be exercised by the Supreme Court and its branches, which will be elaborated on further below.

13.1.1 Supreme Court

The Supreme Court is the highest tier of the Indonesian court hierarchy among all branches of court, and is responsible for the organisation, administration and financial management of subsidiary courts in its respective jurisdiction, in accordance with the applicable laws and regulations of each individual court. Cases from every branch of jurisdiction, as well as from specialised courts, end up in the Supreme Court as the final stage. It is situated in the capital of the Republic of Indonesia and comprises a maximum of 60 Supreme Court justices.

The Supreme Court has jurisdiction over the following matters:

- cassation petitions;
- disputes between courts over jurisdiction;
- petitions for civil review (*peninjauan kembali*) for a final and binding court decision;
- review of legislation below the level of a law, for example, Government Regulations, Presidential Decrees and Ministerial Regulations (Uji Materiil);
- performing the highest supervision over the conduct of its subsidiary judicial institutions from all branches; and
- internal supervision of the conduct of Supreme Court justices, while external supervision is carried out by the Judicial Commission.

Pursuant to the 1945 Constitution, the Supreme Court has four branches of jurisdiction, and additionally manages and supervises special jurisdiction courts that have been established to handle specific cases.

General Jurisdiction

The General Jurisdiction is a branch of the Supreme Court with jurisdiction to hear both criminal and civil cases and is carried out by the district courts and High Courts.

District courts are the first-instance court for General Jurisdiction and are established in every city and regency, but with jurisdiction limited to the borders of their cities or regencies.

High Courts are courts of appeal and are established in every provincial capital city with their jurisdiction limited to their respective province.

Administrative Jurisdiction

The Administrative Jurisdiction is a branch of the Supreme Court set up to examine, adjudicate and determine state administrative disputes, that is, disputes between private individuals/entities and executive government entities, for which the subject matter can either be a decree issued by a government official or failure to take decisive action by not issuing a decree within a reasonable timeframe as provided for under prevailing laws and regulations.

Religious Affairs Jurisdiction

Religious Affairs Courts (Pengadilan Agama), along with Religious Affairs High Courts (Pengadilan Tinggi Agama), are a branch of the Supreme Court with specific judicial power to hear disputes between Indonesian residents of the Islamic faith and corporations that voluntarily follow Islamic teachings.

Military Jurisdiction

The courts in the Military Jurisdiction serve to examine, adjudicate and decide criminal cases involving military personnel and objections against Military Administrative Decrees (Keputusan Tata Usaha Angkatan Bersenjata). In essence, the courts in the Military Jurisdiction guard and protect Indonesian citizens from the misconduct of military personnel, whether as a result of criminal acts or Military Administrative Decrees that are inconsistent with prevailing laws and regulations.

Special jurisdiction courts

In previous years not all Supreme Court branches have been sufficiently prepared to handle the numerous legal complexities presented to them, due to the fluctuating rate of social and legal developments across the country. In response, special jurisdiction courts were established to handle specific cases, such as the Tax Court, Human Rights Court, and Commercial, Juvenile, Fisheries, Industrial Relations and Anti-Corruption Courts.

13.2 Arbitration

Arbitration is commonly used as a dispute settlement mechanism, especially for commercial disputes in Indonesia.

The main source of arbitration law is found in Law No 30 of 1999 on Arbitration and Alternative Dispute Resolution (the 'Arbitration Law'), promulgated on 12 August 1999. It was not modelled on the UNCITRAL Model Law on International Commercial Arbitration.

Article 1(9) of the Arbitration Law defines an international arbitration award as 'an award handed down by an arbitration institution or individual arbitrator outside the jurisdiction of the Republic of Indonesia, or an award by an arbitration institution or individual arbitrator, which under the provisions of laws of the Republic of Indonesia is deemed an international arbitration award'. It can be inferred that a domestic arbitration award is an award issued within the jurisdiction of Indonesia.

While no express distinction exists between 'domestic' and 'international' arbitration proceedings other than what can be inferred by Article 1(9) above, one can conclude that the Arbitration Law only regulates the procedures for domestic arbitration. The following overview outlines domestic arbitration, excluding the enforcement of international arbitration awards.

13.2.1 Arbitration agreement

In line with the Arbitration Law, an arbitration agreement must be made in writing and signed by the parties, and may be in the form of: (1) an arbitration clause contained in a written agreement made *prior to* the dispute; or (2) an agreement specially entered into by the parties *after* the outset of the dispute (*acta compromis*). Alternatively, the parties may make a separate arbitration agreement in notarial deed form.

In the event of an arbitration agreement made *prior to* the dispute, Article 2 of the Arbitration Law requires that it *clearly states* that all disputes that arise or may arise from a legal relationship between the parties must be settled by means of arbitration. If an arbitration agreement is made *after* the dispute arises, Article 9(3) requires that the agreement include, at least:

- the subject matter of the dispute;
- the full names and addresses of the parties;
- the full name(s) and residential address(es) of the arbitrator or the members of the tribunal;
- the place where the arbitrator or the tribunal will render its/their award;
- the full name of the secretary to the arbitrator or the tribunal;
- the time period within which the arbitration is to be completed;
- a statement from the arbitrator(s) accepting their appointment as such; and
- a statement from the disputing parties that they will bear all costs of the arbitration.

13.2.2 Arbitrability

Article 4(3) of the Arbitration Law implies that an arbitration agreement is deemed to be reached when the agreement to arbitrate is contained in an exchange of letters made by means of communication that provides a record of their content; however, the dispatch of the letters by telex, telegram, facsimile, email or other telecommunications facilities must be accompanied by a note of receipt by the parties.

The general approach to decide whether certain subject matter is arbitrable is provided under Article 5(1), which provides that disputes can be settled by means of arbitration if they are of a commercial nature and involve the rights of the disputed parties. Article 5(2) goes on to provide that disputes that cannot be resolved by arbitration are those for which, according to regulations having the force of law, no amicable settlement is possible. These include criminal matters, bankruptcy, adoption and so on. The elucidation to Article 66 offers more intelligible examples of a commercial nature, such as, among others, activity in commerce, banking, finance, investment and intellectual property rights.

13.2.3 *Kompetenz-kompetenz doctrine*

Although the Arbitration Law does not provide specific provisions regarding the *kompetenz-kompetenz* doctrine, Articles 3 and 11 of the Arbitration Law, which prohibit Indonesian courts from becoming involved in arbitration, imply that the arbitration tribunal has the authority to determine its own jurisdiction.

13.2.4 *Preliminary award or interim relief*

Article 32 (1) of the Arbitration Law grants authority to the arbitration tribunal at the request of one party to issue a preliminary award or interim relief, which deals with the manner of running the examination of the dispute, including imposing a security attachment, ordering the deposit of goods with third parties or the sale of perishable goods. However, the Arbitration Law is silent on the procedure to enforce preliminary awards and interim relief.

13.2.5 *Disclosure/discovery*

The Arbitration Law is silent on the arbitrator's authority to order disclosure/discovery. Nevertheless, Article 46(3) of the Arbitration Law stipulates that the arbitrator has the authority to request the parties produce additional written explanations, documents or other evidence deemed necessary within a time period determined by the arbitrator.

13.2.6 *Recourse against an arbitration award*

Within the context of domestic arbitration, the only available recourse against an arbitration award is to annul it or to resist its enforcement.

Articles 70 and 71 of the Arbitration Law provide that parties may file an application for annulment of an arbitration award with the relevant district court on the following grounds:

- letters or documents submitted at the hearings are acknowledged to be false or forged, or are declared to be forgeries after the award has been rendered;
- after the award has been rendered, documents are found that are decisive in nature and were deliberately concealed by the opposing party; or
- the award was rendered as a result of fraud committed by one of the parties to the dispute.

Meanwhile, a party may resist the enforcement of an arbitration award if it establishes that the award concerned violates public policy, as outlined under Article 62(2) of the Arbitration Law.

Under Article 4(2) of Supreme Court Regulation No 1 of 1990, public policy is defined as the fundamental principles of the Indonesian legal system and society. This definition is rather general, but no further elaboration is provided. In practice, the court has and often will exercise wide discretion to interpret this term on a case-by-case basis.

The recognition and enforcement of domestic and international arbitration awards is discussed below.

13.2.7 Recognition and enforcement of domestic and international arbitration awards

Domestic arbitration awards

For a domestic arbitration award, the procedure for enforcement is as follows:

- the tribunal, or its authorised proxy, must deliver and register the original or an authentic copy of the award to the Clerk of the District Court within 30 days of the award's issuance (Article 59(1) of the Arbitration Law);
- failure to register the arbitration award pursuant to the above requirement will render the award unenforceable (Article 59(4) of the Arbitration Law);
- if the losing party fails to perform its obligations under the arbitration award, it will be enforced by order of the Chief Judge of the District Court at the request of the winning party (Article 61 of the Arbitration Law);
- the order of the Chief Judge will be rendered within 30 days of the filing of the request for execution with the Clerk of the District Court (Article 62(1) of the Arbitration Law); however, in practice, the issuance of the order may take longer; and
- the Chief Judge of the District Court must first examine the arbitration award to determine whether it is based on a valid arbitration agreement, if the dispute is arbitrable as a matter of law, and that the award is consistent with good morals and public policy (Article 62 (2) of the Arbitration Law).

The decision of the Chief Judge of the District Court that an award is not enforceable for the above reasons cannot be appealed (Article 62(3) of the Arbitration Law). Further, the Chief Judge of the District Court must not examine the reasoning for the arbitration award (Article 62(4) of the Arbitration Law).

Once endorsed for enforcement by the Chief Judge of the District Court, the award may be executed in the same manner as a final and binding court decision in a civil case.

International arbitration awards

Under Articles 65–66 of the Arbitration Law, the enforcement of an international arbitration award must be applied for at the District Court of Central Jakarta. The award concerned must fulfil the following requirements:

- it is issued by an arbitrator or arbitration tribunal in a country with which Indonesia has a treaty, whether bilateral or multilateral, regarding the recognition and enforcement of an international arbitration award;
- it is in the domain of commercial law according to Indonesian law; and
- it does not violate Indonesian rules of public policy.

The award may be enforced after obtaining an *exequatur* (a writ of enforcement) from the Chairman of the District Court of Central Jakarta. The Arbitration Law requires, as a prerequisite to the issuance of an *exequatur*, the registration of the award directly by the arbitrator(s) or by the disputing parties who have been granted authority to represent the arbitrator(s) by POA. In practice, the latter is commonly chosen as it is more practicable. The POA must be notarised and further legalised by the Indonesian Consulate/Embassy with jurisdiction over the arbitrator or arbitration institution (for institutional arbitration). The following documents must be submitted when registering the award:

- an original or authentic copy of the international arbitration award and a sworn translation in the Indonesian language;
- an original or authentic copy of the arbitration agreement and a sworn translation in the Indonesian language;
- an official statement from the diplomatic representative of the Republic of Indonesia in the country where the international arbitration award was issued, certifying that that country is a party to bilateral and multilateral agreements on the recognition and execution of international arbitration decisions (the New York Convention) with Indonesia;
- a notarised and legalised POA from the arbitrator(s) to the disputing parties to register and enforce the award at the District Court of Central Jakarta; and
- a notarised and legalised substitution POA from the party seeking to enforce the award to its legal representative (in the case where the party is represented by lawyers) to register and enforce the award at the District Court of Central Jakarta.

13.3 Other forms of dispute resolution

In addition to arbitration, Indonesia also recognises other ADR mechanisms, such as consultation, negotiation, mediation, conciliation and expert determination. In fact, parties are given the freedom to set their own dispute mechanism, such as the adoption of a dispute adjudication board, which is quite common in the construction sector.

Compared with arbitration, other forms of dispute resolution are even less regulated. Under the Arbitration Law, there is only Article 6 touches on this area. This single article mentions the possibility of parties settling their dispute out of court. There are three scenarios:

1. The resolution is done by direct meeting for a maximum of 14 days, resulting in a written settlement agreement (*kesepakatan tertulis*).
2. If (1) fails, based on mutual agreement, the dispute can further be settled with assistance from an expert or mediator. If the parties are unable jointly to agree when appointing an expert or mediator, they may seek assistance from a dispute resolution institution to. The period for this process is limited to 30 days. The same as in (1), the end result is a written settlement agreement.
3. If (2) fails, also based on the parties' mutual agreement, the dispute may further be referred to arbitration.

As with an arbitration award, a written settlement is final and binding. It must be registered with the district court within 30 days of its signing date and must be enforced within 30 days following registration.

As a side note, while Indonesia recognises other forms of dispute resolution, to date it still has not ratified the Singapore Convention. Accordingly, the above provisions are only applicable to domestic settlement agreements.

Japan

Chapter 1: Introduction

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Japan has a population of around 126 million people and a GDP of around $5tn. It is ranked 29th in the *Doing Business 2020* listing published by the World Bank. It also belongs in the top tier for various issues such as resolving insolvency, dealing with construction permits and obtaining electricity. Japan is also ranked 106th out of 190 countries for ease of starting a business.

Generally speaking, most industries in Japan are subject to certain levels of governmental regulations. These regulations are considered as one of several difficulties to confront foreign companies that look to invest and operate in Japan. They also make it difficult and burdensome for businesses to embark on innovative projects. The Japanese government has been simplifying regulations and administrative procedures relating to foreign companies and new businesses, but given Japan's *Doing Business* ranking, there is no doubt that a lot more needs to be done.

Japan is a civil law country, with a unitary rather than federal system of government. In addition to statutory codes, case law plays an important role in practice, even though court precedents (except for Supreme Court decisions) do not have legally binding authority. Moreover, although statutory codes are fundamental, government authorities have strong discretionary administrative powers to issue ordinances, orders and guidelines, which are regarded as important forms of administrative law. In recent years the government has been issuing guidelines in various circumstances; these guidelines function effectively as domestic soft law in Japan. Further, Japan tends to track regulations in Europe and the US and its regulations are mostly in line with global standards.

Japan is seen as one of the least corrupt countries in the world. However, in recent years there have been cases involving non-compliance with legal and ethical standards by Japanese companies, such as accounting fraud and falsification of quality standards.

Chapter 2: The business environment

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2.1 Government structure

Japan is a unitary, rather than a federal, state. In other words, the central government represents the country and has ultimate sovereignty. The role of the state is divided into three branches: legislative, judicial and administrative. The organs responsible for each branch are independent and mutually checking, in a system of checks and balances.

The separation of powers was recognised under the Constitution of the Empire of Japan (the 'Meiji Constitution'; the first modern constitution of Japan promulgated in 1889) before the Second World War, but because the Emperor had the right of absolute sovereignty ('The Emperor.... combining in

Himself the rights of sovereignty'), the separation of powers was insufficient under the Constitution of the Empire of Japan. The current Constitution of Japan (promulgated in 1946; during the occupation based on the Potsdam Declaration, it was enacted based on the draft of General Headquarters, the Supreme Commander for the Allied Powers through the process of constitutional amendment under the Meiji Constitution) clarifies the sovereignty of the people (Preamble and Article 1 of the Constitution). Under the current Constitution of Japan, the Emperor does not have authority concerning national administration as the symbol of Japan, and legislative power is vested in the Diet (Article 41 of the Constitution); executive power is vested in the Cabinet (Article 65 of the Constitution); and judicial power is vested in the courts (Article 76 of the Constitution). The Diet consists of two houses (bicameral legislature) and both houses (the House of Representatives and the House of Councillors) in Japan are composed of elected members.

The current Constitution of Japan adopts a parliamentary cabinet system (not a presidential system, but a system similar to that in the UK in this regard) based on the recognition of the separation of powers. The Diet can designate the Prime Minister (Article 67 of the Constitution) and pass a no-confidence resolution against the Cabinet (Article 69 of the Constitution), while the Cabinet has the right to dissolve the House of Representatives. The courts may conduct a constitutional review of laws; however, the courts may do so only in connection with a trial in an ordinary case in which the application of laws is at issue (using the US regime of standing and differing from the German constitutional court system).

Although Japan is not a federal state, the Constitution of Japan guarantees a system of local government (Articles 92–95 of the Constitution), and local governments, in addition to the central government, also engage in politics and administration in local areas. Local governments are divided into prefectures and municipalities. In accordance with the laws stipulated by the Diet, local governments are entrusted by the national government with some of the affairs carried out by the national government, and have responsibility for performing independent and comprehensive administration closely related to local residents (Articles 1–2, Paragraph 1 of the Local Autonomy Act). Local governments can enact ordinances (prefectural or municipal ordinance) within the scope of the law (Article 94 of the Constitution).

Matters relating to investment from foreign countries in Japan are essentially considered to be administrative matters for the national government and are regulated by acts determined by the Diet, or by cabinet orders (determined by the Cabinet) and ministerial ordinances (determined by the ministries) for the enforcement of the laws. However, with respect to certain matters (eg, in Comprehensive Special Zones), local government ordinances (prefectural or municipal ordinance) may be established in place of cabinet orders or ministerial ordinances.

2.2 Legal system

Since a series of political reforms modernising Japan in the Meiji Period (1868–1912), Japan has been a civil law country. The old Meiji Constitution promulgated in 1889 was enacted in accordance with the Constitution of Prussia (1850) in Germany, and the current Civil Code enforced in 1898 was enacted following the German and French Civil Codes. The current Penal Code, which came into effect in 1908, was also enacted after the complete revision of the former Penal Code, which was enacted in 1882 based on the French Penal Code, with reference to the German Penal Code and other relevant laws. Japan adopts a codified law system in which all legal norms, such as the Constitution and laws, are enacted in written form. The current Constitution of Japan is the supreme law in the domestic legal order. Unlike in common law countries, precedents have no binding force and only *de facto* influence on similar cases.

The current Constitution of Japan was promulgated in 1946 under a strong American influence, and the Companies Act was also revised many times after the Second World War under the influence of US law, including major revisions in 1950 and 2005. The Act on Prohibition of Private Monopolization and Maintenance of Fair Trade was enacted in 1947, adopting US antitrust law as its model. The Financial Instruments and Exchange Act (formerly, the Securities and Exchange Act) was also enacted in 1948, subject to the influence of the Securities Exchange Act of the US. Thus, current Japanese law has been influenced not only by Continental law, but also by Anglo-American law.

The courts of justice exercise their powers independently of other organs (ie, the Diet and the Cabinet). The courts are passive organs that properly settle disputes and maintain legal order by interpreting and applying law to the disputes brought before them. Furthermore, under the current Constitution of Japan, administrative tribunals are not permitted final judicial power (Article 76 of the Constitution). The supreme judicial body is the Supreme Court. The Supreme Court, as the sole court of last resort, has jurisdiction over appeals and special appeals. In addition, the Supreme Court has the power to make rules on court proceedings and internal discipline, as well as the power to appoint lower court judges and review constitutionality.

Chapter 3: Business and corporate structures

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3.1 Common legal entities

Foreign individuals or entities may conduct business in Japan either directly or through a Japanese corporation or branch office. The three types of legal entities most commonly used by foreign investors in Japan are stock companies (*kabushiki kaisha* – KK), general partnership companies (*godo kaisha* – GK) and branch offices. Among them, the KK is the most common entity used to operate a business in Japan.

The liabilities of both a shareholder of a KK and a member of a GK are limited to the extent of the assets such a shareholder or member invested in the entity. In the case of a GK, only contributing members are allowed to be representative members and members in charge of the operation of the GK (an 'Executive Member') (this can include legal entities, such as a corporation, although a natural person must be appointed as a representative thereof). On the other hand, in a KK separation of ownership and management means that the owners of a business do not always execute the business of the KK (in addition, legal entities are not entitled to become officers of a KK). In terms of the corporate structure, a GK is more flexible than a KK under the Companies Act in Japan. For example, members of a GK can decide the percentage of profit and loss distribution among them by mutual agreement between the members or in the GK's articles of incorporation, which means that the distribution ratio is not fixed based on their ownership percentages. Although both a KK's shareholders and a GK's members can make investments in kind, such as the contribution of intellectual property, a GK has an easier procedure for making investments in kind. However, unlike a KK, a GK is not permitted to be listed on a financial instruments exchange in Japan.

Other than the three popular types of legal entities described above, limited partnership companies and limited liability companies are also permitted under the Companies Act, and partnerships are permitted under the Civil Code. In addition, limited liability partnerships and investment limited partnerships are also permitted under the Limited Partnership Act and so on. These entities are used, as appropriate, for investment purposes.

3.2 Incorporation process

A KK or GK is legally formed upon registering its formation at the Legal Affairs Bureau with jurisdiction over the location of its head office. Such a registration requires preparing the articles of incorporation (in the case of a KK, the notarisation of its articles of incorporation by a notary public is also required), and subscription of shares for capital contribution, among other matters. The initial capital contribution to a KK or GK must be in assets such as cash. There is no minimum capital requirement, although such initial capital cannot be zero. Accordingly, a KK or GK can be incorporated with a capital of JPY 1.

In practice, it usually takes three weeks to one month to complete the registration, taking into account the time necessary for drafting the articles of incorporation (and notarisation in the case of a KK), verification of signature and purchase of a corporate seal, plus an additional week to complete the registration application at the Legal Affairs Bureau. This is quite slow by international standards. As such, the Japanese government plans to establish a new one-stop online incorporation system by April 2021.

Previously, at least one representative director must have been a resident of Japan. However, this restriction was removed in 2015.

Under the Foreign Exchange and Foreign Trade Act (FEFTA), incorporation by a foreign investor is generally considered as 'inward direct investments, etc', which will require a *post facto* report or, in exceptional cases, prior notification to the Ministry of Finance and other relevant ministers through the Bank of Japan. In 2019 the range of businesses subject to the prior notification requirement was expanded to address growing concerns about cybersecurity.

3.3 Ongoing reporting and disclosure obligations

The directors of a KK must submit or provide financial statements and business reports to annual shareholders' meetings, and the shareholders must approve such documents. A KK generally must give public notice (through the official gazette (*Kampō*), a daily newspaper or via an internet announcement) of its balance sheet (or, for large companies as prescribed in the Companies Act, its balance sheet and profit and loss statement) promptly after the conclusion of the annual shareholders' meeting. At a GK, the members do not need to bear the obligations listed above. However, both types of companies must keep financial statements at their head office for a prescribed period. Shareholders of a KK and members of a GK may inspect or copy such financial statements at any time.

As described above, a KK or GK is formed by registering its incorporation. The main items included in such a registration are its trade name; head office location; business purpose; total number of shares issued (in the case of a KK); type and number of issued shares (in the case of a KK); amount of initial capital; and the names of the director(s), the representative director, and auditor(s) (in the case of a GK, the name of the representative member and the Executive Member); and if an Executive Member is a legal entity, then the name of a natural person who is to perform the duties of such a member ('Functional Manager'). Registration of the composition of shareholders or members is not required, and such information is not generally disclosed to the public. When any resolution is passed at a shareholders' meeting, members meeting or board of directors meeting regarding a change in one of the company's registered matters listed above, such a change must be filed with the Legal Affairs Bureau.

3.4 Management structures

The Companies Act allows the creation of the following corporate organisations within a KK: a shareholders' meeting, director, board of directors (consisting of at least three directors), executive officer (in the case of a company with three committees), statutory auditor, board of statutory auditors (consisting of at least three statutory auditors), committees (including a nominating committee, audit committee and compensation committee), accounting auditor and accounting adviser. All KKs are required to have a shareholders' meeting and one director. All other corporate organisations listed above are optional unless the company is: (1) a 'large company', which is defined under the Companies Act as a KK with stated capital of JPY 500m or more, or with aggregate debt of JPY 20bn or more; or (2) a 'public company', which is defined as a KK that does not restrict the transfer of all or part of its shares under its articles of incorporation.

The Companies Act also provides for three corporate governance systems for a KK (mainly for large companies): (1) company with a board of statutory auditors; (2) company with three committees as described above (each committee must consist of at least three directors and the majority of the members of each committee must be outside directors); and (3) company with an audit and supervisory committee consisting of at least three directors who are elected as audit and supervisory committee members at a shareholders' meeting (the majority of the members of such a committee must be outside directors).

Of the systems described above, very small KKs often choose simply to have one or more directors. In the case of a small or medium-sized KK, a board of directors and one or more statutory auditors is typical. Large companies typically choose one of the following three patterns: (1) board of directors, board of statutory auditors and accounting auditor; (2) board of directors, three committees and accounting auditor; or (3) board of directors, audit and supervisory committee, and accounting auditor.

In the case of a company with three committees, a (representative) executive officer elected by the board of directors executes the business of the company. In the case of companies other than companies with three committees, a representative director elected by the board of directors (in the case of a company without a board of directors, such a representative director is elected at a shareholders' meeting) executes the business of the company.

In the case of a GK, members of the GK execute the business of the GK unless otherwise provided for in the articles of incorporation. If a member who executes the business is provided for in the articles of incorporation, only such a member (ie, an Executive Member) can execute the business of the GK. Since the name of any representative member and Executive Member is disclosed in the registration, if a member wishes not to have his/her name disclosed in the registration, then the GK has to provide for Executive Member(s) in its articles of incorporation. Each Executive Member represents the GK, unless one or more representative members are appointed in the articles of incorporation (or by and from such a member in accordance with a process provided for in the provisions of the articles of incorporation). If an Executive Member is a legal entity, then such a legal entity must appoint a natural person who is to perform the duties of such member (ie, a functional manager).

3.5 Director, officer and shareholder liability

In the case of a KK, directors, statutory auditors, accounting auditors, accounting advisers and executive officers owe the duty of care of a good manager to the company in carrying out their duties. In the case of a GK, members in charge of the operation owe the same duty. If they cause damage to the company in breach of such a duty, they are personally liable for such damage. However, if their decisions in carrying out the business of the company satisfy the standards under the business judgement rule, they will not be held liable. If the company fails to pursue such personal liability, a shareholder or member of such a company may file a derivative lawsuit against such a person on behalf of the company.

A KK may enter into a contract with directors (other than representative directors and directors in charge of the operation of the company), statutory auditors, accounting auditors and accounting advisers establishing a cap on their liability (such a cap must be at least in the amount provided for in the Companies Act). In addition, a KK may exempt the personal liability of directors (including representative directors and directors in charge of the operation of the company), statutory auditors, accounting auditors, accounting advisers and executive officers (exceeding an amount provided for by Companies Act) by a resolution of a shareholders' meeting or a resolution of the board of directors in case the articles of incorporation of the company contain a provision that such persons' personal liability for damage to the company may be exempted by a resolution of the board of directors. In order to exempt all the personal liability for damages to the company, the consent of all shareholders is required.

In the case of a GK, it is interpreted that the articles of incorporation may have a provision that all personal liability for damage to the company is exempted, or a provision regarding the process and requirements for the exemption from personal liability for damage to the company.

With respect to a shareholder or a member who is not in charge of the operation of the business of a company, there is no statutory law or court case that clearly mentions that it owes any duty to other shareholders or members.

Chapter 4: Takeovers (friendly M&A)

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4.1 Overview

In Japan, while we have started to see some hostile takeovers in the capital markets, most M&A transactions involving the acquisition of listed target companies are friendly transactions, where the management of target companies agrees to the acquisition proposed by the buyers.

The Financial Instruments and Exchange Act (Act No 25 of 13 April 1948, as amended, or the FIEA) and the cabinet order, the cabinet office orders and several regulations promulgated thereunder set forth the rules of and process for takeover transactions. The Financial Services Agency (FSA) is the responsible regulator for takeovers, and the Kanto Local Finance Bureau is the delegated contact point for both bidders and target companies. Stock exchanges impose their own disclosure rules on listed companies. This chapter focuses on the rules of Tokyo Stock Exchange (TSE).

4.2 Summary of regulations

4.2.1 Mandatory tender offer

The FIEA requires a buyer to commence a tender offer in any of the following cases:

1. a buyer acquires shares or other securities issued by a listed company (the 'Securities'), and as a consequence the voting rights the buyer owns exceed five per cent of the total voting rights, except in the case where the buyer acquires Securities within 61 days from ten shareholders or less;
2. a buyer acquires Securities, and as a consequence the voting rights the buyer owns exceed one-third of the total voting rights;
3. a shareholder who already holds more than 50 per cent of the voting rights of the target company acquires Securities of the target, and as a consequence, the voting rights the shareholder owns do not exceed two-thirds of the total voting rights, except in the case where the shareholder acquires Securities within 61 days from ten shareholders or less;
4. a buyer acquires Securities, and as a consequence the voting rights the buyer owns become two-thirds or more of the total voting rights;
5. (i) a buyer acquires Securities representing more than ten per cent of the voting rights in any form (including acquisition of newly issued shares) within three months, (ii) which includes acquisition of Securities representing more than five per cent of the voting rights through off-market trading or through off-auction trading, and (iii) as a consequence, the voting rights the buyer owns exceed one-third of the total voting rights; or

6. a tender offer is in process, and a shareholder who already holds more than one-third of the total voting rights acquires Securities representing more than five per cent of the voting rights during the offer period.

A tender offer is not required if all the Securities are acquired through in-market transactions (except for (1), transactions through off-auction trading, such as the electronic trading network system offered by the TSE will not be excluded).

Voting rights held by certain affiliates and other persons with whom a buyer has agreed to purchase, sell or exercise voting rights in concert with are counted together when applying the triggering thresholds under the mandatory tender offer rule.

Virtually all transactions in which a buyer contemplates acquiring more than one-third of voting rights of a listed company through off-market transactions will trigger the mandatory tender offer requirement.

Violation of the mandatory tender offer rule can result in a criminal fine of up to JPY 5m and/or imprisonment up to five years; and an administrative penalty amounting to 25 per cent of the aggregate purchase price of the acquisition can also be imposed.

4.2.2 Tender offer process

Overview

In a friendly takeover deal the buyer usually conducts due diligence on the target company, then discusses and negotiates the terms of the acquisition with the management of the target before launching a tender offer. The negotiation process is subsequently required to be described in the disclosure documents for the tender offer. If there are one or more major shareholders of the target company, it is not uncommon that the buyer and those major shareholders enter into a tender and support agreement, under which the major shareholder(s) agree to tender shares through the tender offer process. Normally, the major shareholder(s) only agree to provide very limited representations and warranties and to make very limited covenants. Once the buyer and the target company reach an agreement on the terms, they prepare the required disclosure documents, consult with the FSA through the competent Kanto Local Finance Bureau and the TSE, and make formal decisions to commence the tender offer. In a typical tender offer, the following disclosures are required for the buyer and the target company.

Disclosure by Tender Offerors

A buyer who commences a tender offer (the 'Tender Offeror') is required to: (1) make a Public Notice for Commencing Tender Offer (*kokai kaitsuke kaishi kokoku*); and (2) file a Tender Offer Notification (*kokai kaitsuke todokedesho*), both through the online disclosure system operated by the FSA (Electronic Disclosure for Investors' NETwork or EDINET). Practically, these are filed and disclosed through EDINET on the next business day when the Tender Offeror makes its decision to commence the tender offer. If the Tender Offeror is a listed company, it is also required to issue a press release on the day it decides to commence the tender offer. In addition, the Tender Offeror must deliver a (3) Tender Offer Statement (*kokai kaitsuke setsumeisho*) to each shareholder who tenders its shares, concurrently with or prior to such tender. The contents of a Public Notice for Commencing Tender Offer, a Tender Offer Notification and a Tender Offer Statement (and press release, if any) are almost identical; they set forth the material terms of the tender offer, including the purpose of the tender offer, tender offer price, tender offer period and number of shares to be purchased.

Any time there is a change to any of the material matters set out in a Tender Offer Notification (typically, a change in the tender offer price, the tender offer period or expiration of the waiting period under competition law), a Tender Offeror must file an amendment of the Tender Offer Notification.

When the tender offer is complete, the Tender Offeror must: (1) make a public notice to announce the result of the tender offer; and (2) file a Tender Offer Report (*kokai kaitsuke hokokusho*), both on the next day after the last day of the tender offer period, through EDINET, to announce the result of the tender offer, including the number of tendered shares. If the Tender Offeror is a listed company, it is also required to issue a press release. In addition, the Tender Offeror needs to file a Report of Possession of Large Volume (*tairyo hoyu hokokusho*) (a report required for holders of Securities representing more than five per cent of a listed company's outstanding shares), and if the target company becomes a subsidiary of the Tender Offeror, make some other filings, which may include a Status Report of the Parent Company (*oyakaisyatou jokyo hokokusho*) and Extraordinary Report (*rinji hokokusho*).

Disclosure by target companies

When a tender offer is commenced, the target company is required to file a Position Statement (*iken hyomei hokokusho*) through EDINET within ten business days after the Public Notice for Commencing Tender Offer is published, and issue a press release to express its opinion on the announced tender offer. In these documents the target company expresses its opinion with respect to the tender offer, and the grounds and reasons thereof. In a friendly takeover transaction the target company usually holds a board meeting on the same day a tender offer is announced, and the board adopts a resolution to determine its opinion on the announced tender offer and files the Position Statement on the same day. In a friendly takeover transaction, the target company normally assents to the tender offer and its board of directors recommends that the shareholders tender their shares. If the tender offer price is lower than the market price (typically in the case where the buyer contemplates acquiring shares held by major shareholder(s) (or a parent company) only), the board of the target company typically assents to the tender offer, but leaves the shareholders to decide whether or not to tender their shares.

Upon the successful completion of a tender offer, the target company is required to file an Extraordinary Report through EDINET announcing the change of its major shareholder(s) (or parent company), and issue press releases depending on the result of the tender offer.

Language of disclosure documents

All required filings and announcements, including the Public Notice for Commencing Tender Offer and Tender Offer Notification, need to be prepared in Japanese. The disclosure documents available on EDINET are in Japanese only. Some Tender Offerors and target companies voluntarily prepare and disclose English translations of their press releases, but such translations are not mandatory.

4.3 Some features of tender offers in Japan

4.3.1 Ceiling of purchased shares/obligation to purchase all shares

A Tender Offeror is not allowed to set an upper limit on the purchased shares if the voting rights to be held by the Tender Offeror after the successful completion of the tender offer will become two-thirds or more of the total voting rights. When a tender offer crosses this threshold, the Tender Offeror needs to solicit a tender from all shareholders and must purchase all tendered shares. In other words, the Tender Offeror may set an upper limit on the purchased shares so long as it does not cross this two-thirds threshold. For example, the Tender Offeror may set an upper limit on the purchased shares so that the total voting rights it will hold after the tender offer will become 51 per cent, and keep the target company listed on a stock exchange after the successful completion of the tender offer.

4.3.2 Tender offer at a discounted price

A Tender Offeror may propose a tender offer price lower than the current market price. This is done when the Tender Offeror contemplates acquiring shares held by major shareholder(s) (or a parent company of the target) only.

4.3.3 Cash-out transactions

In May 2015 a new process for the cash-out of minority shareholders was introduced, and this process now enables a shareholder owning 90 per cent or more of the voting rights of the target company compulsorily to acquire the shares of the target held by other shareholders upon the approval of the board of directors of the target (the 'Call Option by Special Controlling Shareholder'; *kabushikitou uriwatashi seikyu*). This allows the buyer to avoid calling a shareholders' meeting of the target and seeking court approval for a payment to minority shareholders. Since this method was introduced, most cash-out transactions have relied on this approach so that if a Tender Offeror successfully acquires 90 per cent or more of the voting rights through its tender offer, and if the aggregate voting rights after the tender offer do not reach 90 per cent, a cash-out transaction is sought by conducting a reverse stock split. The major difference between relying on a Call Option by Special Controlling Shareholder and a reverse stock split is the need to call for a shareholders' meeting of the target company in the latter case. Therefore, a reverse stock split scheme takes more time to complete the cash-out transaction.

4.3.4 Foreseeability and certainty on acquisition price

In 2016 the Supreme Court held that if the tender offer was made in accordance with a process 'generally accepted to be fair', and the Tender Offeror has offered the same acquisition price paid following the first-step tender offer in the second-step cash-out transaction, then the court should approve that same price as the fair value of the minority shares in the cash-out transaction. A court will therefore primarily review the fairness of the process, and will uphold the acquisition price proposed by the Tender Offeror, if the Tender Offeror has followed a fair process and proposes the same cash-out price as the offer price in the preceding tender offer. While the process that needs to be followed in order to satisfy the ‘process generally accepted as fair’ standard remains open, this Supreme Court decision has nevertheless provided greater foreseeability and certainty on the acquisition price to be paid by the Tender Offeror.

4.3.5 Fair M&A Guidelines

Unlike in some other jurisdictions, such as the US, under Japanese law there is no common understanding of how the ‘duty of loyalty’ concept should be interpreted, nor is it clear how conflict-of-interest transactions should be disciplined in general. On 28 June 2019 the Ministry of Economy, Trade and Industry issued the Fair M&A Guidelines, updating the MBO Guidelines issued in 2007. The Fair M&A Guidelines primarily focus on management buyouts (MBOs) and the acquisition of a controlled company by a controlling shareholder, where issues with respect to structural conflicts of interest and information asymmetries typically exist, aiming to provide a guideline to a fair process in those circumstances.

Among other things, the Fair M&A Guidelines suggest the adoption of some or all of following methods to avoid conflict of interest issues between the buyer (management of the target company) and other general shareholders of the target company (in the case of MBO transactions) or between a controlling shareholder and other general shareholders (in the case of the acquisition of a controlled company by a controlling shareholder): (1) establishment of an independent special committee at the target company; (2) obtaining advice from independent expert advisers (eg, obtaining legal advice from an independent legal adviser and obtaining a share valuation report from an independent share valuation institution); (3) ensuring opportunities for other acquirers to make proposals (market check); (4) enhancing the provision of information to general shareholders so as to improve the process transparency; (5) eliminating coerciveness (eg, avoiding adopting a scheme in which dissenting shareholders will not have an appraisal right, or conducting the cash-out transaction without delay); and (6) establishing a ‘majority-of-minority condition’ for the proposed transaction.

The common practice is to adopt the concepts described in (1)–(5) in a tender offer process. A ‘minority of majority condition’, however, is still uncommon in Japan, and the Fair M&A Guidelines admit that this condition may not always work to avoid conflict of interest issues. As noted, the Fair M&A Guidelines are an update of the MBO Guidelines, and those previously issued guidelines have been respected by the Japanese courts. The measures proposed in the Fair M&A Guidelines are expected also to be respected by the courts, and are considered to provide guidelines of what would be considered a ‘generally accepted to be fair’ process in a tender offer process.

Chapter 5: Foreign investment

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5.1 Foreign investment control/restriction

5.1.1 Foreign Exchange and Foreign Trade Act

The restrictions on investment by foreign investors are governed by the Foreign Exchange and Foreign Trade Act (FEFTA). If a foreign investor intends to make an inward direct investment, such as: the acquisition of a company's shares or equity interests from a resident; consent to a substantial change to the business purpose of the investee company; the acquisition of long-term loans or bonds in excess of JPY 100m; or acceptance of proxy exercise of voting rights, the person must submit a prior notification or report after the fact.

Due to the revision of the FEFTA in January 1992, most inward direct investment became a matter that should be reported after the fact based on the principle of freedom of investment. The *ex post facto* report must be submitted to the MoF and the minister having jurisdiction over the business via the Bank of Japan in a prescribed form by the fifteenth day of the month following the month that includes the date of the transaction or act.

Prior notification is required if the foreign investor's nationality or country of residence is: (1) a country not listed in the published list of countries; (2) the business objective of the investment destination is a business with prior notification (weapons, aircraft, nuclear power, space related, manufacturing of general-purpose products that can be used for military purposes, cybersecurity-related, electricity and gas, heat supply, telecommunications business, broadcasting business, water supply, railways, passenger transportation, manufacturing of biological products, maintenance business, agriculture, forestry and fisheries, petroleum, leather-related, air transportation, shipping etc); or (3) certain actions performed by persons concerned with Iran.

Actions requiring prior notification may not be performed until 30 days (it is usually shortened to two weeks, and for certain cases, such as a capital increase of a wholly owned subsidiary, efforts are made to shorten it to four business days) have elapsed after the prior notification. Prior notification must be made to the MoF and the minister having jurisdiction over the business via the Bank of Japan in a prescribed form from six months prior to the intended act. If, as a result of the examination, the MoF and the minister having jurisdiction over the business find that there is an issue, they may recommend the foreign investors change the content of the transaction or discontinue it. In addition, if prior notification has been provided, an execution report must be submitted to the MoF and the minister having jurisdiction over the business via the Bank of Japan in a prescribed form within 30 days.

5.1.2 Overview of red flag issues that foreign investors should note

As of March 2020 foreign investors are required to submit prior notification when acquiring shares of unlisted companies in businesses covered by prior notification. However, for listed companies they are required to submit prior notification only if the acquisition is more than ten per cent of the listed companies' shares. In October 2019, however, a bill to reduce this ratio to one per cent was approved by the Cabinet and came into effect in the spring of 2020. The explanation given is that portfolio investments and other investments that do not pose a risk to national security, and so on are exempted from prior notification, and a system of exempting prior notification has been introduced by Cabinet Order and public notice, but there is a possibility that it will have a significant practical impact. Furthermore, in the revised bill, the consent of a foreign investor or a person closely related thereto to appoint the position of an officer or consent to the transfer or abolition of a significant business is regarded as inward direct investment and so on, which may have a significant practical impact.

5.1.3 Specific limitations on investment in real estate

Under the Act on Foreign Nationals' Rights in Relation to Land, there are provisions to prohibit or impose conditions or restrictions on the acquisition of land rights by foreigners or foreign corporations in areas necessary for national defence, but no applicable Cabinet Order has been enacted. Accordingly, in Japan there are no limitations on the acquisition of real estate by foreign investors, and even foreigners can acquire full ownership of real estate, and buy and sell it freely.

However, under the FEFTA, when a non-resident acquires real estate in Japan, the person is required to report to the MoF via the Bank of Japan within 20 days after the acquisition (however, reporting is not required in certain cases, such as for residential use or for non-profit business purposes).

In addition, if the payment for real estate (in cases exceeding JPY 30m) is made between a resident and a non-resident, the resident is required to submit a report on the receipt of the payment to the MoF through a bank and so on within ten days from the transaction.

5.2 Foreign exchange control

In Japan foreign exchange control has been abolished, except for transactions with countries subject to economic sanctions, due to the revision of the FEFTA in April 1998. Foreign exchange operations have been liberalised through the liberalisation of domestic and overseas capital transactions and the abolition of the authorised foreign exchange banking system. Therefore, there are no particular issues with foreign exchange control.

However, when a foreign investor conducts a capital increase and it falls under the category of inward direct investment, it may be necessary to submit a prior notification or an *ex post facto* report.

In addition, if a transaction payment equal to JPY 30m or more is made between a resident and a non-resident, a report must be submitted to the MoF through a bank and so on within ten days of the transaction.

5.3 Applicable tax incentive or grants

5.3.1 Overview of tax incentives

Japan's corporate tax rate is one of the highest in the world, and while it has always been pointed out in Japan and abroad that tax incentives are necessary as an incentive to invest in Japan, there are no specific tax incentives for foreign investors that apply to Japan as a whole, and in addition to certain tax incentives under special laws, the use of special economic zones has been introduced, and local governments have established their own tax incentives. Details can be obtained from the websites of INVEST JAPAN FDI Promotion and Japan External Trade Organisation (navigation system for investing in Japan's local regions).

5.3.2 Tax system to strengthen local regions

If the head office functions of a Japanese branch or research institute are 'opened and expanded' in a local city other than the Tokyo metropolitan area by direct investment in Japan, or if a foreign company with head office functions in Tokyo's 23 wards 'relocates' the head office functions from Tokyo's 23 wards to a local city other than the Tokyo metropolitan area, it may receive preferential tax treatment under the tax system to strengthen local regions (certain requirements must be met).

5.3.3 Special economic zones

There are three special zones: National Strategic Special Zones, Comprehensive Special Zones and Special Zones for Reconstruction.

Ten districts have been recognised as National Strategic Special Zones, and more than 300 projects have been recognised. Special tax measures have been implemented in the National Strategic Special Zones, including tax breaks for promoting capital investment and income tax deductions.

Corporate taxes have been reduced in the special zones to enhance international competitiveness.

In the Special Zones for Reconstruction, special tax measures, such as special depreciation of capital investment, are available when business operators engage in projects that contribute to securing employment opportunities, make capital investment or employ disaster victims in industrial cluster zones for reconstruction.

5.3.4 Measures taken by local governments

Some local governments have introduced measures to reduce or exempt corporate citizenship tax for foreign investors when they start up businesses in Japan. However, only a few local governments have established such tax incentives, and many only provide rent subsidies or partial subsidies for the establishment of bases. In addition, the applicable conditions and the amount of subsidies for each industry are different.

Chapter 6: Restructuring and insolvency

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6.1 General overview

In Japan, when a debtor company faces financial difficulty and aims to revitalise itself, it would usually first consider an out-of-court debt-restructuring arrangement with its creditor banks ('out-of-court workout' or *shiteki seiri*). In an out-of-court workout, the target creditors are usually limited to lender banks, and other claims (such as trade claims) will be paid in full outside the process. On top of that, the debtor's workout is kept confidential between the debtor and the banks, and hence the value of the business will not be impaired by the workout. This is why the out-of-court workout is usually the first method of choice for debt restructuring.

However, if such an arrangement is found to be difficult because, for example, one or more banks opposes the plan, or the speed of deterioration of the business or cash liquidity is so fast that the debtor does not have enough time to go through the workout process, the company will likely need to consider filing with the court a petition for civil rehabilitation proceedings (*minji saisei*) or corporate reorganisation proceedings (*kaisha kosei*).

If the company intends to liquidate, a petition for bankruptcy proceedings (*hasan*) or special liquidation proceedings (*tokubetsu seisan*) is available. Bankruptcy proceedings also commence in civil cases where rehabilitation proceedings or corporate reorganisation proceedings fail.

6.2 Out-of-court workout

An out-of-court workout usually initiates with a debtor's notice, which requests the banks to stand still; that is, refraining from collecting claims, setting off or exercising security interests. The debtor then proposes a restructuring plan to the banks, which lays out the terms and conditions of rescheduling or discharging its debts. If the banks find the debtor's restructuring plan fair, economically reasonable and feasible, the banks usually consent to the plan. This consent must be unanimous. Therefore, if one of the banks opposes the plan, even though all the other banks agree, the debt-rescheduling plan or debt-discharge plan will not become effective and the company is likely to need to file for civil rehabilitation or corporate reorganisation proceedings.

In Japan there are several laws and statutes that facilitate systematised out-of-court workout proceedings, such as the Turnaround ADR scheme and the SME Rehabilitation Support Association scheme. In particular, the Turnaround ADR is the most important and is sometimes utilised by listed companies.

6.3 Court insolvency proceedings

As discussed above, in Japan there are four types of in-court insolvency proceedings. Civil rehabilitation and corporate reorganisation are proceedings for the revitalisation of the debtor's business, while bankruptcy and special liquidation are proceedings for the liquidation and winding-up of the debtor company.

The debtor company can file for corporate reorganisation or civil rehabilitation when there is a possibility of the debtor falling into a situation of: (1) excessive debts (ie, insolvency on a balance-sheet basis); (2) general and continuous inability to pay its debts when they become due (ie, insolvency on a cash-flow basis); or (3) significant hindrance to the continued operation of business if it pays its debts when they become due.

The debtor company can file bankruptcy proceedings when it is in a situation of: (1) excessive debts; or (2) general and continuous inability to pay its debts when they become due.

6.3.1 Corporate reorganisation proceedings

Corporate reorganisation proceedings are only available to KKs, and are typically used for large and complex insolvency cases, such as the Japan Airline case.

Under corporate reorganisation proceedings:

- a trustee is always appointed by the court and the right to operate the company's business and dispose of the company's assets solely belongs to that trustee; and
- security interest will no longer be exercisable during the proceeding.

The trustee will formulate a reorganisation plan and propose it to secured creditors and ordinary unsecured creditors. The plan comes into effect if it is approved: (1) by unsecured creditors holding a simple majority of the aggregate unsecured claim amount; and (2) by secured creditors holding either two-thirds or more (if the plan only reschedules the secured claims) or three-fourths or more (if the plan discharges the secured claims) of the aggregate secured claim amount and is then subsequently confirmed by the court. The secured and unsecured creditors will be paid in accordance with the plan. The value of the secured claim will be determined by an amicable settlement between the trustee and the secured creditor if one can be reached, or by a claim assessment procedure in court.

6.3.2 Civil rehabilitation proceedings

Civil rehabilitation proceedings are available to companies of any size and type, as well as individuals.

Under civil rehabilitation proceedings, as a general rule:

- a trustee is not appointed, and the debtor keeps the right to operate the company's business and dispose of the company's assets as the debtor-in-possession under supervision by a court-appointed supervisor and the court itself (certain important matters, such as the transfer of assets, must be conducted only with the consent of the supervisor, or permission of the court); and
- security interests are exercisable during the proceeding unless an order temporarily to suspend exercise is issued by the court.

The debtor-in-possession will formulate the rehabilitation plan and propose it to ordinary unsecured creditors. The plan comes into effect if approved: (1) by a simple majority of the headcount of the ordinary unsecured creditors (by headcount); and (2) by ordinary unsecured creditors holding half or more of the aggregate claimed amount of ordinary debt and is then subsequently confirmed by the court; the confirmation order becomes final and non-appealable. The ordinary unsecured creditors will be paid in accordance with the plan. Secured creditors will be paid in accordance with an amicable settlement with the debtor if one can be reached, or by exercising their security interest.

6.3.3 Bankruptcy proceedings

Bankruptcy proceedings are available to companies of any size and type, as well as individuals.

Under bankruptcy proceedings:

- a trustee is always appointed by the court and the right to dispose of the company's assets belongs solely to the trustee; and
- security interests are exercisable during the proceeding.

Chapter 7: Employment, industrial relations, and work health and safety

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7.1 Employees' rights and protection

The principal sources of employment law and regulations in Japan are: (1) the Labour Standards Act (Act No 49, 1947) (LSA), which lays down the basic principles that govern employment relationships and the minimum standards of employment conditions; and (2) the Labour Contract Act (Act No 129, 2007) (LCA), which also regulates individual employment relationships. As a general rule, Japanese employment laws apply to all employees in Japan, regardless of their nationality, and are very protective of employees.

7.1.1 Working hours regulations

The maximum statutory working hours is 40 hours per week and eight hours per day, and at least one day per week must be provided as a statutory non-working day or rest day, subject to exceptions under the LCA, namely the flextime system, irregular working hours system, discretionary working hour system and advanced professionals system.

Under the flextime system, employees have flexible starting and finishing times of work, and working hours per day, but their designated working hours per month should be fixed (eg, 177 hours). The employer may also designate a core time range when all employees are required to work.

For work with peak and off-peak periods, employers often introduce the irregular working hours system. Under this system, as long as the average working hours do not exceed 40 hours per week over a certain period (one week/one month/one year), no overtime pay is required to be paid to employees who work more than the statutory maximum working hours.

As to the discretionary working hours system, it can be either the expert type, or the planning or proposal type under the LCA. The requirements to apply this system are strict, and for the introduction of the planning or proposal type system the employer must establish a labour-management committee to adopt this system by a vote of at least four-fifths of its members. Thus, this system may only be used for a limited number of employees. On 1 April 2019 the advanced professionals system was introduced as a new exception to the discretionary working hours system. However, only a limited number of companies have adopted this system because it only applies to employees with specific job descriptions and advanced vocational skills with a certain annual income (eg, no less than JPY 10,750,000), and the labour-management committee must adopt it by a vote of at least two-thirds of its members.

7.1.2 Overtime agreement

To ask employees to work more than the maximum working hours or on rest days, the employer must: (1) enter into a labour-management agreement that permits such overtime work (the 'Overtime Agreement') with a representative majority of employees; and (2) submit such agreement to the labour standards inspection office. In principle, under this agreement, overtime limits should be 45 hours per month and 360 hours per year, except as otherwise specified therein. A breach of these limits shall be subject to criminal penalties, except for cases where an Overtime Agreement has been established for temporary and special situations.

In any event, overtime working hours should not exceed 720 hours per year, even in such exceptional cases, and within such a 720-hour limit, the following limits also apply: (1) the overtime working hours should not exceed 80 hours per two or six months on average (including rest days); (2) the overtime working hours should be less than 100 hours per month (including rest days); and (3) the overtime working hours should not exceed 45 hours per month more than six times (the principal limitation).

7.1.3 Overtime work compensation

Employers must pay extra compensation for work performed in excess of the maximum working hours and work performed on rest days (collectively, 'Overtime Work Compensation'). In addition, employers must pay extra compensation for work performed between 2200 and 0500 ('Late Night Work Compensation'). The minimum rates of Overtime Work Compensation and Late Night Work Compensation under the LSA are summarised below.

Type of work	Applicable work	Minimum hourly rate
Overtime work	Over eight hours per day or 40 hours per week	125% of the normal base hourly wage
Rest day work	On a rest day	135% of the normal base hourly wage
Late night work	Between 2200 and 0500	125% of the normal base hourly wage

The hourly rates are to be combined if any two of the above types of work overlap. For example, an hour of Overtime Work and Late Night Work should be compensated at 150 per cent of the normal base hourly wage.

The current statute of limitations for wages including Overtime Work Compensation under the LSA is two years. However, a bill to initially extend such a period to three years, and then later to five years, was submitted to the ordinary Diet in 2020 and took effect on 1 April 2020.

7.1.4 Annual paid leave

An employee who has continuously worked for six months and has worked for at least 80 per cent of the total number of working days is entitled to receive annual paid leave. The minimum number of days to be granted as annual paid leave in accordance with Article 39 of the LSA is in proportion to the length of service, as shown in the table below:

Years of service	6 months	1 year, 6 months	2 years, 6 months	3 years, 6 months	4 years, 6 months	5 years, 6 months	6 years, 6 months
Days of annual paid leave	10	11	12	14	16	18	20

Unused paid leave may be carried over until the next year only since the current statute of limitations for rights is two years. An employer is not required to provide paid sick leave in addition to the above annual paid leave.

7.1.5 Termination of the employment contract

The LSA, LCA and case law require employers to have objectively 'reasonable grounds' for dismissing employees. In the absence thereof, a dismissal would not be considered appropriate in general societal terms, and it will be treated as an abuse of the employer's right and declared invalid.

All possible grounds for such a dismissal must be clearly provided in the rules of employment or an employment agreement for the dismissal of an employee to be valid. Unlike an ordinary dismissal, a disciplinary dismissal involves a disciplinary action of the employer and is considered to be the most severe method of dismissal. It can be justified only when, for example, an employee has committed a crime or a very serious ethical breach, or was unreasonably absent from work.

Under the LSA, in dismissing an employee, an employer must provide at least 30 days' advance notice or pay the average wage for a period of not less than 30 days in lieu of notice (except for disciplinary dismissal cases with the prior approval of the relevant authority). The employer may reduce the 30-day notice period by paying the average wage for each day reduced.

Since courts tend to review the 'reasonable grounds' very narrowly, and the employer has the burden of proof, it is hard to dismiss employees validly in Japan. The law also does not allow an employer to terminate the employment unilaterally by paying some severance allowance. Thus, most employers attempt to execute a separation agreement with the employee, often including the payment of a severance allowance, to terminate the employment in a fast and amicable manner. There is no statutorily mandated severance pay, and the amount thereof is influenced by the expectation of the employee. However, it is generally calculated to reflect the years of service, amount of remuneration and so on. The amount is also affected by the size and particular industry of the employer.

The discussions above apply to redundancy. Courts uphold a redundancy as a dismissal due to reorganisation (*seiri kaiko*) only where the employer can demonstrate the following requirements: (1) the redundancy is necessary to accomplish a reasonable management action; (2) the employer has made all possible efforts to avoid dismissal of the employees; (3) the terminated employees were chosen based on an appropriate selection criteria; and (4) the employer has provided a sufficient explanation and offered the employees an opportunity to discuss the matter – something akin to due process. Redundancy measures that are taken based only on a slowdown in business activity or a temporary economic downturn to increase profits (as opposed to saving the company) would be considered an abuse of the right of the employer.

7.2 Statutory contributions and minimum wage

An employer must participate in four kinds of insurance system: workers' accident compensation insurance, employment insurance, health insurance and nursing care insurance, and employee's pension insurance. All employees who meet certain criteria shall be covered by such insurance systems. In general, the employer pays the insurance premiums by deducting the portion payable by employees from their wages, and paying them to the relevant authorities together with the portion payable by the employer.

No employer can hire an employee for less than the legal minimum wage under the Minimum Wage Act. The minimum hourly wage is determined based on the region and industry. If two different minimum wage amounts apply to an employee, the employee is entitled to the higher amount. Tokyo has the highest minimum wage of JPY 1,013 as of 1 October 2019.

7.3 Work permits

A foreigner who wishes to work in Japan must obtain the appropriate visa and work permit (collectively, the 'work visa') under the Immigration Control and Refugee Recognition Act (ICA). Until recently, work visas only covered work that required a high level of professional knowledge or skill. Therefore, in principle, it was not possible for foreigners to engage in manual labour under work visas, unless they were granted work visas based on their family status, had trainee visas or were part-time workers on student or dependent visas. The latest major amendment to the Immigration Control and Refugee Recognition Act in April 2019 created a new status of residence called a 'Specified Skilled Worker'. To cope with current labour shortages, this amendment now allows the entry of relatively unskilled labour from foreign countries to work for Japanese companies, though still limited to certain industries (eg, healthcare, construction, agriculture, food services and shipbuilding).

Chapter 8: Tax law

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8.1 Taxes applicable to individuals

Income tax, local inhabitant tax and special reconstruction income tax are listed as taxes applicable to employees.

Under the Income Tax Act, salary earned by employees is classified as salary income. The amount of salary income is calculated by deducting the amount of salary income deduction from the amount of salary revenue. The amount of salary income deduction increases in accordance with the amount of salary revenue, but is capped at JPY 1.95m. The amount of gross income is calculated by offsetting losses arising from certain categories of income against the amount of salary income and other certain income, and the amount of taxable income is calculated by deducting income deductions, such as the basic deduction from the amount of gross income. The amount of income tax is calculated by multiplying the amount of taxable income by the applicable tax rate. The Income Tax Act adopts progressive rates, with the maximum tax rate being 45 per cent.

The amount of income tax for a calendar year is fixed by filing a tax return and must be paid by 15 March of the following calendar year, in principle. However, as to salary, withholding income tax is withheld from salaries when it is paid by the employer and the difference between the income tax to be paid and the amount of WHT is settled by way of a year-end adjustment made by the employer who pays the salary. Accordingly, employees who receive only salary income generally do not need to file a tax return.

In addition to income tax, a special reconstruction income tax is imposed at the rate of 2.1 per cent of the basis amount of income tax from 2013 through 2037.

Furthermore, salary income received by employees residing in Japan is subject to local inhabitant tax. It is usual for local inhabitant tax to be withheld from salary payments.

Under the Income Tax Act, salary paid to non-residents is subject to WHT in Japan at the rate of 20.42 per cent only if and to the extent that such a salary is paid for services performed in Japan. Non-residents without a permanent establishment in Japan generally are not required to file an income tax return for such salary. Such WHT may be exempt under a tax treaty.

8.2 Taxes applicable to businesses

8.2.1 Corporation tax

Taxation on domestic corporations

Domestic corporations are required to pay corporation tax on their income for each business year. The applicable tax rate depends on the type and size of corporation; however, it is 23.2 per cent, in principle. Such income is calculated by deducting the amount of deductible expenses from the amount of gross profits. The amount of deductible expenses and the gross profits are to be calculated in accordance with generally accepted accounting principles (GAAP) unless otherwise stipulated under exceptional provisions of Japanese law.

Most of such exceptional provisions are stipulated so as to deny the deduction of expenses recorded under GAAP for the purpose of corporation tax. For example, certain expenses, such as remuneration for officers, appraisal losses on assets, depreciation expenses or allowances recorded under GAAP are deducted for corporation tax purposes only to the extent of a limited amount or if they satisfy certain requirements specified under such provisions. On the contrary, there are some exceptional provisions that stipulate that certain types of revenue under GAAP are not included in gross profits for corporation tax purposes. For example, dividends received from an entity's subsidiaries, etc, are included in revenue under GAAP; however, all or part of such dividends may not need to be included in gross profits depending on the shareholding ratio and so on for corporation tax purposes.

Capital transactions, which are transactions that cause an increase or decrease in the amount of stated capital and so on of a corporation, and the distribution of profits or surplus conducted by a corporation do not cause taxation on such a corporation. In the case where a corporation that files a final return form shows any net operating loss that arose in a business year starting within ten years prior to the first day of each of its business years, the amount equivalent to such a loss may be included in deductible expenses to the extent of 50 per cent of the income before such an inclusion (100 per cent for SMEs), when calculating the amount of income for each relevant business year.

Corporations should file a tax return and pay their corporation tax within two months from the date following the final day of each business year, in principle; however, such a deadline may be extended in certain cases.

The amount of income and corporation tax is to be calculated by each respective corporation, in principle. As an exception, subject to the approval of its consolidated tax return, the consolidated income of corporations is calculated by aggregating the income of a corporation and that of each of its perfectly controlled subsidiaries, and the amount of corporation tax is calculated based on such consolidated income. Even when such a consolidated tax return is not adopted, a group taxation system applies and certain transactions conducted between group companies may benefit from the deferral of capital gains and losses. Note that there will be an overhaul of the consolidated tax return system that will come into effect on 1 April 2022.

There is no general anti-avoidance rule (GAAR) under Japanese tax law; however, there are comprehensive rules to deny tax avoidance that are applied to closely held corporations, corporation reorganisations and consolidated tax returns.

Foreign corporations

Under the Corporation Tax Act, foreign corporations are obliged to pay Japanese corporation tax only on income sourced in Japan. The scope of income sourced in Japan subject to corporation tax depends on whether the foreign corporation has a permanent establishment and the type of permanent establishment. Certain categories of income sourced in Japan are subject to withholding income tax.

8.2.2 Systems to prevent international tax avoidance

There are various systems for preventing international tax avoidance under the Corporation Tax Act and the Act on Special Measures Concerning Taxation. For example, Japan has controlled foreign corporation rules by which the income of certain overseas corporations is included in the income of their large Japanese corporation shareholders. Japan also has thin capitalisation rules and earnings stripping rules, which prohibit the deduction of certain interest. Under Japanese law, the transfer pricing rule applies to transactions conducted with overseas affiliates of Japanese corporations.

8.2.3 Other taxes applicable to businesses

Some other taxes are imposed based on the income of a corporation, such as local corporation tax and corporation special business tax (which are national taxes) and corporation business tax and corporation inhabitant tax (which are local taxes).

If the transactions are conducted in Japan for consideration as a business, consumption tax and local consumption tax will be imposed on transactions at the rate of ten per cent in total in principle.

8.3 Other taxes

It is necessary to pay attention to stamp tax, registration tax, real estate acquisition tax, office tax and excise tax when conducting business in Japan.

Chapter 9: Intellectual property

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9.1 Patents

9.1.1 Patentable subject matter

Under Japanese law, patentable subject matter encompasses ‘inventions’, which is defined under Article 2, paragraph 1 of the Patent Act as ‘significant creations of technical ideas utilizing the laws of nature’. Inventions can be classified into three categories: ‘inventions of products’, ‘inventions of processes’ and ‘inventions of processes for producing products’. A patent may be granted for business methods that are combined with computer systems or other devices. Methods of medical treatment and diagnosis for human illnesses are not patentable. The mere discovery of microorganisms that occur naturally, or components thereof, such as a DNA sequence or a protein, is not a patentable invention. However, if the microorganism or its component is artificially isolated from its natural source or has mutated, and is demonstrated to meet the utility requirement, such a discovery can be a patentable invention.

9.1.2 *Requirements for inventions to be eligible for patents*

To be eligible for a patent, an invention must meet the novelty requirement and the 'inventive step' requirement (the latter is equivalent to the 'obviousness' requirement in certain other jurisdictions).

To meet the novelty requirement, an invention cannot be identical to another invention that has been publicly known, publicly implemented, or described in a publication in Japan or in a foreign country prior to the filing or relevant priory date of the patent application. Further, the invention must not be identical to: (1) an invention of others and described in any part (claims, specifications or drawings) of a patent application that was filed by another person in Japan earlier and was subsequently published ('laid open'); and (2) an invention that was described in the claims of an issued patent previously filed by the same applicant in Japan.

To meet the inventive step requirement, an invention cannot be something that could have been made easily by a person ordinarily skilled in the art based on other inventions that were publicly known, publicly implemented, or described in a publication in Japan or in a foreign country prior to the filing of the patent application.

9.1.3 *Ownership of patents*

The inventor has the right to obtain a patent for the invention and such a right can be transferred. For an invention created by an employee during the course of employment, the right to obtain a patent may be assigned to the employer or even automatically vested in the employer in accordance with employment rules set by the employer, and the employer may file the patent application as the applicant. In the case of multiple inventors, the right to file a patent application is held jointly by all of them, and the patent application needs to be filed by all of them together. The transfer of ownership of an issued patent becomes effective when such a transfer is recorded with the Japan Patent Office (JPO).

9.1.4 *Duration of patent rights*

A patent expires 20 years after the filing date of the patent application. For pharmaceutical and agrochemical patents, a patent term extension is available for up to five years upon request by the patentee if the patentee or a licensee thereof receives marketing approval for the patented drug or pesticide from the relevant Japanese authority.

9.1.5 *Remedies for patent infringement*

If a patent is infringed, the patentee may seek an injunction against the infringer. A permanent injunction is available almost automatically if the court finds the patent valid and infringed. A request to destroy the infringing products can be made together with a claim for an injunction. A preliminary injunction is also available through summary proceedings and may be granted if the court finds a *prima facie* case of infringement, and that the patentee is likely to suffer irreparable harm without the preliminary injunctive relief.

In addition, under the Patent Act of Japan, a patentee may seek compensation for damages caused by infringement, based on the following three theories:

1. the patentee's lost profits;
2. the profits of the accused infringer; and/or
3. reasonable royalties.

Punitive damages are not allowed in Japan for patent infringement, even in cases of wilful infringement.

9.2 Trademarks

9.2.1 *Scope of trademarks*

Under the Trademark Act of Japan a 'trademark' is defined as 'any character(s), figure(s), sign(s), three-dimensional shape(s) or any colour(s), or any combination thereof, sounds or other marks provided by a Cabinet Order' and needs to be recognisable by human perception. In particular, 'motion marks', 'holograms', 'colours without profiles', 'position marks' and 'sound marks' can be protected in addition to traditional text and graphic trademarks.

9.2.2 *Ownership of trademarks*

Any Japanese individual or legal entity, any foreign individual domiciled or residing in Japan and any foreign legal entity having a place of business in Japan may apply for trademark registration in Japan, provided that such an individual or entity uses or intends to use a trademark on its goods or in its services in connection with its business. This also applies to individuals or legal entities from a country that allows Japanese nationals to register their trademarks in that country, provided that such foreign individuals or entities have a representative in respect of the said trademark in Japan.

9.2.3 *Duration of trademark rights*

The term of protection for a registered trademark is ten years from the date of the registration, and is renewable. An owner of a trademark shall submit a request for renewal to the JPO within six months prior to the expiry date of the trademark. After the expiry of the trademark, the owner may still file a request for renewal within six months from the date of expiry. No proof of use is required for renewal. However, if a registered trademark has not been used in Japan by the owner or its licensee for three consecutive years, any person may file a request for a trial for rescission of such a trademark registration. As a defence against such requests, the trademark owner needs to submit proof of use, such as copies of catalogues, advertisements, publications, websites, and trade documents bearing the trademarks and showing the dates of such materials.

9.2.4 *Remedies for trademark infringement*

Permanent injunctions and monetary relief are available through a primary civil action on the merits. In addition, a preliminary injunction is available through summary proceedings. As to monetary relief, the amount of damages is limited to actual damages, and punitive damages are not allowed in Japan, even in cases of wilful infringement.

The amount of damages is usually determined by:

1. the trademark owner's lost profits;
2. the profits of the accused infringer; and/or
3. reasonable royalties.

To obtain a permanent injunction in a lawsuit on the merits, the trademark owner does not have to establish any fact other than an ongoing infringement or a threat of infringement. For preliminary injunction, the trademark owner must additionally establish that it is likely to suffer irreparable harm without a preliminary injunction.

9.3 Copyright

9.3.1 Copyrightable subject matter

Under the Copyright Act of Japan, copyrightable subject matter encompasses 'works of authorship', which is defined as 'productions in which ideas or emotions are expressed in a creative way in the literary, scientific, artistic, or musical domains'. Letters, diaries and other kinds of confidential writings can also be protected by copyright. In court precedents, typeface designs (fonts) are held outside the scope of works of authorship under the definition above and are therefore not copyrightable.

9.3.2 Ownership of copyrights

In principle, the author of a work of authorship holds the copyright. The term 'author' is defined in the Copyright Act as 'a person who creates a work of authorship'. If a work is created by employees of a legal entity during the course of employment and at the employer's initiative and is to be published under the name of the employer, the legal entity is regarded as the author of the work, unless the employment contract or employment rules in force at the time of creation provide otherwise. As for the author of a motion picture, the Copyright Act provides that 'the authorship of a cinematographic work shall be attributed to those who, by taking charge of producing, directing, filming, and art direction, have contributed to the creation of that work as a whole, excluding authors of novels, scenarios, music, or other works adapted or reproduced in that work'. If a work is jointly created by several persons and consists of inseparable contributions, the work is regarded as a joint work, and the copyright in the work is jointly owned and must be exercised jointly by all the authors.

9.3.3 Author's moral rights

The author of a work of authorship also has the following moral rights: the right to make a work public; the right to claim authorship; and the right to maintain the integrity of his/her work.

A moral right is exclusively personal to the author and is not alienable. Although, in general, a moral right ceases to exist when the author dies, the publisher of a work is prohibited from infringing the author's moral rights not only during the author's lifetime, but also after the author's death.

9.3.4 Duration of copyright

Copyright protection begins at the time the work is created and continues for 70 years following the death of the author (for a jointly created work, for 70 years after the death of the last surviving co-author). The duration of copyright for a work whose author is a legal entity or other corporate body is 70 years from the time the work was first made public, or, if the work was not made public within 70 years following its creation, 70 years from its creation.

The duration of a copyright for a cinematographic work (regardless of whether its author is a corporation or an individual) is either 70 years from the time the work was first made public, or, if the work was not made public within 70 years from its creation, 70 years from its creation.

9.3.5 Remedies for copyright infringement

When an author's moral rights or copyrights are infringed or are likely to be infringed, the author may seek an injunction against such an infringement. The plaintiff in an infringement action may demand the destruction of the infringing objects and any equipment or instruments used solely for committing the infringement, and may demand any other measures necessary for the discontinuance or prevention of the infringement.

For monetary damages, the Copyright Act provides three presumptive theories of damages:

1. the copyright owner's lost profits;
2. the profits of the accused infringer; and/or
3. reasonable royalties.

9.4 Designs

9.4.1 Subject matter of design rights

Under the Design Act of Japan, a protectable 'design' is defined as 'a shape, pattern, or color or any combination thereof in an article (including part of an article) which produces an aesthetic impression on the sense of sight'. It should be noted that designs registrable under the Design Law can be protected concurrently by copyright if they also constitute 'works of authorship' under the Copyright Act.

9.4.2 Ownership of design rights

Under the Design Act of Japan, any person who has created a design may file an application for design registration. The right to obtain design registration is assignable. The rules governing employees' inventions under the Patent Act are also applicable to designs created during the course of employment.

9.4.3 Duration of design rights

For a design right for which the application was filed on or before 31 March 2020, the duration is 20 years from the date of registration. For a design right for which the application is filed on or after 1 April 2020, the duration is 25 years from the date of application.

9.4.4 Remedies for design right infringement

The Design Act of Japan provides three types of civil remedies for design right infringement: injunction, damages and measures to restore the plaintiff's business reputation.

Similar to other types of intellectual property, the Design Act provides three presumptive theories of damages:

1. the design right owner's lost profits;
2. the profits of the accused infringer; and/or
3. reasonable royalties.

9.5 Other

9.5.1 Utility model rights

Utility model rights protect 'devices', and are defined under Article 2(1) of the Utility Model Act as 'the creation of technical ideas utilizing natural laws'. Compared with utility patents under the Patent Act as explained above, which requires a 'significant' creation of technical ideas, utility model registration does not have to meet such a high standard.

Since a utility model right is established by registration without an examination of substantive requirements, the right holder is required to obtain from the JPO a technical appraisal report of the utility model and deliver the report to an alleged infringer together with a warning before the right holder can institute an infringement action, pursuant to Article 29-2 of the Utility Model Act. The right holder may seek compensation for damages and injunction against infringement of a registered utility model right.

The duration of a utility model right is ten years from the date of application.

9.5.2 Integrated circuit layout design utilisation rights

The Act on the Circuit Layout of Semiconductor Integrated Circuits establishes layout design utilisation rights to protect the layout design of semiconductor integrated circuits. Under the act, a person who has created a layout design, or his/her heir or successor is eligible for the registration of a layout design utilisation right. If there are two or more creators, they shall jointly apply for a registration of the right. The right holder of a layout design utilisation right may seek compensation for damages and injunctive relief against infringers.

The duration of a layout design utilisation right is ten years from the date of registration.

9.5.3 *Breeder's rights*

The Plant Variety Protection and Seed Act establishes breeder's rights. The subject matter of breeder's rights encompasses plant 'varieties', which means a group of plants that can: (1) be distinguished from other groups of plants by the expressions of at least one of the important characteristics of the plant; and (2) be propagated while maintaining all its expressions of the characteristics. The breeder's right becomes effective upon registration of the variety. Under the act, any person who has created a plant variety meeting the following requirements may obtain a registration for the variety: (1) the variety is clearly distinguishable, by expression of at least one of the important characteristics, from any other variety the existence of which is a matter of common knowledge in Japan or in any foreign state at the time of the filing of the application for registration; (2) all the plants under the variety at the same propagation stage are sufficiently similar in all their expressions of the characteristics; and (3) all the expressions of the characteristics of the variety remain unchanged after repeated propagation.

The holder of a breeder's right has an exclusive right to exploit, in the course of business, the registered variety and any other varieties that are not clearly distinguishable from the registered variety by the expressions of the characteristics.

The duration of a breeder's right is 25 years from the date of variety registration.

9.5.4 *Act for Prevention of Unfair Competition*

The Act for Prevention of Unfair Competition provides protection for: (1) unregistered trademarks; (2) configuration of goods; (3) trade secrets; (4) certain types of data; and (5) domain names. Although the act does not establish any statutory intellectual property rights, it prohibits unfair competition that would infringe others' business interest in (1) – (4). As for civil remedies, the act provides both monetary damages and injunctive relief.

Chapter 10: Financing

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10.1 Licensing requirements for banks, etc

10.1.1 *Banking Act*

An entity that intends to engage in 'banking business' is required to obtain a licence from the Prime Minister in accordance with the Banking Act. The Banking Act defines 'banking business' as the operation of a business conducting any of the following activities:

- acceptance of deposits together with lending funds or discounting bills; or
- fund transfers for customers

In order to obtain a banking business licence, the applicant must be a stock company having a board of directors, a board or a committee of company auditors and an accounting auditor. The stated capital of the applicant must not be less than JPY 2bn. In addition, the applicant must satisfy other licence requirements, such as securing qualified directors experienced in banking business and establishing a system necessary for the proper execution of the banking business. The FSA of Japan (JFSA) supervises banks.

If a foreign bank wishes to engage in banking business in Japan, it is required to specify a single branch in Japan that serves as the principal base of the foreign bank's banking business in Japan, and it must obtain a banking licence from the Prime Minister. The branch is supervised by the JFSA.

10.1.2 Money Lending Business Act

The act of lending money as a business does not fall under banking business but generally falls under 'money lending business' under the Money Lending Business Act (MLBA). An entity that intends to engage in money lending business is required to establish a business office or other office in Japan and to register with the Prime Minister or prefectural governor. In order to complete such a registration, the applicant must satisfy the registration requirements, such as securing persons with at least three years' experience in loan business, as well as a registered chief of money lending operations; having net assets of at least JPY 50m; and establishing a system necessary for the proper execution of money lending business. Money lending business operators are subject to supervision by the JFSA and the relevant prefectural government.

10.1.3 Applicability of the Civil Code, etc to money lending business

A loan agreement is subject to the Civil Code, and the content of a contract may be freely determined by agreement between the lender and the borrower under the principle of the freedom of contract. However, the Interest Rate Restriction Act stipulates the maximum rates (15 – 20 per cent of the amount of the loan's principal). If the interest rate exceeds the maximum rate, the amount in excess is void. The Act Regulating the Receipt of Contributions, the Receipt of Deposits, and Interest Rates also stipulates the maximum rate (20 per cent of the amount of the loan's principal). If the operator of a loan business exceeds the maximum rate, such a person (including the representative, an agent or employee if the person is a juridical person) is subject to criminal punishment. Further, if a borrower is an individual who is not categorised as a business operator, the Consumer Contract Act applies, and any one-sided contract clause that impairs the interests of consumers is void.

10.2 Requirements for issuing bonds

10.2.1 Companies Act

Bonds issued in Japan include public bonds, such as government bonds and municipal bonds, and private bonds, such as straight bonds, convertible bonds and financial bonds issued by financial institutions under special laws. The issuance of corporate bonds is one of the primary financing methods used by stock companies.

Under the Companies Act, if a stock company intends to issue corporate bonds, it must determine the subscription requirements, such as the total amount, amount of each bond, interest rate, method and due date of redemption, method and due date of interest payments, and other matters relating to the bonds and specified in the Companies Act. In the case of a stock company with a board of directors, such a decision is generally made by the board of directors, but the board of directors may delegate such a decision to an individual director if the board of directors determines the total amount and certain other matters regarding the bonds prescribed in the Companies Act. A third party must be appointed as a bond manager unless: (1) the amount of each bond is JPY 100m or more; or (2) the number obtained by dividing the total amount of the class of bonds to be issued by the minimum amount of each bond of the class is less than 50. A bond manager is a person who receives payments, preserves rights of claims and otherwise manages bonds on behalf of bondholders. In cases where a bond manager is not required, a fiscal agent is generally appointed to handle the payment process on behalf of the issuing company. Bondholders' meetings may be convened to make resolutions on matters in relation to the interests of the bondholders, but in practice there are not many cases of holding bondholders' meetings due to the large administrative burden.

10.2.2 Financial Instruments and Exchange Act

A corporate bond falls under the definition of 'Securities' in the Financial Instruments and Exchange Act (FIEA), and such Securities are subject to disclosure requirements in accordance with the FIEA. Offerings of corporate bonds may not be made without filing a Securities Registration Statement (SRS) with the competent local finance bureau, unless exempted from the registration requirements. An SRS describes, in detail, the content of the Securities (securities information) and the business outline, financial status and so on of the issuer (corporate information) and is made available for public inspection. In addition, the issuer is required to prepare a prospectus containing almost the same content as the SRS and must deliver it to investors. Further, the issuer is subject to ongoing disclosure obligations and must file an annual securities report and so on. These disclosure requirements only apply to public offerings and do not apply to private placements. There are three types of private placements: (1) private placement to qualified institutional investors; (2) private placement to professional investors; and (3) private placement to a small number of investors. The concept of 'private placement to professional investors' was introduced in 2008, aiming at creating a new professional market. A professional investor as defined in the FIEA means any of the qualified institutional investors, the government of Japan, the Bank of Japan and certain other investors considered able properly to manage risk arising from financial transactions based on their knowledge and experience, as well as the status of assets specified in the FIEA.

10.3 Requirements for issuing stocks

10.3.1 Companies Act

The Companies Act governs the procedures for issuing new shares. Under the Companies Act, the issuance of new shares is broadly divided into 'allotment to shareholders' and 'other than allotment to shareholders'. An 'allotment to shareholders' grants all existing shareholders the right to receive an allotment of shares in proportion to the number of shares they hold. This method is generally used for private companies where shareholders are interested in maintaining their shareholding ratio. On the other hand, 'other than allotment to shareholders' is classified into 'public offerings', where shares are issued to many and unspecified investors, and 'third-party share issuance', where shares are issued to specific investors. A 'public offering' is generally used to raise funds for listed companies or companies seeking IPOs of their shares. An 'allocation to third parties' is often used not only for raising funds but also for strengthening business relationships with underwriters or for bailing out companies facing financial difficulties.

In the issuance of shares, a stock company needs to determine the subscription requirements in accordance with the Companies Act. For example, for a third-party share issuance by a public company, a resolution of the board of directors is generally required unless such an issuance can be classified as an issuance favourable to underwriters. However, where shares are issued at a particularly favourable price, such an issuance requires a special resolution of a shareholders' meeting. The term 'a particularly favourable amount' means an amount particularly low compared with 'the fair amount to be paid', and the term 'fair amount to be paid' means the market value of shares; in other words, the latest market price of shares for listed companies. According to the Guidelines for Handling of Third-Party Share Issuance of the Japan Securities Dealers Association, as it is assumed that an issuance of new shares at ten per cent or less discount is not an advantageous issuance, in practice the amount to be paid will be the price discounted by less than ten per cent of the market price.

10.3.2 FIEA

Shares fall under the definition of 'Securities' in the FIEA and therefore the disclosure regulations under the FIEA apply. The framework of disclosure regulations is essentially the same as that for corporate bonds.

10.4 Other financings

10.4.1 Crowdfunding

Crowdfunding is a fundraising method whereby an entity that needs money raises funds from an unspecified number of investors through an internet platform. In 2014 a small-amount investment-type crowdfunding system was introduced in Japan to promote the supply of risk money. The 'small-amount' here means that the total offering amount is less than JPY 100m and the investment amount per person is less than JPY 500,000. Under the FIEA, the market entry requirements that apply to a business operator handling a public offering or private placement of unlisted stocks or funds were relaxed, while new requirements were imposed on them. The new requirements include the duty to disclose appropriate information through the internet and the duty to conduct due diligence on the business of venture companies.

10.4.2 Peer-to-peer lending

Peer-to-peer lending is categorised as social lending. Under this system, an unspecified number of investors lends money to SME or individual seeking funds through an online platform. In a typical scheme, a business operator collects contributions in a silent partnership (*tokumei kumiai*) from investors and lends money to a person seeking funds by using such contributions. Such a business operator is required to register as a money lending business operator under the MLBA. In addition, such a business operator is required to register as a Type II financial instruments business for soliciting contributions in a silent partnership, which falls under the concept of 'deemed securities' as defined in the FIEA.

Chapter 11: Privacy laws and data protection

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The Act on the Protection of Personal Information (APPI) is the main data protection legislation in Japan and imposes legal obligations on private business operators who handle personal information (each is a 'Handling Operator'). Replace with: The amendments to APPI were enacted in June 2020, and most clauses will take effect by June 2022.

Another important law is the Act on the Use of Numbers to Identify a Specific Individual in the Administrative Procedure (the 'My Number Act'), which stipulates special rules for what is known in Japan as My Number, a 12-digit individual number assigned to each resident of Japan.

The Personal Information Protection Commission (PPC) is the primary regulator responsible for the APPI and the My Number Act, and publishes guidelines for the handling of personal information.

In order to understand the restrictions under the APPI, it is important to distinguish between three terms: personal information, personal data and retained personal data.

Personal information means information about living individuals that: (1) can identify specific individuals; or (2) contains an individual identification code as defined by the APPI.

Personal data means personal information contained in a personal information database, which is a collection of information (which includes personal information) that is systematically organised to enable a computer or other means to search for particular personal information.

Retained personal data means personal data that a Handling Operator has the authority to disclose, correct, add or delete content from; and discontinue the use of, erase or discontinue its provision to a third party, excluding personal data that is scheduled to be deleted within six months (note that the anticipated amendment of the APPI is likely to remove this six-month qualification) and certain other limited personal data.

The Handling Operator has various obligations under the APPI, including the following:

- It must specify and make known to the data subject the purpose of collecting that subject's personal information.
- It cannot use personal information for any other specified purpose without the consent of the data subject.
- It must establish appropriate safeguards to protect personal data.
- It must manage employees and data-handling service providers on their handling of personal data.
- It cannot transfer personal data to another entity without the opt-in consent of the data subject, unless it falls under an exception under the APPI. Exceptions include instances when the transfer is required by law or is necessary to perform governmental duties; to protect the life, body or property of a person; or to improve public health. Other major exceptions include the delegation of the handling of personal data to another entity; joint use of personal data with another entity; business succession resulting from a merger or other legal reasons; or filing of a notification of opt-out consent with the PPC. Note that the anticipated amendment of the APPI may change the opt-out scheme.
- It must keep a record of the provision of personal data to a third party.
- It cannot transfer personal data to countries that do not have sufficient data protection safeguards without the consent of the data subject. The data subject's consent to overseas data transfers is not necessary only if: (1) the foreign country is designated by the PPC as a country with a data protection regime with a level of protection equivalent to that of Japan (only member countries of the European Economic Area and the UK have been designated to date); or (2) the recipient has a data protection system that meets the standards prescribed by the PPC. Please note that the APPI has no general data localisation requirements for personal information.
- It must make certain mandatory elements accessible to data subjects and respond to data subjects' requests (to disclose, correct, add or delete content from; and discontinue the use of, erase or discontinue its provision to a third party) regarding retained personal data.
- It must endeavour to notify the PPC of data breaches, and the APPI recommends that it notify data subjects of data beaches. Note that notification to the PPC and data subjects may become legal obligations under the anticipated amendment of the APPI.
- It must endeavour to keep personal data accurate and to erase personal data without delay when it becomes unnecessary to use it.

An outline of the sanctions for violations of the APPI is as follows:

- The PPC may require a Handling Operator to report or submit materials regarding its handling of personal information, and may enter a Handling Operator's offices or other places to investigate, make enquiries and check records or other documents (Article 40).
- The PPC may provide guidance or advice to a Handling Operator (Article 41).
- The PPC may recommend that a Handling Operator cease a violation and take other necessary measures to correct the violation (Article 42.1).
- The PPC may order a Handling Operator to take necessary measures to implement the PPC's recommendations and to rectify certain violations of the APPI (Articles 42.2 and 42.3).
- If a Handling Operator breaches an order of the PPC that is issued as part of an administrative sanction (note that 'order' does not include guidance, advice or a recommendation from the PPC), it may be subject to imprisonment of up to six months or a fine of up to JPY 300,000. If the breach is committed by an employee of an entity, that entity will be subject to a fine of up to JPY 300,000. Note that the anticipated amendment of the APPI may toughen the penalties Especially in the case of a corporate body violating an order of the PPC, the penalty will be a fine of up to JPY 100m.

Chapter 12: Competition law

Yusuke Takamiya, Mori Hamada & Matsumoto, Tokyo

12.1 Relevant legislation

The Anti-Monopoly Act (AMA) is the fundamental legislation of Japan's antitrust legal framework. It was enacted in 1947 and is sometimes called 'Japan's Economic Constitution'.

The AMA covers multiple areas of antitrust practice, such as cartel issues, merger filings, abuse of monopoly and unfair trade practices. However, given that the language of the AMA provisions is ambiguous, businesses are strongly advised to refer to the Japan Fair Trade Commission (JFTC) enforcement policies and guidelines and case law for further guidance.

Other statutes and rules relating to antitrust rules are:

- General Designation of Unfair Trade Practices, which identifies 16 categories of unfair trade practices in accordance with the framework of the AMA;
- Act against Delay in the Payment of Subcontract Proceeds, which regulates the abuse of a superior bargaining position by large companies;
- Unfair Competition Prevention Act, which regulates some kinds of unfair trade practices, such as trade secrets; and
- Act against Unjustifiable Premiums and Misleading Representations, which regulates unfair trade practices especially relevant to consumer transactions.

12.2 Relevant authorities

The principal authority charged with the enforcement of the AMA is the JFTC. The JFTC is headquartered in Tokyo and has over 800 officials. It consists of a chairperson and four commissioners. It also has a Secretariat, which handles policy-making; an Economic Affairs Bureau, which handles merger reviews and various general enforcement of the AMA; and an Investigation Bureau, which handles specific investigations of the alleged violation of the AMA.

The other major authorities tasked with enforcing antitrust laws and policies are:

- Public Prosecutor's Office (PPO), which investigates and prosecutes criminal violations after receiving the JFTC's criminal complaint;
- Ministry of Economy, Industry and Trade, which handles competition policy from an industrial policy perspective;
- Consumer Affairs Agency, which handles enforcement and policy-making for unfair trade practices regarding consumer transactions, such as misleading advertisements; and
- courts, which handle private antitrust cases, appeals against the JFTC's administrative actions and criminal prosecutions by the PPO.

12.3 General enforcement trends

The majority of the targets of the JFTC's enforcement consists of companies in Japan. However, the JFTC is increasing its investigation of foreign companies, especially in merger control cases. The JFTC sometimes makes high-profile investigations of foreign companies or their Japan subsidiaries.

In private practice around five large Japanese law firms that are all headquartered in Tokyo typically handle large merger control cases and government investigations. At the same time, a couple of boutique law firms focus on antitrust and consumer protection affairs. Some international law firms have antitrust teams that include Japanese qualified attorneys working at their Tokyo offices.

Apart from law firms, a couple of world-renowned economic consulting firms with offices in Tokyo are also active in the practice. Economic analysis is becoming increasingly important in high-profile cases, especially in merger reviews. The JFTC has some in-house economists as well, who are often seconded from academic institutions and private practice.

12.4 Cartel cases

12.4.1 General trends

In the early half of the 2010s enforcement actions against cartels and bid rigging were quite active. By contrast, the number of cartel investigations in the last couple of years has been moderate.

12.4.2 Prohibition

The AMA prohibits 'unreasonable restraint of trade', which includes collusive activities such as cartels and bid rigging. However, the prohibition requires that there is a 'substantial restraint on competition' in the relevant market. Thus, cartels and bid rigging are not per se illegal in Japan.

12.4.3 Enforcement

Cartel activities can be both administrative and criminal violations in Japan. The JFTC, however, usually first pursues an administrative case and imposes administrative sanctions. A criminal investigation commences only after the JFTC's accusation to the PPO.

The issuance of a cease-and-desist order is the most common administrative sanction. This order directs the cessation of specific conduct by cartel participants. Typically, it also imposes an obligation to establish or improve a participant's compliance system to prevent future antitrust violations.

Another common administrative sanction is an administrative surcharge, which amounts to 'monetary fines' in other major jurisdictions. The JFTC has no discretion on the amount of the surcharge as it is automatically calculated as the multiple of the following factors: (1) the volume of commerce affected by the cartel for three years before cessation of the violation; (2) fixed percentage (manufacturer: ten per cent; retailer: three per cent; and wholesaler: two per cent); and (3) aggravating and mitigating factors.

Cartels and bid rigging are also subject to criminal fines and imprisonment. Moreover, cartel participants are often debarred from various public procurements.

12.4.4 Leniency programme

A leniency programme is available in Japan and has been vigorously used since its introduction in 2006. The benefits for the first applicant are huge as it can receive full immunity from both the administrative surcharge and criminal prosecution. Employees are also entitled to immunity from personal criminal liability. There are certain, though lesser, benefits for subsequent applicants who can receive a reduction of the administrative surcharge (ie, they cannot receive immunity from criminal liability).

12.5 Merger controls

12.5.1 General trends

The number of filings each year in Japan is around 300. While there are two phases in the merger control regime, most cases were cleared during Phase I. The average period for merger review after the submission of the official application is two to three weeks. However, for difficult or complex cases, the entire review period may last several months to over a year.

12.5.2 Fundamental factors of merger control

The AMA requires the filing of a mandatory merger notification under threat of sanctions. The reporting party is required to make the notification at least 30 days prior to a filing event. Non-notifiable transactions may be reviewed if there are substantive concerns. The types of transactions caught in the notice requirement are broad, including share acquisition, statutory merger, statutory demerger (ie, corporate split), and assets or business transfer. The two fundamental thresholds for notification are relevant to the consolidated turnover in Japan (CTJ) of the following parties:

- acquirer/one participating party: CTJ > JPY 20bn; and
- target/other party: CTJ > JPY 5bn (JPY 3bn for assets or business transfer).

12.5.3 Enforcement and sanctions

The failure to notify may be penalised by criminal fines of less than JPY 2m. In actual practice, however, there have been no sanctioned cases to date. Nonetheless, the JFTC, from time to time, requests a written explanation for a failure to notify.

The JFTC may open an investigation on a non-reporting transaction if it believes that the deal may raise a substantial competition concern. Thus, to avoid unnecessary friction with the JFTC, the parties may make a voluntary merger filing if there is a possible substantial competition issue in the transaction.

12.6 Other areas of antitrust law

Aforementioned, in addition to cartels and merger control, the AMA also regulates the abuse of monopolies and unfair trade practices. Although those fields are relatively remote for foreign businesses, some regulations, such as prohibitions against retail price maintenance, abuse of a superior bargaining position, trade with restrictive terms and exclusive dealings, may be critical for foreign businesses that wish to conduct business in Japan.

Chapter 13: Dispute resolution

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13.1 Judicial courts

13.1.1 Structure

Since Japan is not a federal state, all judicial courts are integrated into one nationwide court system. The Constitution of Japan anticipates lower courts in addition to the Supreme Court, but it is silent on the number of instances. According to the Code of Civil Procedure (CCJ), in most civil cases there are three instances: a regional court as the first instance, a high court as the second instance, and the Supreme Court as the third and last instance. Since the grounds for appeal to the Supreme Court are very limited (eg, on the grounds that a judgment contains a misinterpretation of the Constitution or any other violation of the Constitution), realistically, for most cases, it is a two-instance system. Among others, factual assertions and fact-finding can be made only in the first two instances.

Japanese law belongs to the Roman law system, and this also applies to procedural law such as the CCJ. The current CCJ of 1996 continued many legal concepts from the initial CCJ of 1890, the first draft of which was prepared by a German jurist, Eduard Hermann Robert Techow. Accordingly, the German influence on the Japanese CCJ is still strong.

13.1.2 Court practice

There is a widespread myth that Japanese people do not like court cases. This is somewhat accurate, especially in comparison with the US, where there is much litigation. However, the reason is not only because of the Japanese culture, in which people do not like open confrontation, but also because the courts do not necessarily function quickly and in a cost-effective manner. Some scholars use the term '20 per cent justice', which implies that only 20 per cent of Japanese citizens receive adequate judicial services. In fact, according to *Doing Business 2019* published by the World Bank, Japan is ranked as low as No 52 among the 190 countries in the category 'Enforcing Contracts'.[1] A frequently asked question for business lawyers in many jurisdictions is whether a lawsuit is advisable or not, and most often the answer is negative if a lawsuit can reasonably be avoided due to various jurisdiction-specific reasons. The following factors should be considered before initiating a lawsuit in Japan:

- overloaded judges: in 2018 the courts accepted 1,552,708 new civil (and administrative) cases, while there were only 2,782 judges in all Japan; this roughly means 558 new civil cases per judge, in addition to criminal and family law cases;
- longer court proceedings: according to a report prepared by the Supreme Court, in 2018 the first instance took nine months on average, and the second instance took 5.7 months on average;[2]
- settlements: the parties are frequently encouraged, recommended or expected by the judge to make a settlement rather than waiting for a verdict;
- relatively weak fact-finding: Japanese law does not have a discovery system like in the US, and Japanese judges have a tendency not to exercise the judge's right in fact-finding aggressively; judges are vested by the CCJ with the power to issue an order to a party to submit written evidence under his possession, but this power is rarely exercised; and, on another note, perjury is a crime, but it is extremely rare that a witness is indicted due to his/her false testimony;
- relatively conservative fact-finding: Japanese courts tend to impose a high burden of proof, and tend to be careful in admitting the causal relationship and in calculating the damage to be awarded;

1 See www.doingbusiness.org/content/dam/doingBusiness/media/Annual-Reports/English/DB2019-report_web-version.pdf accessed 13 May 2020

2 See www.courts.go.jp/toukei_siryou/siryo/hokoku_08/index.html accessed 13 May 2020.

- inefficient procedure: the submission of briefs or evidence via the internet has not yet been allowed, and there are many occasions in which the lawyer must appear before the court in person, which results in additional time and legal fees; and
- legal fees: although the lawyer's fees tend not to be as high as those in some Western countries, in a contractual dispute each party shall bear its own lawyer's fee, which is a big problem for foreign parties in particular because its legal fee will be increased by an expensive translation cost.

Some recent trends may make Japanese courts more attractive. For example:

- Intellectual Property High Courts were established in 2005. The Constitution of Japan prohibits the establishment of special courts outside the court hierarchy, with the Supreme Court at the top. The Intellectual Property High Courts are constitutional because they are integrated into the existing court hierarchy.
- In March 2018 the Cabinet Secretariat announced its plan to introduce IT into court procedures in three phases. Phase 1 began the following year, and a web meeting system has been introduced in some courts. From 2020 the arrangement of issues can be made at some courts in Tokyo, Osaka and several other major cities using a cloud service. Japanese courts had not necessarily been enthusiastic about the introduction of IT, but the coronavirus pandemic may accelerate the reform process.

13.2 Alternative dispute resolution

A non-binding conciliation (*chōtei*) is commonly used in family law or for labour law cases. A special type of conciliation was conducted by the Conflict Resolution Center for Nuclear Damages, established based on the Act on Compensation for Nuclear Damage, in a systematic and concentrated manner to offer a special conciliation service to cope with the largest civil law disputes in Japanese judicial history as a result of the nuclear power plant accident in Fukushima in 2011. By the end of July 2012 only about 20 claims for damages related to the nuclear accident had been submitted to judicial courts, while 3,398 applications had been received by the Conflict Resolution Center for Nuclear Damages.

The inclusion of an arbitration (*ch sai*) clause in cross border transactions in increasing. However, the actual number of arbitration cases is still limited. Since the arbitration language of most cases is English, and considering the high language barrier in Japan, if something goes wrong with some of these agreements and arbitrations start one after another at some point in the future, it will be a big challenge for the Japanese parties.

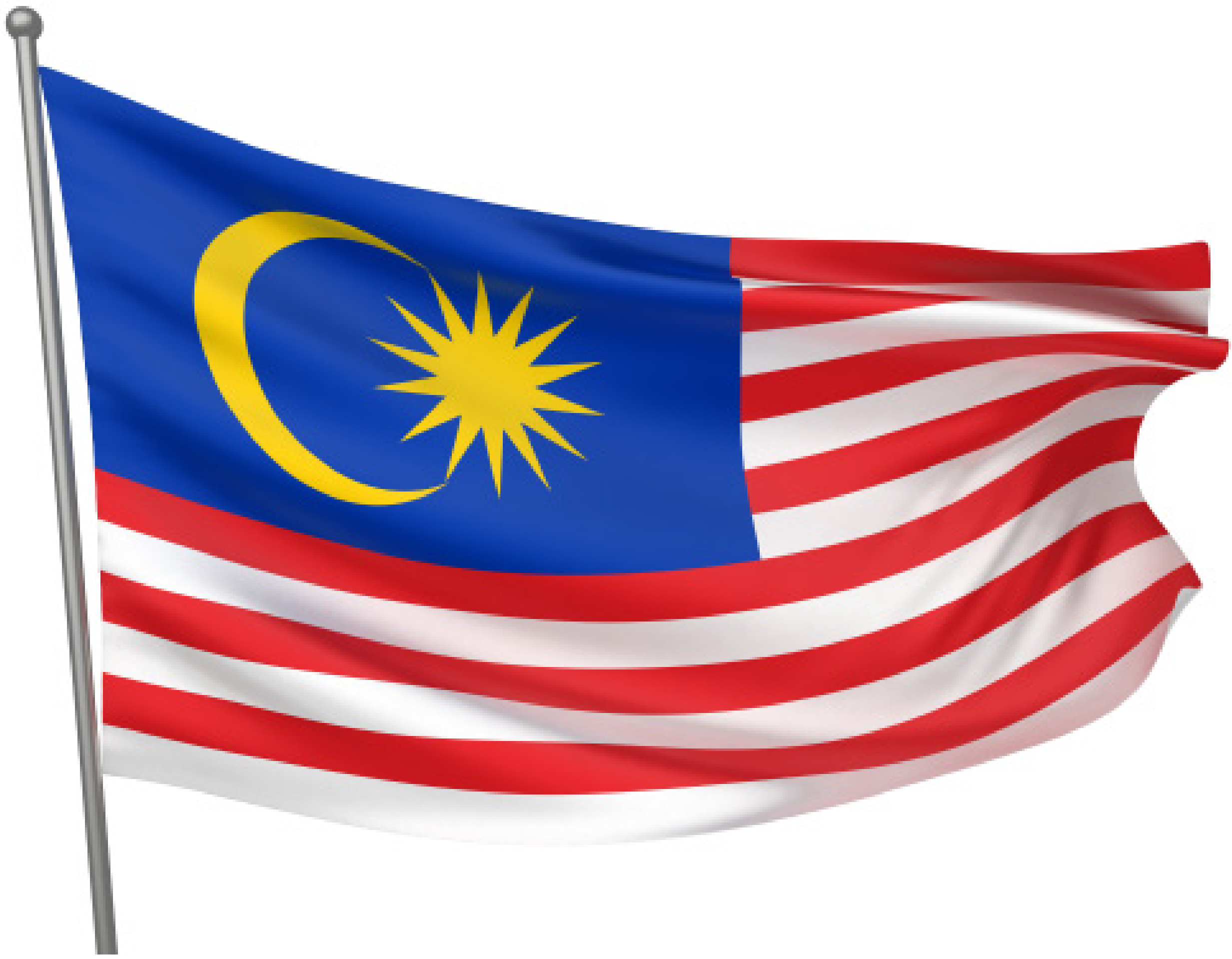
13.2.1 Enforcement of foreign judgments/arbitration awards in Japan

Japan is one of the more than 150 signatories to the New York Convention, so the enforcement of an arbitration award is not complicated.

Enforcement in Japan of a judgment by a foreign judicial court is not simple: Article 118 of the CCJ sets forth that a final and binding judgment rendered by a foreign court shall be effective only where it meets all the following requirements: (1) the jurisdiction of the foreign court is recognised under laws or regulations, or conventions or treaties; (2) the defendant has been served (excluding being served by the publication or any other means similar thereto) with a summons or order necessary for the commencement of the suit, or has appeared without being so served; (3) the content of the judgment and the court proceedings are not contrary to public policy in Japan; and (4) a mutual guarantee exists.

Among these conditions, (4) refers to reciprocity; for example, it is considered that there is reciprocity between Japan and Germany, while there is no reciprocity between Japan and China. In the US reciprocity depends on the state. As regards (3), one example that cannot be enforced in Japan due to *ordre public* violation is a US judgment that orders the paying of punitive damages. Furthermore, there is a tendency for this condition to be abused by Japanese defendants by prolonging the execution procedure through arguing that the foreign judgment violates public order in Japan, with the hidden intention of making a settlement at a lower amount.

Malaysia



Chapter 1: Introduction

Janet Looi, Skrine, Kuala Lumpur

Malaysia consists of 13 states and three federal territories, separated by the South China Sea into two regions: Peninsular Malaysia and Borneo's East Malaysia. Kuala Lumpur is the national capital and largest city, while Putrajaya is the seat of the federal government. With a population of over 30 million, Malaysia is the world's 44th most populous country.

The country is multi-ethnic and multi-cultural. About half the population is ethnically Malay, with large minorities of Chinese, Indians and indigenous peoples. While recognising Islam as the country's established religion, the Constitution grants freedom of religion to non-Muslims.

The official language of Malaysia is Bahasa Malaysia. English is the most common business language. Mandarin and local dialects are widely used forms of communication.

Malaysia is a member of the ASEAN, which is an intergovernmental organisation aimed primarily at promoting economic growth and regional stability among its members.

The overall infrastructure of Malaysia is one of the most developed in Asia. Malaysia is highly ranked for the quality of its roads, port infrastructure and air transport infrastructure. The country has seven international ports and five international airports (all with air cargo facilities). Its telecommunications network is served by digital and fibre optic technology.

Malaysia is a relatively open, state-orientated and newly industrialised market economy. Technological advancement has become an integral part of Malaysia's growth as an industrialised nation through the country's involvement in advanced electronics manufacturing, R&D, biotechnology, photonics, logistics, design, innovation and a highly automated manufacturing sector, to name a few. Industries in Malaysia are predominantly located in over 500 industrial estates and free zones throughout the country. These zones are categorised as export processing zones, which cater to the requirements of export-orientated industries. There are also specialised parks that have been developed to cater to the needs of specific industries. Malaysia's objective is to become a hub for other value chain activities, such as R&D, design and development, procurement, logistics, distribution and marketing, business support services and shared services.

According to the World Bank's *Doing Business 2020* report, Malaysia is ranked 12th among 190 countries, an improvement from 15th in 2019, while the 2020 Index of Economic Freedom, which measures, among other things, investment freedom, trade freedom, judicial effectiveness, government spending and fiscal health, puts Malaysia's economic freedom score at 74.7. This ranks Malaysia 24th in the world and 6th among 42 countries in the Asia Pacific region, above South Korea, Japan, Thailand, Indonesia, the Philippines and a number of other ASEAN countries.

Chapter 2: The business environment

Yee Mei Ken, Shearn Delamore & Co, Kuala Lumpur

2.1 Government structure

Malaysia is a federation of 13 states. The Federation of Malaysia practises parliamentary democracy, with a federal constitutional monarch, the Yang di-Pertuan Agong (the 'King'). The King is the Supreme Head of the Federation and is commonly referred to as the head of state.

Based on the Federal Constitution, one of the characteristics of the parliamentary democracy practised in Malaysia is the separation of powers into three parts: legislative, judiciary and executive. The separation of powers also occurs at the federal and state levels, where the federal and state governments are accorded defined law-making powers based on the Federal List, State List and Concurrent List.

2.1.1 Legislature

At the federal level, the bicameral Parliament headed by the King is comprised of two houses: the Upper House (House of Senate or Dewan Negara) and the Lower House (House of Representatives or Dewan Rakyat). The Dewan Negara has 70 Senators, consisting of 44 members appointed by the King and 26 members elected by the State Legislative Assemblies. The Dewan Rakyat, on the other hand, is made up of 222 members elected through a general election every five years.

Primarily, the Parliament enacts and approves federal laws, as well as amends and examines existing federal laws and government policies. The Dewan Rakyat also functions as a forum for its members to debate and question government policies and national issues.

Draft bills may originate from either house, except money bills, which are initiated in the Dewan Rakyat. All draft bills approved by either house are sent to the other house for approval. In each phase, a chamber of Parliament must undergo four stages: the first reading, second reading, discussion at committee level and third reading of the bills. If the bills are passed by both chambers, they are assented by the King through affixing the Public Seal. Thereafter, the bills become law and enforceable upon publication in the Government Gazette.

2.1.2 Executive

The executive authority of the federation is vested in and led by the King subject to the provisions and limitations enshrined in the Federal Constitution. The King appoints a Council of Ministers to form the Cabinet (Jemaah Menteri) to advise the King on the execution of his functions as the head of the executive authority. The ministers are appointed by the King, on the advice of the Prime Minister, and shall be members of either the Dewan Negara or Dewan Rakyat.

In governing the country, the King acts on the advice of the Prime Minister, who leads the Cabinet of Ministers. In short, the Prime Minister acts as the head of the government.

The Cabinet holds the highest administrative authority in the country and is responsible for forming government policy. Each minister is assigned different portfolios and is usually assisted by a deputy minister. The Cabinet is collectively accountable to Parliament for every decision it makes.

In appointing the Prime Minister, the paramount consideration of the King is that the Prime Minister shall be likely to command the confidence of the majority of the members of the Dewan Rakyat. As such, if the Prime Minister ceases to command the confidence of the majority of the members of the Dewan Rakyat, then, unless at his request the King dissolves Parliament, the Prime Minister shall tender his/her resignation of the Cabinet.

2.1.3 Judiciary

The judiciary refers to the Malaysian court system, which is made up of a body of judges. Judges interpret and implement laws enacted by the legislature, executive and state assemblies. The judiciary is also empowered to interpret the highest law of the land, the Federal Constitution, and declare any written law to be unconstitutional or illegal.

The judiciary body and the court structure are enshrined under Article 121 of the Federal Constitution. The hierarchy of the courts is classified into subordinate courts and superior courts. Subordinate courts refer to the Magistrates' Court and the Sessions Court. The superior courts consist of the two High Courts (High Court in Malaya and High Court in Sabah and Sarawak) and two Appellate Courts, namely the Court of Appeal and the Federal Court, which is also the apex court in Malaysia.

2.2 Legal system

There are multiple sources of law in Malaysia. 'Law' is defined under Article 162(2) of the Federal Constitution to include any written law, common law operating in the federation and any custom or usage having the force of law in the federation. Under the Civil Law Act, 1956, the common law of England and the rules of equity of certain cut-off dates are also statutorily recognised as sources of law.

Therefore, Malaysian law can broadly be categorised into two groups: written and unwritten law.

2.2.1 Written law

The written law of Malaysia is made up largely of the following components:

- the Federal Constitution and the Constitutions of the 13 states of Malaysia;
- legislation enacted by Parliament and the state assemblies;
- subsidiary or delegated legislation by persons or bodies empowered by the Acts of Parliament or Enactments of the state assemblies;
- ordinances made by the King during a state of emergency; and
- the Islamic law or Syariah Enactments.

2.2.2 Unwritten law

The unwritten law of Malaysia consists mainly of the following:

- principles of English Law applicable and permitted by the local circumstances and subject to such qualifications as local circumstances render necessary;
- judicial decisions or case law of the two High Courts, the Court of Appeal and the Federal Court;
- judicial decisions of the former superior courts, that is, the Supreme Court, the former Federal Court and the Privy Council;
- customary laws of local inhabitants, including native practices in Sabah and Sarawak; and
- the principles of Syariah in the form of judicial decisions.

Chapter 3: Business and corporate structures

Michelle Wong Min Er, Shearn Delamore & Co, Kuala Lumpur

3.1 Common forms of legal entities

The most common form of legal entity in Malaysia is the private company limited by shares incorporated pursuant to the Malaysian Companies Act, 2016. It is a separate legal entity from that of its shareholders/members, and it can have up to 50 members. A private company shall restrict the transfer of its shares.

Unless regulated by industry or business rules and requirements, a private company can be incorporated with a sole shareholder. A private company must have, at all times, a minimum of one resident director, that is, a director who ordinarily resides in Malaysia.

Other forms of legal entity are a public company limited by shares, a company limited by guarantee and an unlimited company, all of which can be incorporated pursuant to the Companies Act.

The below information focuses on private companies.

3.2 Incorporation process

A name search must first be carried out to ensure that the proposed name of the company is available. Once the name is approved, the name can be reserved and an application for registration of the company is to be submitted online within 30 days after the name is approved to the Companies Commission of Malaysia (CCM) with the following information and an incorporation fee of MYR 1,000:

- proposed company name;
- status of a private or public company;
- proposed type of business;

- address of the registered office;
- business address;
- complete details of the directors(s) and promoter(s);
- declaration from the directors(s) and promoter(s);
- declaration of compliance from individuals responsible for incorporation; and
- additional documents (if any).

Upon the submission of complete information, and compliance with all required procedures, the CCM will issue a notice of registration, which signifies that the company has been successfully incorporated. If the company requires, it can submit a prescribed fee to the CCM to request a certificate of incorporation.

The incorporation process is fairly quick and can be completed within a week or two, depending on the compilation and submission of the necessary information, documents and fee required.

3.3 Ongoing reporting and disclosure obligations

Apart from ongoing documents and notifications that are required to be filed or lodged under the Companies Act (eg, changes to the directors, register of members and issuance of new shares, every year, a private company is required to lodge with the CCM:

- an annual return not later than 30 days from the anniversary of its incorporation date; and
- the financial statements (which are to be audited unless exempt pursuant to the Companies Act) and directors' report within 30 days of the circulation of the documents to the shareholders of the company. The documents have to be circulated to the shareholders within six months of the private company's financial year end. An auditor is required to be appointed for each financial year of the private company (unless exempt pursuant to the Companies Act according to the conditions determined by the CCM).

3.4 Management structures

The board of directors has all the powers necessary for managing, directing and supervising the management of the business and affairs of the company subject to any modification, exception or limitation contained in the Companies Act or in the constitution of the company.

The Companies Act does not impose a limit on the maximum number of directors, but a company may want to limit the number of directors in its constitution. The board of directors can set out their powers in the constitution of a company, and officers can have limits of authority imposed on them. The board of directors may delegate its powers to any committee of the board of directors, director, officer, employee, expert or any other person.

There is no legal requirement to have a risk/compliance/governance committee or officer for a private company.

3.5 Director, officer and shareholder liability

A company incorporated in Malaysia can have a constitution to set out the rights, powers, duties and obligations of the company, each director and each member of the company (to the extent that they are permitted to be modified in accordance with the Companies Act and the constitution does not contravene and is not inconsistent with the Companies Act). If a company has no constitution, the company, each director and each member of the company shall have the rights, powers, duties and obligations set out in the Companies Act.

A director of a company shall at all times exercise his/her powers in accordance with the Companies Act, for a proper purpose and in good faith in the best interest of the company. The directors owe a fiduciary duty to the company.

Directors and officers of a company can be personally liable for breaches of the Companies Act. For example, a failure to keep accounting records can result in every officer who is in breach to be liable, on conviction, to a fine not exceeding MYR 500,000 or imprisonment for a term not exceeding three years, or both.

A private company is a separate legal entity from that of its members, and the liability of its members is limited to the amount, if any, unpaid on shares held by the members. While the Companies Act establishes that a company incorporated in Malaysia is a separate legal entity, cases decided in Malaysia have, in certain instances, pierced the corporate veil where there is evidence of actual fraud in common law, or some inequitable or unconscionable conduct amounting to fraud in equity.

Chapter 4: Takeovers

Janet Looi, Skrine, Kuala Lumpur

4.1 Overview of key laws and regulations

Takeovers of public companies in Malaysia are primarily governed by the Malaysian Code on Takeovers and Mergers, 2016 (the 'Code'), the Rules on Takeovers, Mergers and Compulsory Acquisitions, 2016 (the 'Rules') and the Capital Markets and Services Act, 2007 CMSA.

The Code, which is issued by the Securities Commission Malaysia and enacted pursuant to Section 217 of the CMSA, sets out 12 principles to be observed and complied with by all persons engaged in any transaction that is subject to the Code and Rules. This includes, among others, the principle that all shareholders must be treated equally in any takeover transaction and should not be disadvantaged by the treatment or conduct of any relevant party to a takeover.

The Rules stipulate operational and conduct requirements in relation to takeovers, and are issued by the Securities Commission under section 377 of the CMSA.

The Code and Rules apply to mergers and takeovers of listed companies, unlisted public companies with more than 50 shareholders and net assets of MYR 15m or more, business trusts listed in Malaysia and real estate investment trusts listed in Malaysia.

If the disposal, acquirer or target in a takeover is listed on Bursa Malaysia Securities Berhad ('Bursa'), they are also subject to the listing requirements issued by Bursa.

4.2 Types of takeover

4.2.1 Mandatory offer

An acquirer, together with persons acting in concert (PAC) with the acquirer (if any), triggers the obligation to extend a mandatory offer to acquire all the shares of a target that are not already owned by the acquirer and any PAC, if the acquirer together with any PAC:

- obtains 'control' of the target (ie, acquires more than 33 per cent of the target); or
- triggers the creeping provisions (ie, acquires more than two per cent of the voting rights or shares of a target in any six-month period where the acquirer and the PAC's shareholding was more than 33 per cent but less than 50 per cent of the voting rights or shares in the target.

4.2.2 Voluntary offer

An acquirer who has not incurred an obligation to make a mandatory offer is allowed to make a voluntary offer to acquire the voting shares or rights of a target that is not already owned by the acquirer.

However, such a voluntary offer must be conditional upon the acquirer having received acceptances that would result in the acquirer holding in aggregate more than 50 per cent of the voting shares or rights of the target.

4.2.3 Partial offer

An acquirer who has not incurred an obligation to make a mandatory offer is also allowed to make a partial offer (ie, a voluntary offer to acquire less than 100 per cent of any class of the voting shares or rights of a target) for the voting shares or rights of a target that is not already owned by the acquirer.

However, an acquirer is not allowed to make a partial offer unless approved by the SC.

4.3 Process overview

4.3.1 Pre-bid due diligence

Generally, due diligence on targets that are listed public companies is limited to information that has been publicly announced by the target, or by public searches, such as company searches at the CCM, or bankruptcy or winding-up searches at the Department of Insolvency.

In a friendly takeover a shareholder of the target company is likely to have initiated discussions with the potential acquirer subject to confidentiality undertakings and entry into non-disclosure or confidentiality agreements that would allow the acquirer and its appointed advisers to conduct due diligence on the target. Where a target company is a listed public company, the scope of the due diligence is limited to information on the target that is publicly announced, as the parties have to be very careful not to allow access to information that will be deemed insider information.

4.3.2 Definitive agreement

The shareholder of the target company and the potential acquirer in a friendly takeover may enter into a definitive sale and purchase agreement for the acquisition of a specific block of shares in the target company before the takeover offer is launched. The definitive agreement typically includes provisions such as the purchase consideration, undertakings or covenants, conditions precedent and termination rights.

In the event that the sale and purchase of the shares pursuant to the definitive agreement involves the acquisition of more than 33 per cent of the target or triggers the creeping provision, the acquirer would be under the obligation to extend a mandatory offer to acquire all the shares of a target that is not already owned by the acquirer and any PAC.

4.4 Related party transactions

If the potential seller or potential acquirer of the shares is a listed public company or a subsidiary of a public company listed on the Main Market of Bursa the transaction will be a related party transaction and the prior approval of the shareholders (of the listed company) in a general meeting will be required where the transaction has a percentage ratio of five per cent[1] or more.

Where any one of the percentage ratios of a related party transaction is 0.25 per cent or more, such a related party transaction must be announced to Bursa as soon as possible after the terms of the transaction have been agreed, unless, inter alia, the value of the consideration of the transaction is less than MYR 500,000.

A related party includes a person who is or was a director or major shareholder of the listed public company, or persons connected with such director or major shareholder, within the preceding six months of the date on which the terms of the transaction were agreed.

4.5 Takeover process

An acquirer who intends to make a takeover offer is required to make an immediate announcement regarding the takeover offer by way of a press notice and send a written notice to the board of the target or adviser designated by the board of the target. The notice is also to be sent to the Securities Commission and Bursa if the acquirer or the target is listed in Malaysia.[2]

The board of the target upon receiving a written notice make an immediate announcement of the receipt of the written notice and dispatch a copy to all shareholders of the target within seven days.

Within 21 days from sending the written notice, the acquirer is required to dispatch the offer documents (upon clearance by the Securities Commission) to the board and shareholders of the target.

Within ten days from the dispatch of the offer documents, the board of the target is required to issue its comments, opinion and views on the takeover offer in a board circular to the shareholders of the target. The independent adviser appointed is also required to issue an independent advice circular to the board and shareholders of the target.

The acquirer must keep the offer open for at least 21 days from the dispatch of the offer documents (unless the Securities Commission has granted approval for an extended period, in which case the offer must be kept open until the end of the extended offer period).

Unless prior written consent of the Securities Commission has been obtained, the board of the target shall not announce material information relating to trading results, profit or dividend forecasts, or asset valuations until after the 39th day following the dispatch of the offer documents.

The acceptance condition to the takeover offer must be met (ie, the acquirer holding in aggregate more than 50 per cent of the voting shares or rights of the target) within 60 days from the dispatch of the offer documents.

4.6 Reporting obligations

Each substantial shareholder of the target is also required to comply with disclosure requirements on a substantial shareholding as set out in the Companies Act 2016.

A substantial shareholder of the target is required to notify the target of its interest or change in its interest in voting shares in the target. Persons ceasing to be a substantial shareholder are also required to notify the target. A copy of such a notice shall also be served to the CCM on the day on which such a person gives notice.

Chapter 5: Foreign investment

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5.1 Foreign investment control/restriction

Over the years, foreign equity restrictions in many sectors across Malaysia have been liberalised. For instance, in April 2012 the government allowed up to 100 per cent foreign equity participation in various services sectors, such as telecommunications, healthcare and education.[3]

Notwithstanding such liberalisation policies, restrictions on foreign equity ownership remain in place for certain sectors. These restrictions may be imposed through the approval of, or issuance of licence by, the relevant ministries or regulatory bodies in Malaysia. Some of the affected sectors include trading, manufacturing, and oil and gas.

Foreign investors looking to set up business in the trading sector need to be aware of the Guidelines on Foreign Participation in the Distributive Trade Services Malaysia (DTG)[4] issued by the Ministry of Domestic Trade, Co-operatives and Consumerism (MDTCC). The DTG regulates the distributive trade sector and requires proposals for foreign involvement in distributive trade to be approved by MDTCC. While the government has gradually liberalised equity ownership in trading companies, those conducted on a larger scale, such as hypermarkets, must still have at least 30 per cent equity participation by Bumiputera.[5] Further, the DTG prohibits foreign involvement in certain distributive trade businesses, such as mini-markets and convenience stores.

In the manufacturing sector, under the Industrial Co-ordination Act, 1975 of Malaysia, companies intending to carry out manufacturing activities are required to submit an application to the Malaysian Investment Development Authority for a licence,[6] unless it is a manufacturing company with shareholders' funds of less than MYR 2.5m and less than 75 full-time paid employees.[7] Equity shareholding in all manufacturing projects were liberalised effective from 17 June 2003, allowing foreign investors to hold 100 per cent of the equity in all investments in new projects, as well as investments in expansion or diversification projects by existing companies irrespective of the level of exports and type of product or activity.[8] Nevertheless, foreign investors seeking a stake in manufacturing companies that were granted manufacturing licences prior to liberalisation of the equity conditions in 2003 will have to be wary that these manufacturing licences may still have equity conditions attached to them. Therefore, their investments may be affected unless the manufacturing company applies for, and is granted, a waiver of the equity conditions that were imposed prior to 17 June 2003.

The Petroleum Development Act, 1974 and the Petroleum Regulations, 1974 are the main legislation governing petroleum activities and operations in Malaysia. Any person wishing to participate in the upstream sector of the oil and gas industry must obtain a licence from Petroliam Nasional Berhad (PETRONAS),[9] which has been vested with the ownership and control of petroleum resources in Malaysia.[10] Foreign companies wanting to participate in exploration operations are required to enter into production sharing contracts with PETRONAS, which will contain the requirements imposed by PETRONAS. Further, no person other than PETRONAS may carry out business in the downstream sector unless the Prime Minister and Ministry of International Trade and Industry have given permission.[11][12]

There are also foreign restrictions on the acquisition of property in Malaysia. There are certain properties that are off-limits to foreigners:

- property valued at less than MYR 1m per unit;
- residential units under the category of low and low-medium cost;
- properties built on Malay reserved land; and
- properties allocated to Bumiputera interest in any property development project.

Further, there is a minimum threshold for foreigners to acquire property in Malaysia, which varies in different states or zones/areas across the states. For instance, the minimum threshold in Kuala Lumpur is MYR 1m, whereas in Kuala Selangor in the state of Selangor, the threshold is a minimum of MYR 2m for residential property and MYR 3m for commercial and industrial property.

5.2 Foreign exchange control

Pursuant to the Foreign Exchange Administration (FEA) administered by the Central Bank of Malaysia (Bank Negara Malaysia – BNM), generally non-resident investors are free to:

- undertake any type of investment in ringgit assets or foreign currency assets in Malaysia (direct or portfolio investment) without any restriction;
- open a ringgit account or foreign currency account with a licensed onshore bank; funds are free to be remitted into and out of such accounts, subject to normal due diligence processes by a licensed onshore bank; and
- repatriate divestment proceeds, profits, dividends or any income arising from investments in Malaysia, provided that repatriation is made in a foreign currency.

Non-resident investors also have the flexibility to hedge foreign exchange exposure arising from their investments in Malaysia, either via a licensed onshore bank or an Appointed Overseas Office (AOO). Further details on AOOs is available on the BNM website on www.bnm.gov.my/documents/aoo/FAQ%20on%20AOO.pdf. Further information in respect of the FEA rules applicable to non-residents is also available on www.bnm.gov.my/index.php?lang=en&ch=fea&pg=en_fea_overview&ac=100.

5.3 Applicable tax incentive or grants

Malaysia offers a wide range of tax incentives designed to attract foreign investment. These incentives are applicable to, among others, the manufacturing, agricultural, tourism and approved services sectors, including R&D, training and environmental protection.

Direct tax incentives grant partial or total relief from income tax for a specified period, while indirect tax incentives come in the form of exemptions from import or export duty, sales tax and excise duties.

The key tax incentives available in Malaysia are pioneer status, investment tax allowance and reinvestment allowance. There are also ‘special pre-packaged’ incentives covering a number of areas of direct and indirect tax and regional economic corridors.

Other available tax incentives include double deduction of certain expenses, R&D incentives, industrial building allowance, principal hub incentive, incentives in the Labuan international business and financial centre, and tariff-related incentives, such as exemption from import duty on machinery, equipment or raw materials.

Chapter 6: Restructuring and insolvency

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6.1 Main legislation and processes

The main legislation governing corporate restructuring and insolvency is the Companies Act, 2016, while individual bankruptcy is governed by the Insolvency Act, 1967. The main corporate restructuring and insolvency processes are corporate voluntary arrangement (CVA), judicial management (JM), schemes of arrangement, receivership and winding up. The first two processes are new statutory mechanisms that came into force on 1 March 2018. The procedural implementation of these mechanisms is governed by the Companies (Corporate Rescue Mechanism) Rules, 2018.

6.2 Corporate voluntary arrangements

The CVA is modelled on the company voluntary arrangement under the UK Insolvency Act, 1986. It is meant to be a quick and cheap restructuring process with little court intervention. As the CVA cannot be applied to public listed companies or companies with charges over its assets or undertakings, its application is limited to private companies with no secured debts.

The CVA is proposed by the directors of a company (which is not under JM and not being wound up) to the company and its unsecured creditors. No court sanction is required for a voluntary arrangement, even after it has been approved by the requisite majority of creditors and members. There is also no requirement to separate creditors into separate classes for the purpose of approving a voluntary arrangement.

A qualified insolvency practitioner is appointed as a nominee to assess the viability and prospect of success of the proposed CVA. He/she has to issue a statement with his/her opinion on whether the proposed arrangement has a reasonable prospect of being approved and implemented; whether the company is likely to have sufficient funds available during the proposed moratorium to enable the company to carry on its business; and that meetings of the company and its creditors should be summoned to consider the proposed CVA.

Upon the filing of a CVA application, a statutory moratorium of 28 days commences (subject to a further extension of 60 days). During this period, no proceedings may be taken by creditors against the company.

Once the requisite majority approval of the creditors (75 per cent of the total value of creditors present and voting at a meeting) and members (simple majority approval of 51 per cent) is obtained, the CVA will be implemented by a supervisor (who is normally the nominee). All parties will be bound by the voluntary arrangement, including non-consenting creditors.

There is no recourse under the Companies Act for aggrieved parties to challenge the proposal/arrangement or outcome of the creditors' meetings. There is, however, provision to challenge the act, omission or decision of the supervisor by way of an appeal to the court.

6.3 Judicial management

A company (via its members or board of directors) and its creditors (including contingent or prospective creditors) may apply to the court to appoint a qualified insolvency practitioner as a judicial manager of the company. The court must be satisfied that the company is or will be unable to pay its debts, and that the making of a JM order is likely to achieve one or more of the three statutory purposes: the company may survive; there may be a compromise or arrangement reached under section 366 of the Companies Act; or it would result in a more advantageous realisation of the company assets than on a winding up. Like a CVA, JM cannot be applied to public listed companies. However, JM is more popular than a CVA as it allows the arrangement of secured debts.

Upon the filing of a JM application, a statutory moratorium commences. During this period, no proceedings may be taken by creditors against the company. Only a debenture holder or a secured creditor may appear and oppose the application for JM, while an unsecured creditor may arguably be heard on the nomination of the proposed judicial manager. Once a judicial manager is appointed, the director's power to manage the company is largely stripped and placed in the hands of the judicial manager. If the company is in receivership, the receiver and manager must vacate the office, and if there is any pending winding up petition against the company, the same shall be dismissed. The judicial manager has wide powers, including the power to take control of assets, deal with and dispose of assets (including charged assets, subject to court approval), enter into new contracts, and summon persons to appear and produce documents relating to the company.

The judicial manager needs to come up with a rescue proposal within the first two months of his/her appointment, and the proposal needs to be approved by at least 75 per cent of the total value of creditors present at a meeting and voting.

Once approved, the judicial manager will submit the plan for sanction by the court. The plan will be implemented by the judicial manager and binding on all creditors, including the non-consenting creditors. The JM order remains in force for six months, and can be extended on the application of the judicial manager for another six months.

6.4 Scheme of arrangement

A scheme of arrangement (or compromise) is another corporate rescue mechanism. It can be adopted by a company that is not insolvent, but is facing financial difficulties. It is commonly used to alter the rights of creditors, reorganise the share capital of the company, or to undertake a reconstruction or merger involving the company.

The advantage of this process is that it enables the company to continue with its daily operations, even during times of financial distress, and the directors continue to be in control of the company.

A scheme of arrangement can be agreed by contract between the company and its creditors without any court intervention. Generally, there are two types of contractual schemes:

- a moratorium scheme of arrangement, where the creditors agree to restructure the debt by the postponement of payment, and the creditors will eventually be paid in full; and
- a compromise scheme of arrangement, where the creditors agree to a full settlement of their debts by accepting a reduced/discounted amount in cash or, sometimes, a share swap.

As contractual schemes are only binding on creditors who have consented to the same, the other non-consenting creditors are still free to pursue their remedies against the company.

In order to bind all creditors to a scheme of arrangement, an application may be made to the court for a statutory scheme of arrangement or compromise under the Companies Act (commonly known as a 'Section 366 Scheme'). The application for a Section 366 Scheme may be made by the company, any creditor or member of the company, a liquidator or a judicial manager. It is normal for such an application to include a request for an order to restrain all proceedings against the company pending the approval of the scheme. Such a restraining order may be granted for not more than three months, and may be extended for not more than nine months by way of application to the court.

The court may appoint an approved liquidator to assess and report to the court on the viability of the proposed scheme. The majority of 75 per cent in value of the creditors or class of creditors present and voting is required to approve the proposed scheme. Once approved and a court sanction is given, the scheme will be binding on all parties, including the non-consenting creditors.

6.5 Receivership

A receiver may be appointed privately by a creditor (debenture holder) or by the court.

6.5.1 Private receiver

A private appointment is governed by the terms of the instrument creating the charge. Such an instrument is usually a debenture, often created by a company as a loan security in favour of a financial institution. It is usual for a debenture to provide for the appointment of not only a receiver but also a manager with the power to manage the charged assets. The scope of the debenture is critical, as the receiver/manager is only empowered to take control of assets that are charged under the debenture (either by way of a fixed charge or floating charge). There is a statutory presumption that the receiver/manager acts as the agent of the company, unless the instrument of appointment expressly provides otherwise. The receiver/manager seeks the best means of recovering for the debenture holder, without the need seriously to consider the benefits to the chargor.

6.5.2 Court-appointed receiver

The court may appoint a receiver/manager under the following circumstances:

- the company has defaulted in its payment or obligations to a debenture holder;
- the company proposes to sell or otherwise dispose of the secured property in breach of the terms of any instrument creating the security or charge;
- it is necessary to preserve the secured property for the benefit of the debenture holder; or
- it is necessary to preserve the property of a company pending the disposal of a suit, where there is a good *prima facie* claim of title by the applicant and evidence that the property is in jeopardy.

A court-appointed receiver/manager is an officer of the court, and not an agent of the company.

6.5.3 Power and duties of a receiver

In addition to the powers conferred either under a debenture or by a court order, a receiver shall have the powers set out in the sixth schedule of the Companies Act, which includes, among others, the power to take possession and control of the property in accordance to the terms of that order, grant options over the property, carry on the business of the company, demand and recover income of the property in receivership and exercise the right to inspect books or documents that relate to the property in receivership.

6.6 Winding up

There are two types of winding up process: compulsory winding up and voluntary winding up.

6.6.1 Compulsory winding up

The company, its contributory and any creditor (including a contingent or prospective creditor) of a company may petition for the company to be wound up by the court. The commencement of winding up shall be at the date of the winding up order. Section 465(1) of the Companies Act stipulates 12 situations where the court may order a company to be wound up. The most common situation is where the company is unable to pay its debts. A company is deemed unable to pay its debt when it is indebted in a sum exceeding MYR 10,000 and fails to pay the same within 21 days on receipt of a written demand for payment; when an execution or other process issued on a judgment, decree or order of any court in favour of a creditor of the company is returned unsatisfied in whole or in part; or it is proved to the satisfaction of the court that the company is unable to pay its debt after taking into account the contingent and prospective liabilities of the company.

6.6.2 Voluntary winding up

A company may also be wound up voluntarily by its directors and shareholders or creditors. The court is generally not involved in the process. A voluntary winding up shall commence where an interim liquidator has been appointed before the resolution for voluntary winding up is passed and, in any other case, at the time of the passing of the resolution for voluntary winding up.

There are two types of voluntary winding up:

- Members' voluntary winding up: The directors and shareholders of a company may agree for a resolution to be passed to wind up the company, even when the company is solvent. The directors must make a declaration of solvency by confirming that the company will be able to pay its debts in full within 12 months after the initiation of the winding up process. During this process, the assets of the company are sold, liabilities paid and the balance assets distributed among the members. If it is subsequently discovered that the company is insolvent, the members' voluntary winding up is converted into a creditors' winding up.
- Creditors' voluntary winding up: If the directors are unable to make a declaration of solvency, a resolution can still be passed for a creditors' voluntary winding up, whereby the creditors will be involved in charting the course of the liquidation.

6.6.3 Effect of winding up

Once a winding up process has commenced, there shall be no disposition of property of the company other than an exempt disposition, including any transfer of shares or alteration in the status of the members of the company, except with the approval of the court.

Unless a private liquidator (often an accountant holding a liquidator's licence) is appointed, the official receiver will by default be appointed as the liquidator of the wound-up company. The wound-up company continues to exist as a legal entity under the management of the liquidator.

The liquidator's duties include managing the assets of the company, ascertaining its liabilities, investigating the internal affairs of the company, realising the assets, making the appropriate distribution to parties entitled to the assets and applying for the dissolution of the company when the winding up process comes to an end.

6.7 Personal bankruptcy

The statutory threshold for the commencement of bankruptcy proceedings against an individual debtor is a judgment debt of a minimum of MYR 50,000. On the making of a bankruptcy order, all the bankrupt's assets shall vest in the Directors General of Insolvency.

Pursuant to recent amendments to the Insolvency Act, 1967, a debtor may propose a voluntary arrangement to his/her creditors any time before he/she is adjudged bankrupt. A debtor who intends to propose a voluntary arrangement shall appoint a nominee to act in relation to the voluntary arrangement or for the purpose of supervising the implementation of the voluntary arrangement.

Chapter 7: Employment, industrial relations, and work health and safety

Selvamalar Alagaratnam, Skrine, Kuala Lumpur

7.1 Employees' rights and protection

Employee's rights and other statutory protection for employees in Malaysia depend on several statutes.

The Employment Act, 1955 (EA) applies to employees in West Malaysia who earn a monthly salary of MYR 2,000 and below. They are employed:

- as manual labourers or supervisors of manual labourers;
- to operate or maintain any mechanically propelled vehicle for the purpose of transporting passengers or goods or for reward or commercial purposes;
- as a domestic servant; or
- in certain positions on seagoing vessels;

The Employment Act for minimum terms and conditions of employment, such as wage and hours, and several leaves, which may not be contractually waived.

The states of Sabah and Sarawak in East Malaysia have equivalent legislation (with some differing provisions) that cover similar categories of employees.

7.1.1 Working hours and leave

Employees who come within the scope of the EA ('EA employees') are entitled to protection in terms of maximum hours of work. No EA employee may be required to work more than eight hours a day or more than 48 hours a week, or more than five consecutive hours without a break of at least 30 minutes. Every EA employee is entitled to one whole day of rest each week (rest day).

EA employees are also entitled to paid sick leave, annual leave and public holidays

Sick leave

Sick leave is as follows:

- 14 days in each calendar year if he or she has been in employment for a period of less than two years;
- 18 days in each calendar year if he or she has been in employment for a period of two years or more but less than five years; and
- 22 days in each calendar year if he or she has been in employment for a period of five years or more.

If hospitalisation is necessary, an EA employee is entitled to sick leave of 60 days in each calendar year, provided the total number of days of paid sick leave in a calendar year to which the employee is entitled does not exceed 60 days in aggregate.

Annual leave

Annual leave is as follows:

- eight days for every 12 months of continuous service if he or she has been in employment for a period of less than two years;
- 12 days for every 12 months of continuous service if he or she has been in employment for a period of two years or more but less than five years; and
- 16 days for every 12 months of continuous service if he or she has been in employment for a period five years or more.

Public holidays

There are 11 paid gazetted holidays, five of which must be:

- the National Day (31 August);
- the birthday of the King (Malaysia's monarch and head of state) (the first Saturday of every June);
- the birthday of the ruler of the state (differs from state to state) or the federal territory (1 February) in which the employee wholly or mainly works;
- Workers' Day (1 May); and
- Malaysia Day (16 September).

If an EA employee works in excess of p hours, he or she is entitled to overtime pay, which is calculated as follows:

- for any overtime work carried out in excess of normal hours of work, at a rate that is not less than 1.5 times the hourly rate of pay;
- for work on a rest day:
  - for any period of work that does not exceed half the normal hours of work, wages equivalent to 0.5 times the ordinary rate of pay for work done on that day; and
  - for any period of work that is more than half but that does not exceed the normal hours of work, one day's wages at the ordinary rate of pay for work done on that day;
- for any work carried out in excess of the normal hours of work at a rate that is not less than two times the hourly rate of pay; and
- for work on a public holiday, in addition to the day's wages, two days' wages at the ordinary rate of pay, regardless of whether the period of work done on that day is less than the normal hours of work, and for work in excess of the normal hours of work, at a rate that is not less than three times the hourly rate of pay.

Notwithstanding the payment of overtime pay, no EA employee may be required to work more than 12 hours a day or in excess of 104 hours of overtime in any one month.

Employees who are not covered by the EA ('non-EA employees') do not have any rights to sick leave, annual leave or paid public holidays. Neither do they have any limitations or restrictions on their hours of work and are entitled to overtime pay. Their rights in these matters are subject to contract.

All female employees (including non-EA employees) are entitled to paid maternity leave of no less than 60 consecutive days. This entitlement is limited to employees who have been in employment for no less than 90 days in the nine-month period immediately preceding confinement, which must include employment in the four months immediately preceding confinement. An employee is also not entitled to paid maternity leave if she has five or more surviving children.

7.1.2 Termination

All employees in Malaysia, regardless of salary or nationality, enjoy protection against unjust dismissal. Pursuant to the Industrial Relations Act, 1967 (IRA), an employee may only be terminated for just cause or excuse. 'Just cause or excuse' is not defined by the IRA or any other legislation. Generally, misconduct, poor performance and redundancy are accepted as just cause for termination.

Where termination is on the ground of redundancy, termination or retrenchment benefit is payable. Case law dictates that if the financial position of the employer permits it, and especially if the retrenchment exercise is carried out with the aim of increasing efficiency and profits, fair and reasonable benefits should be made available. Currently, one month's salary for each year of service is considered fair and reasonable.

EA employees are entitled to minimum termination benefits as follows and pro rata in respect of an incomplete year of service, calculated to the nearest month:

- ten days' wages for every year of employment if he or she has been employed for a period of less than two years;
- 15 days' wages for every year of employment if he or she has been employed for a period of two years or more but less than five years; and
- 20 days' wages for every year of employment if he or she has been employed for a period of five years or more.

If the EA employee's contract of employment provides for a more favourable termination/retrenchment benefit, he or she is entitled to that contractual benefit.

7.1.3 Retirement

Permanent employees are entitled to the minimum retirement age of 60 years as provided for by the Minimum Retirement Age Act, 2012.

7.1.4 Freedom of association

Every employee has the right to freedom of association. The IRA prohibits any person from interfering with or restraining an employee from forming, assisting in the formation of or joining a trade union.

7.1.5 Safety, health and welfare

Pursuant to the Occupational Safety and Health Act, 1994, employees have a right to safety, health and welfare at work. Employers' duties extend, but are not limited to:

- the provision and maintenance of systems of work that are, so far as is practicable, safe and without risk to health;
- the provision of such information, instruction, training and supervision as is necessary to ensure, so far as is practicable, the safety and health at work of employees;
- so far as is practicable, the maintenance of any place of work in a condition that is safe and without risk to health;
- the provision and maintenance of the means of access to and egress from a place of work that are safe and without such risk; and
- the provision and maintenance of a working environment for employees that is, so far as is practicable, safe, without risk to health and adequate as regards facilities for welfare at work.

7.1.6 Data protection

The Personal Data Protection Act, 2010 (PDPA) gives employees the right to be informed by way of a Personal Data Protection notice (that is to be issued to them in both English and Malay) of the purpose of collection of their personal data, how their personal data will be processed and their rights as data subjects. These rights include the right to access personal data; to correct personal data where it is inaccurate, incomplete, misleading or not up-to-date; and to withdraw consent to the processing of personal data. In certain circumstances, for example, where sensitive personal data is processed or where data is transmitted beyond borders, the employee's explicit consent is required.

7.2 Statutory contributions and minimum wage

Employees' entitlement to statutory contributions and minimum wages are governed by the following legislation outlined below:

7.2.1 Employees Provident Fund Act, 1991

Employees Provident Fund Act, 1991 (EPF) makes it mandatory for all employers and most employees (except for those excluded from the application of the EPF Act) to contribute to a state-managed provident fund at contribution rates that are no less than the rate prescribed by the EPF Act. Contributions by foreign nationals employed in Malaysia and domestic servants are voluntary.

7.2.2 Employees' Social Security Act, 1969

The Employees' Social Security Act, 1969 provides social security for all employees in the event of contingencies, such as employment injuries. The act makes it mandatory for employers and employees to contribute to the fund at the rate prescribed by the act.

7.2.3 Employment Insurance System Act, 2017

The Employment Insurance System Act, 2017 provides certain benefits and a re-employment placement programme for insured persons in the event of the loss of employment, and makes it mandatory for employers and employees to contribute to the fund at the prescribed rate.

7.2.4 Minimum Wages Order, 2020

The Minimum Wages Order, 2020 provides different minimum wage rates payable to an employee, depending on the employee's place of employment. The minimum wage rate payable to an employee who works in a place of employment in any of the 16 City Council areas or the 40 Municipal Council areas specified in the Schedule to the Order is MYR 1,200 per month or MYR 5.77 per hour. The minimum wage rate payable to an employee who works in a place of employment in any areas other than the City Council or Municipal Council areas specified in the Schedule to the Order is MYR 1,100 per month or MYR 5.29 per hour.

7.3 Work permits

There are several types of work permit or visa available to foreign nationals who are gainfully employed in Malaysia. The types of pass issued by the immigration authorities of Malaysia are outlined below:

7.3.1 Short-term social visit pass

Short-term social visit passes are issued at the entry point to foreign citizens for social and business visits, and are usually valid for 30 days or less. The duration is discretionary, but is usually for a period of 30 days. Examples of limited business purposes include attending meetings, conferences, business discussions or seminars; inspecting or setting up factories; auditing a company's accounts; signing agreements; and surveying business opportunities and investment potential.

7.3.2 Professional visit pass

Professional visit passes are issued to foreign citizens who hold acceptable professional qualifications for the purpose of taking up professional work in Malaysia for a Malaysian entity for a short-term period (including extensions) not exceeding 12 months. Applications must be made by the Malaysian entity concerned.

7.3.3 Employment pass

Employment passes are issued to foreign citizens who enter Malaysia to take up paid employment under a contract of service with an employer, referred to as expatriates. The duration of employment passes depends on the nature of employment and the needs of the employer. The maximum period for any employment pass is five years, and the norm is between two and three years.

Applications must be made by the employer, and the requirements below must be met before an application will be considered by the Immigration Department:

- minimum paid-up capital of employer ranging between MYR 250,000 and MYR 1m;
- recommendation from monitoring agencies;
- registration of employer with relevant monitoring agencies;
- minimum monthly salary of at least MYR 3,000;
- the skill, qualification and experience required for the expatriate position must be such that it cannot be fulfilled by local candidates; and
- the expatriate's role must be relevant to the activities of the employer.

7.3.4 Residence Pass–Talent

The Residence Pass–Talent is only available in Peninsular Malaysia and is issued to foreign citizens considered to be high-achieving individuals with the capacity to drive business results that contribute towards the national key economic areas (NKEA). The 12 industries forming the NKEA are Greater Kuala Lumpur/Klang Valley; oil, gas and energy; palm oil; financial services; tourism; business services; communication, content and infrastructure; electronics and electrical; wholesale and retail; education;

healthcare; and agriculture. A high-achieving individual with the capacity to drive business results that contribute towards Malaysia's economic transformation may apply for the Residence Pass–Talent. Applications must be submitted by the foreign citizen online at https://rpt.talentcorp.com.my.

Applications are reviewed against a set of criteria designed to gauge both the applicant's qualifications and economic contributions to the country. The applicant is required to:

- have worked in Malaysia for a minimum period of three continuous years;
- hold a valid employment pass with more than three months' validity at the time of the application;
- hold a PhD, master's degree, bachelor's degree or diploma in any discipline from a recognised university, or a professional or competency certificate from a recognised professional institute;
- hold a Malaysian income tax file number and have paid income tax for at least two years;
- possess five years of total work experience; and
- earn a basic salary of MYR 15,000 per month.

7.3.5 Visit pass (temporary employment)

These passes are issued for the employment of foreign nationals as semi-skilled, unskilled or domestic helpers, from specific source countries in certain sectors of the economy, such as agriculture, construction, manufacturing, plantation and various types of services.

Different procedures for the recruitment of foreign workers are applicable to employers in Peninsular Malaysia, Sabah, Sarawak and the Federal Territory of Labuan.

Chapter 8: Tax

Preetha Pillai, Skrine, Kuala Lumpur

8.1 Taxes applicable to individuals

8.1.1 Tax resident employees

Individual income tax is payable by tax resident employees at rates of between zero and 30 per cent (effective from the year of assessment 2020) on gross income in respect of gains and profits from employment exercised in Malaysia (after deducting personal relief and tax rebates).

The tax is deducted from the employee's salary and remitted to the tax authorities by the employer under the Monthly Tax Deduction (MTD) scheme. Under the MTD scheme, the employer must deduct and remit stipulated amounts of tax from the employee's emoluments to the Inland Revenue Board on a monthly basis. The amount to be deducted varies depending on multiple factors including, among others, the employee's residence status, marital status, contribution to retirement funds and number of dependents: see Income Tax (Deduction from Remuneration Rules), 1994.

Employees who have been subject to MTD and who fulfil the criteria of MTD as final tax are exempt from filing income tax returns. They can elect for the MTD as their final tax payment.

8.1.2 Non-tax resident employees

Non-tax resident employees do not qualify for tax relief or rebates and must pay tax at 30 per cent of their Malaysian source income.

For gains and profits from employment exercised in Malaysia, tax is deducted from the employee's salary and remitted to the tax authorities by the employer under the MTD scheme. Non-tax resident employees who exercise employment in Malaysia for a period or periods that together do not exceed 60 days in a calendar year are exempt from tax. However, the income of a non-resident individual who is a public entertainer is not exempt from tax.

8.2 Taxes applicable to businesses

8.2.1 Corporate income tax

Companies, limited liability partnerships and business trusts are subject to a 24 per cent income tax rate. Income of any person, other than a resident company carrying on the business of banking, insurance, or sea or air transport, for the basis year for a year of assessment derived from sources outside Malaysia and received in Malaysia, is exempt from tax.

From the year of assessment 2020 onwards, tax resident companies and limited liability partnerships with a paid up capital/capital contribution of MYR 2.5m and below (and which are not controlled by or do no not directly or indirectly control another company with a paid up capital of more than MYR 2.5m, and have a gross business income of less than MYR 50m) are subject to 17 per cent for the first MYR 600,000 of chargeable income. Any subsequent chargeable income will be taxed at 24 per cent.

Effective from 2008, Malaysia has implemented the single-tier system. Under the single-tier system, the tax on a company's chargeable income is the final tax and the dividends received in the hands of the shareholders is tax exempt. There is no WHT on Malaysian dividends.

8.2.2 Sales tax

Sales tax is a single-stage tax levied on goods manufactured and sold, used or disposed of in Malaysia by a registered manufacturer or imported into Malaysia by any person. Sales tax rates differ between five and ten per cent, depending on the group of taxable goods. There are specific sales tax rates applicable on other taxable goods, such as petroleum products.

8.2.3 Service tax

Service tax is charged and levied on taxable services provided in Malaysia by a registered person in the carrying on of his/her business at the rate of six per cent. However, an exemption of service tax is available for intra-group services.

8.3 Other taxes

8.3.1 Stamp duty

Stamp duty is imposed on certain instruments and documents under the Stamp Act, 1949. The rate of stamp duty depends on the nature of the instrument involved and varies from a fixed charge, *ad valorem* or a certain percentage of the value of the subject matter of the transaction.

8.3.2 Digital service tax

Digital service tax at the rate of six per cent is imposed on any foreign service provider who provides any digital service delivered or subscribed over the internet or other electronic network, which cannot be obtained without the use of IT and where delivery of service is essentially automated.

8.3.3 Excise duty

Excise duty is levied on selected Malaysian manufactured products and selected imported goods, such as cigarettes and motor vehicles. Excise duty rates range from five to 105 per cent, depending on the category of the product.

8.3.4 Capital gains

Malaysia does not impose tax on capital gains, save for gains on disposal of real property and shares in a real property company, which are chargeable to tax under the Real Property Gains Tax Act, 1976 at a rate (for a company) between 30 per cent for a disposal within the first three years of acquisition, and ten per cent for disposals in the sixth or subsequent years.

8.3.5 Customs duties

Customs duties (including import duty and export duty) are imposed under the Customs Act, 1967. The rates, and any applicable exemptions, are set by subsidiary legislation made under the act and depend on the type of goods imported or exported. Most goods are subject to import duties ranging from zero to 60 per cent. Higher rates apply to luxury goods, automobiles, tobacco, alcoholic beverages, and processed and high-value food products.

8.3.6 Withholding tax

When a payer who is a tax resident in Malaysia makes a payment to a payee who is a non-resident in Malaysia for a service rendered in Malaysia, the payer is required to withhold an amount according to the prescribed rate (varying between five and 25 per cent, depending on the nature of the payment and subject to the double taxation agreement) and remit the same to the Inland Revenue Board of Malaysia within the stipulated period.

Chapter 9: Intellectual property

Charmayne Ong, Skrine, Kuala Lumpur

9.1 Patents

The Patents Act, 1983 and Patents Regulation, 1986 provide for the law on the patentability, rights, ownership, infringement and offences relating to patents. An invention is patentable if it:

- is new;
- involves an inventive step;
- is industrially applicable; and
- does not fall into any non-patentable invention category, such as discoveries, scientific theories, mathematical methods, plant or animal varieties, or essentially biological processes for the product of plants or animals, schemes, and rules or methods for doing business.

An application for a grant of a patent can be filed with the Intellectual Property Corporation of Malaysia (MyIPO). As Malaysia has also acceded to the PCT, PCT applications can also be filed through MyIPO.

The duration of a patent shall be 20 years from the filing date of the application. However, where a patent application was filed before 1 August 2001, and was pending on that date, the duration of the patent granted on that application shall be 20 years from the date of filing or 15 years from the date of grant, whichever is longer. The duration of a patent granted before 1 August 2001 and still in force on that date shall be 20 years from the date of filing or 15 years from the date of grant, whichever is longer. Patent applications derived from PCT applications are protected for a maximum of 20 years from the international PCT filing date.

The owner of a patent has exclusive rights to exploit the patented invention, assign or transmit the patent and conclude licence contracts. The owner of a patent shall have the right to institute court proceedings against any person who has infringed or is infringing the patent by performing any act exploiting the owner’s rights in the patent without the owner’s agreement. The owner of the patent may obtain remedies, such as damages, an account of profits or injunctions.

Utility innovations are also protected under the Patents Act, 1983, and require the same elements as patents, except for the requirement of an inventive step. The duration of protection for a utility innovation is an initial term of ten years, which can be extended for two additional periods of five years each.

9.2 Trademarks

The Trademarks Act, 2019 and Trademarks Regulations, 2019 provide for the law on the use, registrability, duration, ownership, infringement and offences relating to trademarks.

A trademark means any sign capable of being represented graphically that is capable of distinguishing goods or services of one undertaking from those of other undertakings. A sign includes any letter, word, name, signature, numeral, device, brand, heading, label, ticket or shape of goods or their packaging, colour, sound, scent, hologram, positioning, sequence or motion, or any combination thereof.

Any person claiming to be a bona fide proprietor of a trademark may apply for the registration of the trademark if the person is using or intends to use the trademark, or has authorised or intends to authorise another to use the trademark in the course of trade. A trademark cannot be registered if:

- it is not capable of being represented graphically;
- it is not capable of distinguishing goods or services of one undertaking from those of other undertakings;
- it is not distinctive;
- it consists exclusively of signs or indications that may serve to designate the kind, quality, quantity, intended purpose, value, geographical origin or other characteristics of goods or services;
- it consists exclusively of signs or indications that have become customary in the current language of the territory or in the bona fide and established practices of the trade;
- it consists exclusively of the name of a country; or
- it contains or consists of recognised geographical indications.

Applications for registrations of a trademark must be made to MyIPO. Malaysia has acceded to the Madrid Protocol; thus, trademark owners may also obtain protection abroad by filing one international application through MyIPO.

The duration of protection is for ten years from the date of registration. This can be extended for additional ten year periods upon subsequent payment of renewal fees.

The registered proprietor of a trademark has the exclusive rights to use the trademark and authorise others to use the trademark in relation to the goods or services for which the trademark is registered. A registered proprietor of a trademark can also institute court proceedings against infringers for the infringement of a trademark. In enforcing trademark rights, the registered proprietor can seek remedies, such as damages, an account of profits in lieu of damages, injunctions and additional damages.

9.3 Copyright

The Copyright Act, 1987 provides for the law on the subsistence, duration, ownership, infringement and offences relating to copyright.

The following works are eligible for copyright:

- literary works;
- musical works;
- artistic works;

- films;
- sound recordings; and
- broadcasts.

Derivative works of original works, such as translations, adaptations and arrangements, are eligible for copyright. Copyright protection does not extend to any idea, procedure, method of operation or mathematical concept.

In order for copyright to subsist, it must be shown that sufficient effort has been expended to make the work original in character, the work has been reduced to a material form and the author is a qualified person and that the work was first published in Malaysia. There is no registration requirement. There is a voluntary notification of copyright mechanism; however, failure to notify does not mean that copyright does not subsist in the said work. First ownership will vest with the author unless:

- the work is commissioned, in which case ownership will be deemed to be transferred to the person who commissioned the work; or
- the work was made in the course of the author's employment, in which case ownership will be deemed to be transferred to the author's employer.

The duration of protection for literary, musical or artistic works is for the life of the author plus 50 years. The duration for protection for published editions, films, sound recordings, broadcasts and performances is for 50 years from the beginning of the calendar year after which the work was first published or performed.

The rights conferred by copyright are the exclusive right to control the reproduction in any material form; communication to the public; performance, showing or playing to the public; distribution of copies to the public by sale or other transfer of ownership; and commercial rental to the public. The owner of a work that is protected by copyright can institute civil proceedings against any person who infringes the copyright, and seek remedies, such as damages, account of profits in lieu of damages, statutory damages or injunctions.

9.4 Designs

The Industrial Designs Act, 1996 provides for the registration, duration, ownership, infringement and offences relating to industrial designs.

Industrial design means the features of shape, configuration, pattern or ornament applied to an article by any industrial process or means, being features which in the finished article appeal to and are judged aesthetically. Industrial design does not include a method or principle of construction, or features of shape or configuration that are dictated solely by the function that the article has to perform or are dependent on the appearance of another article of which the article is intended by the author of the design to form an integral part. The author of an industrial design shall be treated as the original owner of the industrial design unless:

- the industrial design is commissioned, in which case the person commissioning the industrial design shall be treated as the original owner of the industrial design; and

- the industrial design is created by an employee in the course of employment, in which case the employer shall be treated as the original owner of the industrial design.

The owner of an industrial design is entitled to make an application for the registration of the industrial design. An industrial design shall not be registered unless it is new. An application to register an industrial design must be made to MyIPO.

The duration of protection is five years from the date of filing. The period of registration of an industrial design may be extended for four further consecutive terms of five years each.

The owner of a registered industrial design shall have the right to institute legal proceedings against any person who has infringed or is infringing any of the rights conferred by the registration of the industrial design to obtain remedies, such as damages, account of profits in lieu of damages or injunctions.

9.5 Other

9.5.1 Geographical Indications Act, 2000

The Geographical Indications Act, 2000 protects geographical indications. Geographical indication means an indication that identifies any goods as originating in a country or territory, or a region or locality in that country or territory, where a given quality, reputation or other characteristic of the goods is essentially attributable to their geographical origin. An application for the registration of a geographical indication can be made; however, protection will be given to a geographical indication regardless of whether or not the geographical indication is registered.

9.5.2 Layout-Designs of Integrated Circuits Act, 2000

The Layout-Designs of Integrated Circuits Act, 2000 protects the layout of integrated circuits. Layout-design means the three-dimensional disposition, however expressed, of the elements of an integrated circuit and some or all of the interconnections of the integrated circuit, or such a three-dimensional disposition prepared for an integrated circuit intended for manufacture.

9.5.3 Protection of New Plant Varieties Act, 2004

The Protection of New Plant Varieties Act, 2004 provides for the protection of the rights of breeders of new plant varieties. An application for the registration of a new plant variety and a grant of a breeder's right can be made to the Plant Varieties Board.

Chapter 10: Financing

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10.1 Licencing requirements for banks

Malaysia has a dual banking system, where the conventional banking system operates side-by-side with the Islamic banking system. The key statute governing the conventional banking industry is the Financial Services Act, 2013 (FSA), whereas the Islamic Financial Services Act, 2013 (IFSA) governs the Islamic banking industry. The regulator of banks licensed under the FSA and IFSA is Bank Negara Malaysia (BLM). BNM has broad powers of supervision and control over banking institutions licensed under the FSA and the IFSA. BNM has also issued various guidelines, standards and directives relating to, among others, prudential matters applicable to banking institutions, including standards relating to capital adequacy, liquidity, corporate governance, risk management and related party transactions.

A bank may be licensed under the FSA as a commercial bank or investment bank. Investment banks that undertake capital market activities in addition to banking activities are also regulated by the Securities Commission and are licensed to carry on business in dealing in securities under the CMSA. BNM and the Securities Commission work hand-in-hand to regulate investment banks and have both issued guidelines regulating investment banks.

BNM also regulates development financial institutions prescribed under the Development Financial Institutions Act, 2002 to promote the industrialisation of important sectors of the Malaysian economy.

The FSA regulates, among others, licensed business. Licensed businesses are businesses licensed by the Minister, on the recommendation of BNM under section 10 of the FSA. Licensed business includes the following activities with the following definitions under subsection 2(1) of the FSA:

1. banking business, which means
   '(a) the business of— (i) accepting deposits on current account, deposit account, savings account or other similar account; (ii) paying or collecting cheques drawn by or paid in by customers; and (iii) provision of finance; and (b) such other business as prescribed under section 3 [of the FSA]';

2. insurance business;

3. investment banking business, which means '(a) the business of— (i) accepting deposits on deposit account; and (ii) provision of finance; Act 671; (b) any regulated activity carried on pursuant to a Capital Page 18 of 180 Markets Services licence under the Capital Markets and Services Act 2007; and (c) such other business as prescribed under section 3 [of the FSA]'.

An applicant for a commercial banking licence, investment banking licence or Islamic banking licence under the FSA or IFSA must be a public company incorporated under the Companies Act, 2016.

A Labuan company may carry on business in Labuan as a Labuan bank licensed under the Labuan Financial Services and Securities Act, 2010 (LFSSA) or the Labuan Islamic Financial Services and

Securities Act, 2010 (LIFSSA). The Labuan banks are subject to the regulation and supervision of the Labuan Financial Services Authority (the 'Labuan FSA').

The LFSSA regulates, among others:

1. Labuan banking business, which means:

   '(a) the business of receiving deposits on current account, deposit account, savings account or any other account as may be specified by the [the Labuan FSA]; (b) Labuan investment banking business; (c) Labuan financial business (d) Labuan Islamic banking business; (e) such other business as the [Labuan FSA], with the approval of the Minister, may specify, in any currency (including ringgit where permitted by the Exchange Control Act 1953 or such other relevant law in force)';[13] and

2. Labuan investment banking business, which means:

   '(a) the business of providing credit facilities; (b) the business of providing consultancy and advisory services relating to corporate and investment matters, including dealing in securities, or making and managing investments on behalf of any person; (c) the business of undertaking foreign exchange transactions, interest rate swaps, dealings in derivative instruments or derivative financial instruments or any other similar risk management activities; (d) Labuan Islamic investment banking business; (e) Labuan financial business; or (f) such other business as the [Labuan FSA], with the approval of the Minister, may specify, in any currency (including ringgit where permitted by the Exchange Control Act 1953 or such other relevant law in force)'.[14]

For a person who carries on Labuan banking business, Labuan investment banking business or Labuan financial business to be a Labuan company, a foreign Labuan company (which is a corporation incorporated or registered under the Labuan Companies Act, 1990) or a Malaysian bank, he/she must hold a valid licence to carry on such business.[15]

Chapter 11: Privacy laws and data protection

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The PDPA came into force on 15 November 2013. Certain industries, for instance, financial institutions and private hospitals, are subject to industry-specific secrecy requirements.

The PDPA applies to personal data held, used or to be used in Malaysia (whether recorded/processed manually or electronically), subject to certain exemptions.

Under the PDPA, personal data means any information in respect of commercial transactions, which is:

- processed wholly or partly by means of equipment operating automatically in response to instructions given for that purpose;

13 Sub-s 2(1) of the LFSSA.

14 Sub-s 2(1) of the LFSSA.

15 Sub-s 87(1) of the LFSSA.

- recorded with the intention that it should wholly or partly be processed by means of such equipment; or
- recorded as part of a relevant filing system or with the intention that it should form part of a relevant filing system;

that relates directly or indirectly to a data subject, who is identified or identifiable from that information or from that and other information in the possession of a data user, including any sensitive personal data and expression of opinion about the data subject.

The term 'processing', in the context of personal data, has a wide meaning. Under the PDPA, 'processing' means collecting, recording, holding or storing personal data, or carrying out any operation or set of operations on personal data.

11.1 Personal Data Protection Principles

The PDPA stipulates various principles that form the basis of protection of personal data and the free flow of information. The seven principles (the 'Personal Data Protection Principles') and a brief description on each principle are set out below.

11.1.1 General Principle

The General Principle relates to the processing of personal data, including sensitive personal data. A data user shall not process personal data from the data subject unless consent is given. In the case of sensitive personal data, the data user shall not process such personal data unless it is with explicit consent or under very limited circumstances. This principle also states that the collection of data must be lawful, purpose-related and not excessive in nature.

11.1.2 Notice and Choice Principle

Under the Notice and Choice Principle, a data user shall, by written notice in the national and English language, inform an individual of eight matters:

1. that personal data of the data subject is being processed by or on behalf of the data user, and shall provide a description of the personal data to that data subject;
2. the purposes for which the personal data is being or is to be collected and further processed;
3. of any information available to the data user as to the source of that personal data;
4. of the data subject's right to request access to and the correction of the personal data and how to contact the data user with any inquiries or complaints in respect of the personal data;
5. of the class of third parties to whom the data user discloses or may disclose the personal data;
6. of the choices and means the data user offers the data subject for limiting the processing of the personal data, including personal data relating to other persons who may be identified from that personal data;

7. whether it is obligatory or voluntary for the data subject to supply the personal data; and
8. where it is obligatory for the data subject to supply the personal data, the consequences for the data subject if he/she fails to supply the personal data.

11.1.3 Disclosure Principle

The Disclosure Principle provides that personal data shall not, without the consent of the data subject, be disclosed for any purpose other than the purpose for which the personal data was to be disclosed at the time of collection of the personal data or a purpose directly related to it, or be disclosed to a third party other than that specified in the notice.

However, this principle is subject to section 39 of the PDPA, which sets out the circumstances where personal data may be disclosed without the consent of the data subject. The exemptions include the following circumstances:

- prevention of crime;
- investigations;
- court orders;
- reasonable belief of such a right to disclosure; and
- public interest.

11.1.4 Security Principle

This principle states that a data user shall, when processing personal data, take practical steps to protect the personal data from any loss, misuse, modification, unauthorised or accidental access or disclosure, alteration or destruction.

This principle is extended further to cover situations where the processing of personal data is carried out by a data processor on behalf of the data user. In such a situation, the data user shall, for the purpose of protecting the personal data from any loss, misuse, modification, unauthorised or accidental access or disclosure, alteration or destruction, ensure that the data processor:

- provides sufficient guarantees in respect of the technical and organisational security measures governing the processing to be carried out; and
- takes reasonable steps to ensure compliance with those measures.

11.1.5 Retention Principle

The Retention Principle provides that personal data processed for any purpose shall not be kept longer than is necessary for the fulfilment of that purpose. This principle mandates that the data user must take reasonable steps to ensure that all personal data is destroyed or permanently deleted if it is no longer required for the purpose for which it was to be processed.

11.1.6 Data Integrity Principle

The Data Integrity Principle specifies that personal data must be accurate, complete, not misleading and kept up-to-date.

11.1.7 Access Principle

The Access Principle provides that a data subject shall be given access to his/her personal data and be able to correct that personal data, except where compliance with a request to such access or correction is refused under the PDPA.

In light of the foregoing, so long as data to be processed falls within the definition of Personal Data, the PDPA applies and the Personal Data Protection Principles outlined above will have to be adhered to.

The processing of data without consent, unless exempt under the PDPA, is prohibited. The PDPA provides that anyone who contravenes the Personal Data Protection Principles commits an offence and shall, on conviction, be liable to a fine not exceeding MYR 300,000 or imprisonment for a term not exceeding two years, or both.

11.2 Offshore transmission and retention of data

The PDPA aims to regulate the flow of personal data outside Malaysia by prohibiting the transfer of personal data to any place outside Malaysia, unless consent to the transfer has been obtained. The PDPA sets out certain exceptions to the requirement of consent, such as where the transfer is necessary for the performance of a contract between the data subject and the data user.

Chapter 12: Competition

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12.1 Legislation and the regulator

Competition law in Malaysia is governed by the Competition Act, 2010 and the relevant competition authority is the Malaysian Competition Commission (MyCC) which has been given wide powers of investigation and enforcement under the Competition Act.

12.2 Anti-competitive agreement

Section 4 of the Competition Act prohibits both horizontal and vertical agreements between enterprises that have the object or effect of significantly preventing, restricting or distorting competition in any market for goods or services (the 'Chapter 1 Prohibitions').

The act deems as anti-competitive all 'horizontal agreements' between enterprises that have the object of: (1) fixing purchase or selling prices or any other trading conditions; (2) sharing market or sources of supply; (3) limiting or controlling production, market outlet or market access, technical or technological development, or investment; or (4) bid rigging.

There is no similar deeming provision for 'vertical agreements', but the MyCC has set-out in its Chapter 1 Prohibition Guidelines the types of vertical agreements that the MyCC will initially consider as its enforcement priorities:

- those involving price (in particular, the MyCC states that it would take a strong stance against minimum resale price maintenance); and
- those involving non-price restrictions (eg, tying, exclusive distribution agreements, agreements that require the buyer to purchase all/most of its supplies from the supplier, exclusive customer allocation agreements, franchise agreements and up-front access agreements).

12.3 Abuse of dominance

Section 10 of the Competition Act prohibits an enterprise that is in a dominant position from engaging, either independently or collectively, in any conduct that amounts to an abuse of that dominant position in any market ('Chapter 2 Prohibitions').

'Dominant position' is when one or more enterprises possess significant power in a market to adjust prices, output or trading terms, without effective constraint from competitors or potential competitors. The act does not define 'abuse of dominant position', but provides a non-exhaustive list of what may amount to such conduct, such as imposing unfair prices or unfair trading conditions on any supplier or customer, refusing to supply an enterprise or a category of enterprises and so on.

The MyCC has set out in the Chapter 2 Prohibition Guidelines two categories of anti-competitive conduct in this regard: (1) 'exploitative conduct': taking advantage of the market structural conditions and charging an excessive price (eg, if a dominant entity believes that there are no new entrants likely, then it will set a high price to exploit customers); and (2) 'exclusionary conduct': conduct that prevents efficient new competitors from entering or significantly harming equally efficient competitors, either by driving them out or preventing them from effectively competing.

Exception/defence to a finding of an abuse of dominance

A conduct will not amount to an 'abuse' of dominance if the enterprise in a dominant position has a reasonable commercial justification for its actions or such actions represent a reasonable commercial response to the market entry or market conduct of a competitor.

12.4 Merger controls

M&A are not subject to merger control under the Competition Act, but based on publicly available information, it is likely that the MyCC will be introducing merger control provisions in Q3 or Q4 of 2020.

Currently, merger controls have been introduced to regulate enterprises carrying on commercial activities relating to aviation services under the Malaysian Aviation Commission Act, 2015. Parties must notify the Malaysian Aviation Commission (MAVCOM) if a merger may result in a substantial lessening of competition within any aviation service market.

MAVCOM is unlikely to investigate a merger situation unless:

- the combined turnover of the merger parties in Malaysia in the financial year preceding the transaction is at least MYR 50m; or
- the combined worldwide turnover of the merger parties in the financial year preceding the transaction of the merger parties is at least MYR 500m.

12.5 Exemption orders

Parties may also apply to the MyCC for an individual exemption of a particular agreement or a block exemption of a category of agreements from the Chapter 1 Prohibitions. The applicant must show that they meet all the criteria set out in section 5 of the Act (the 'Exemption Criteria').

On 13 November 2019 the MyCC issued a block exemption order (BEO) for certain liner shipping agreements, namely vessel-sharing agreements (VSAs) between liner operators in which the parties agree on the operational arrangements relating to the provision of liner shipping services through transport by sea pursuant to section 8 of the Competition Act.

This BEO, which is effective for the period 7 July 2019 to 6 July 2022 (unless it is withdrawn by the MyCC), is the third BEO issued by the MyCC in respect of the said VSAs. The previous BEOs expired on 6 July 2017 and 6 July 2019. The liner shipping industry remains the first and only industry in Malaysia to receive formal block exemptions under the Competition Act.

12.6 Enforcement and penalties

An investigation by the MyCC has no duration and may arise in three ways: (1) the MyCC can initiate investigations; (2) by the direction of a minister for domestic trade and consumer affairs; (3) by third-party complaints.

The MyCC has wide powers under the Competition Act, which include:

- the power to enter and search premises with or without a warrant;
- the power to require access to or require the production of documents and information; and
- the power to impose interim directions during an investigation, such as prohibiting parties from acting in accordance with any agreement that may be in breach of the act.

Upon the finding of an infringement, the MyCC is empowered to impose a financial penalty of up to ten per cent of the worldwide turnover of an enterprise for any infringement of the prohibitions over the entire period during which the infringement occurred.

Chapter 13: Dispute resolution

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13.1 Structure of the courts

The Malaysian judicial system is composed of subordinate and superior courts. The jurisdictions and powers of the courts are stipulated in the Subordinates Courts Act, 1948 (SCA) for the subordinate courts and Courts of Judicature Act 1964 (CJA) for the superior courts.

The hierarchy of the courts begins from the Magistrates' Court, Sessions Court, High Court, Court of Appeal and the Federal Court as the highest court of the land.

The Magistrates' Court and the Sessions Court form the subordinate courts, while the High Courts (consisting of the High Court in Malaya and the High Court in Sabah and Sarawak), the Court of Appeal and the Federal Court make up the superior courts.

The SCA and CJA outline the different jurisdictions of the courts in both criminal and civil matters. The sentences permissible to be delivered by the courts are also encapsulated in the SCA and CJA.

13.1.1 Magistrates' Courts

For criminal matters, the First Class Magistrates' Courts have jurisdiction to try offences punishable by fines only (not exceeding MYR 100,000) or where their maximum term of imprisonment does not exceed ten years. Further, the two offences of: (1) robbery; and (2) lurking, house-trespass or housebreaking by night in order to commit an offence punishable with imprisonment are specifically stated to be under the jurisdiction of the First Class Magistrates' Courts. On the other hand, the Second Class Magistrates' Courts only have the jurisdiction to try offences for which the offence is punishable by a fine only or where the maximum imprisonment term does not exceed one year.

For civil matters, the First Class Magistrates' Courts can try all actions and suits where the amount in dispute or value of the subject matter does not exceed MYR 100,000. The Second Class Magistrates' Courts are only empowered to try original actions or suits of debt recovery or liquidated monetary demand of not exceeding MYR 10,000.

13.1.2 Sessions Court

For criminal matters, the Sessions Courts have jurisdiction to try all offences, except offences punishable by death.

For civil matters, the Sessions Courts have unlimited jurisdiction to try matters pertaining to motor vehicle accidents, landlords and tenants, and distress. The Sessions Courts also have jurisdiction to try all actions and suits where the amount in dispute or the value of the subject matter does not exceed MYR 1m.

13.1.3 High Court

High Courts have unlimited original jurisdiction to try any criminal and civil matter, and pass any sentence and award allowed by law. High Courts also exercise supervisory, revisionary and appellate jurisdiction. For instance, High Courts may decide on Constitutional questions and hear appeals from subordinate courts, subject to the applicable laws.

The decisions of subordinate courts must involve an amount in dispute exceeding MYR 10,000 to be appealable except on a question of law. High Courts are also empowered to hear all appeals from subordinate courts where they concern the maintenance of wives or children, regardless of the amount in dispute.

13.1.4 Court of Appeal

Generally, every proceeding in the Court of Appeal shall be heard and disposed of by a panel of three judges or a greater uneven number of judges.

The Court of Appeal has jurisdiction to hear all appeals against any decision made by the High Court in the exercise of its original jurisdiction and in the exercise of its appellate or revisionary jurisdiction in respect of any criminal matter originated from the Sessions Court.

For civil matters, the Court of Appeal has jurisdiction to hear and determine appeals from any judgment or order of any High Court in any civil cause or matter, provided that, among others, the amount in dispute must exceed MYR 250,000 unless with leave of the Court of Appeal; the judgment or order sought to be appealed against is not a consent judgment or order; and the judgment or order sought to be appealed against is not one that relates to costs only unless with leave of the Court of Appeal.

13.1.5 Federal Court

The Federal Court was established under Article 121(2) of the Federal Constitution. It is the final court of appeal and/or the apex court in Malaysia.

Similar to the composition of the Court of Appeal, every proceeding in the Federal Court is usually heard and disposed of by a panel of three judges. That said, the law provides that Federal Court cases may be presided over by a panel of a greater uneven number of judges. For example, in 2019 an unprecedented bench of nine judges was convened to hear and deliver a landmark case in Malaysia.

The Federal Court has jurisdiction to hear and determine any criminal appeal from any decision of the Court of Appeal in its appellate jurisdiction in respect of any criminal matter decided by the High Court in its original jurisdiction.

For civil matters, the Federal Court only has jurisdiction to hear the following matters, subject to leave of the Federal Court being granted:

- the decision of the Court of Appeal in respect of any civil matter decided by the High Court in exercise of its original jurisdiction where it involves a question of general principle decided for the first time;
- the decision of the Court of Appeal in respect of any civil matter decided by the High Court in exercise of its original jurisdiction where it involves an important question of law and the further deliberation of the law will be for public advantage; or
- the decision of the Court of Appeal is in relation to any questions on the Federal Constitution, including the validity of any written law relating to any such provision.

13.2 Use of arbitration

In Malaysia, other than resolving disputes through court proceedings, which is the most commonly used method, there are also other forms of ADR, such as arbitration and mediation.

Arbitration proceedings are presided over by arbitrators and governed by the Arbitration Act, 2005. Arbitration proceedings may be held in the Asian International Arbitration Centre or any other premises agreed upon between the parties. Parties are also free to agree on the procedure to be abided by the arbitral tribunal in the conduct of the proceedings. An arbitration award is final, conclusive and enforceable, like any other court orders.

Parties entering into commercial agreements may agree to resolve their disputes through arbitration, which is often spelled out in the contract. Many opt for arbitration for various reasons and the most hailed advantage of arbitration is its confidentiality. In contrast to court proceedings, arbitration is a private process whereby only the parties to the dispute and the arbitrator presiding over the matter will be privy to the matter. The parties are prohibited from publishing, disclosing or communicating any information relating to the arbitration proceedings or an award made in those arbitral proceedings to any third party.

13.3 Other forms of dispute resolution

Other than court proceedings and arbitration, parties may also resolve their disputes through mediation. The mediation procedure is governed by the Mediation Act, 2012. In a mediation procedure, parties may jointly appoint a mediator from the list of Certified Mediators registered with the Malaysian Mediation Centre.

Mediation focuses on the interests and needs of the parties over and above the rights and legal positions of the parties under the law. Hence, mediation is a more relaxed and flexible procedure where parties are free to negotiate and voice their wants and expectations. Further, all admissions and concessions made or documents produced during mediation occur on a without-prejudice basis. A successful mediation will result in the signing of a settlement agreement or recording of a consent order.

In reality, mediation is often directed by courts before trials. There is an in-built mediation mechanism in the court proceedings. Mediation under the Mediation Act will not prevent the commencement of any civil action in court or arbitration.

Singapore

Chapter 1: Introduction

Dinesh Dhillon, Allen & Gledhill, Singapore

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1.1 Political and constitutional structure

Singapore is a republic with a parliamentary system of government based on the Westminster model, with Members of Parliament representing constituencies. The Constitution lays down the basic framework for the three organs of state: the executive, legislature and judiciary.

Parliament and the President jointly make up the Legislature of Singapore. The Singapore Parliament is unicameral and is made up of Members of Parliament who are elected, as well as Non-Constituency Members of Parliament and Nominated Members of Parliament who are appointed. Singapore's executive branch of government consists of the elected President as the Head of State, the Cabinet led by the Prime Minister and the Attorney-General.

1.2 Legal structure

Singapore is a common law jurisdiction and derives its legal system from English common law. Until 1994, Singapore's court of final appeal was the Privy Council in the UK and decisions on common law by the House of Lords were taken as being virtually binding on the local courts. It is expressly provided in the Application of English Law Act that English common law, insofar as it was part of the law of Singapore before 12 November 1993, continues to be a part of the law of Singapore. However, Singapore has built its own substantial body of case law over the years. English judgments are still referred to and applied where appropriate by the local courts, although Australian and Canadian judgments are also referred to for guidance.

The judiciary consists of the Supreme Court and the state courts. The head of the judiciary is the Chief Justice. The Supreme Court comprises the Court of Appeal and the High Court, and specialised courts such as the Singapore International Commercial Court (SICC). The state courts comprise several courts, including specialised courts such as the Small Claims Tribunals and Employment Claims Tribunals.

1.3 Economy

The World Bank, in its *Doing Business 2020* report, ranked Singapore as the world's second-easiest place to do business. The World Economic Forum ranked Singapore as the top-most competitive economy in the world for 2019.

Singapore has one of the highest GDP per capita ratios in the world. Singapore's attractiveness to investors and businesses is the result of its strong economy, its sophisticated and stable business and political environment, and its highly skilled workforce.

Chapter 2: The business environment

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2.1 Government structure

The Singapore government is modelled after the English Westminster system. It has three branches: the legislature, executive and judiciary.

The Prime Minister is the head of the government, while the President is the Head of State. The Chief Justice is the head of the judiciary.

The legislature is responsible for making laws, and comprises the President and Parliament. The proceedings of the legislature may be found in the Official Reports of the Singapore Parliamentary Debates (Hansard).

The executive is responsible for administering laws, and comprises the President, Cabinet and Attorney-General. The Attorney-General is also the Public Prosecutor, and therefore has the discretion to bring charges or not (ie, prosecutorial discretion).

The judiciary is responsible for interpreting the law through the courts and comprises the Supreme Court (made up of the Court of Appeal and the High Court), the state courts (which includes the Small Claims Tribunals) and the Family Justice Courts. The SICC is a division of the High Court and is designed to deal with transnational commercial disputes. A panel of local judges and international judges from both the civil law and common law traditions hear an increasing number of commercial cases brought before the SICC.

2.2 Legal system

Singapore is a common law jurisdiction. In Singapore, the law (both criminal law and civil) can be found in statutes and cases. The Singapore Constitution is the supreme law of the republic, and any law enacted by the legislature after the commencement of the Constitution that is inconsistent with the Constitution is, to the extent of the inconsistency, void.

Statutes are passed by Parliament. These statutes may be accessed online at Singapore Statutes Online. Some key commercial statutes include the Companies Act (Cap 50), the Employment Act (Cap 91) and the Competition Act (Cap 50B). Some key statutes governing criminal law are the Penal Code (Cap 224) and the Criminal Procedure Code (Cap 68).

Case law comprises the corpus of cases decided by the judiciary over time. Many cases are reported and can be found in online depositories. Where cases involve statutory provisions, in the process of deciding the case the courts may interpret certain provisions in a statute. Consequently, a full understanding of what a statutory provision entails may require an examination of the relevant case law.

Singapore courts practice the doctrine of binding precedent or *stare decisis*. In essence, this means that courts lower in the judicial hierarchy are bound to follow the decision of the courts above it if the case they are deciding cannot be distinguished from the prior case. For example, the decisions of the Singapore Court of Appeal are binding on the Singapore High Court. The decisions of courts in other parts of the Commonwealth are not binding on Singapore courts, although it is not unusual for English cases to be cited in Singapore's courts, especially when there is no direct local authority on a topic.

Deciding which court to bring a particular case in may not always be straightforward. While the quantum of the dispute is usually one of the first factors to consider, there may be other considerations. Disputes where the claim exceeds SGD 250,000 are usually litigated in the High Court. Disputes where the claim does not exceed SGD 20,000 are commonly heard by the Small Claims Tribunal.

Alongside the courts, arbitration has long been a popular dispute resolution mechanism. The SIAC is a global arbitration institution providing cost-competitive and efficient case management services to parties from all over the world. Besides cases, Singapore's arbitration law may also be found in statutes like the Arbitration Act (Cap 10) and the International Arbitration Act (Cap 143A). Singapore is a party to the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the 'New York Convention'). Singapore arbitration awards are thus enforceable in many countries around the world. Singapore courts are also supportive of arbitration, and a party to an arbitration agreement may be able to seek a range of critical interim orders from Singapore courts in aid of arbitration.

Some regulatory bodies in Singapore are empowered to seek penalties for breaches of legislation/regulations/licences. Such enforcement actions are not unusual. For example, the Monetary Authority of Singapore (MAS) has on various occasions sought civil penalties for breaches of the Securities and Futures Act (Cap 289) (the 'SFA'). The Infocomm Media Development Authority (IMDA) has also taken enforcement action on various occasions for breaches of the terms of issued licences. These penalties can be substantial, and it may be worth considering written representations to the authorities when an enforcement issue arises. Depending on the circumstances, it may also be worth considering commencing internal corporate investigations. Singapore law protects privileged communications, which makes understanding your rights at an early stage of any potential enforcement action critical.

Chapter 3: Business and corporate structures

June Ho, TSMP Corporation, Singapore

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3.1 Common forms of legal entities

In Singapore, most business entities and structures are regulated by the Accounting and Corporate Regulatory Authority (ACRA). Prior to registering the chosen business structure, the applicant may choose from the following common forms of corporate structures:

3.1.1 Sole proprietorship

A sole proprietorship is a business owned and controlled by an individual, a company or a limited liability partnership (LLP). It does not constitute a separate legal entity from its proprietor. As such, the sole proprietor is personally liable for all liabilities incurred during the course of business, and a sole proprietorship can sue or be sued in the proprietor's name. A sole proprietorship structure is usually recommended for small-scale businesses with no or negligible risk, and it is not usually recommended for businesses that require the hiring of staff or are looking at rapid expansion.

3.1.2 Partnership

A partnership is a business that may be owned by a minimum of two to a maximum of 20 partners. A partnership and all of its partners are regarded as a single legal entity. This means that partners have unlimited liability and are personally liable for the debts or legal liabilities of the partnership. In addition, partners are personally liable for the actions of other partners in the business and a partnership can sue or be sued in the partners' names. A partnership is usually recommended for individuals looking to start and operate a small-scale business with few compliance requirements. However, this structure is not usually recommended for businesses looking to own property, or involving more than 20 individuals.

3.1.3 Limited liability partnership (LLP)

An LLP is a vehicle that gives business owners the flexibility to operate as a partnership while having a separate legal identity, like a private limited company. Registration costs are lower than that of a company, and there are fewer formalities and procedures to comply with. An LLP structure is usually used by chartered professionals, such as lawyers and accountants.

A change in the partners of an LLP will not affect its existence, rights or liabilities. Unlike partnerships, an LLP can sue, be sued and acquire and hold property in its own name. While the partners will generally not be held personally liable for the debts incurred by the LLP, each partner may be held liable for his or her own wrongful acts or omissions.

3.1.4 Limited partnership (LP)

An LP is a vehicle for doing business consisting of a minimum of two partners, including at least one general partner and at least one limited partner. The general and limited partners may be individuals or corporations. In contrast to an LLP, an LP does not have a separate legal personality. Accordingly, it cannot sue or be sued, or own property, in its own name. While the general partner is liable for the actions of the limited partnership, including its debts and obligations, a limited partner generally is not liable for the debts or obligations of the LP beyond its agreed contribution.

In Singapore the LP structure is typically used by investment funds, and it is usually recommended where investors want the general partner of the business to be fully accountable. Accordingly, it is not usually recommended for business owners who do not want to be personally liable for the debts and obligations of the business.

3.1.5 *Private company limited by shares*

A company is a business entity registered under the Companies Act (Cap 50) of Singapore. The company is a separate legal entity from its shareholders, and its shareholders' liabilities are limited to the amount not paid up on shares bought by them. There are two types of private companies in Singapore:

- exempt private company: 20 members or less and no corporation holds a beneficial interest in the company's shares; and
- private company: 50 members or less.

A company tends to have higher set-up and maintenance costs relative to other business structures. Nevertheless, it is usually recommended for business operation, owing to its perception of credibility under requirements in the Companies Act, and its enjoyment of corporate tax rates and coverage pursuant to double tax agreements.

3.1.6 *Branch*

A branch is an extension of a foreign company, often used by foreign companies wishing to conduct business in Singapore. Through the branch, the foreign company carries out its Singapore operations while using its own name. The branch is usually recommended for a foreign company wishing to leverage its existing name and reputation. However, as a branch and its foreign parent company constitute a single legal entity, it is not usually recommended for a foreign business requiring a separate legal entity in Singapore.

3.1.7 *Representative office*

Like a branch, a representative office is an extension of its foreign parent company and is not a separate legal entity from the parent company. However, unlike a branch, it is not permitted to conduct any commercial activities and is temporary in nature, usually for one year with the potential to renew for a maximum of three years. It is typically used by foreign companies wishing to conduct market research in the Singapore market, without incurring incorporation and compliance costs, prior to establishing full-scale operations in Singapore.

3.2 Ongoing reporting and disclosure obligations

3.2.1 *Sole proprietorship*

Sole proprietorships are generally not required to file annual returns nor financial statements. However, sole proprietors may be required to file their annual tax return if they receive a notification from the Inland Revenue Authority of Singapore (IRAS) to do so.

3.2.2 Partnership

Partnerships are exempt from annual audit and are not required to file annual financial statements with ACRA. The partners must file a personal income return and it must relay the revenue and profits of the partnership to the IRAS.

3.2.3 LLP

An LLP is not required to file its accounts or have them audited, but is required to keep its books (accounting records, profit and loss accounts, and balance sheets) up-to-date so as to substantiate all the transactions and financial position of the LLP. Further, the manager of an LLP must submit an annual declaration of solvency or insolvency to ACRA. Such a declaration must be lodged within the first 15 months from the date of the registration of the LLP. Subsequently, a declaration once in every calendar year must be submitted at intervals of not more than 15 months. LLPs will not be liable to tax at the entity level, but each individual partner will be taxed on his or her share of the income from the LLP.

3.2.4 LP

An LP is not required to file its accounts or have them audited, but is required to keep accounting and other records that will sufficiently explain its transactions and financial position. Similar to LLPs, LPs will not be liable to tax at the entity level, but where the partner is an individual, his or her share of the income will be taxed at the tax rate for companies.

3.2.5 Private company limited by shares

All private companies, including exempt private companies, are required to file annual returns with ACRA. The annual return is an electronic form that provides critical information that helps the company's stakeholders to make informed decisions.

Private companies and insolvent exempt private companies are required to file their full set of financial statements with their annual returns, whereas solvent exempt private companies are exempt from filing their financial statements.

3.2.6 Branch

Together with its foreign parent company, a branch office is required to lodge its financial statements with ACRA on an annual basis. These financial statements must consist of audited statements of its assets and liabilities, and profit and loss account arising out of its Singapore operations. These statements are to be prepared in accordance with the Singapore Financial Reporting Standards.

3.2.7 Representative office

The representative office is not obligated to file annual returns with ACRA or annual tax returns with the IRAS.

3.3 Management structures

3.3.1 Sole proprietorship and partnership

In order to set up a sole proprietorship or a partnership, the sole proprietor or at least one partner of the partnership must be: (1) at least 18 years old; and (2) a Singapore citizen, a Singapore permanent resident or an EntrePass holder.

Nevertheless, a foreigner (or foreigners in the case of a partnership) residing overseas may set up a sole proprietorship or a partnership provided that the foreigner(s) appoint(s) at least one authorised representative. Such an authorised representative must be: (1) a natural person; (2) at least 18 years of age; (3) of full legal capacity; and (4) ordinarily resident in Singapore (the 'Requirements'). A person is considered to be 'ordinarily resident in Singapore' if he/she is a Singapore citizen, a permanent resident or a foreigner who has been issued an employment pass.

3.3.2 LLP

The partner in an LLP can be an individual, local company, foreign company or another LLP. Every LLP must have at least one manager ordinarily resident in Singapore, who is a natural person of at least 18 years of age. The manager need not be a partner, and takes part in the management of the LLP. This means that where the LLP fails to comply with certain rules and regulations of the Limited Liability Partnership Act, for example, by failing to file a declaration of solvency, this manager will be held responsible. Thus, compared with partners, the manager of the LLP shoulders heavier responsibilities.

A foreigner who wishes to register an LLP in Singapore is also required to appoint a locally resident manager, or seek approval from the Ministry of Manpower (the 'MOM') if the foreigner wishes to be present in Singapore to manage the operations of the LLP.

3.3.3 LP

The general partner of an LP can be an individual or a company, and the limited partner of an LP can be an individual, company or unregistered foreign company. A foreigner who wishes to register an LLP in Singapore is required to appoint a locally resident manager, or seek approval from the MOM if the foreigner wishes to be present in Singapore to manage the operations of the LLP.

3.3.4 Private company limited by shares

A company must have a company secretary, and at least one director must be resident in Singapore. An auditor is also necessarily appointed three months upon incorporation, unless the company is exempt from audit requirements.

3.3.5 Branch

A branch office must appoint at least one authorised representative who meets the Requirements that apply to an authorised representative appointed under a sole proprietorship or partnership.

3.3.6 Representative office

A representative office can have a maximum of five staff members. It must also appoint a staff member from the foreign company or a Singapore resident employee of the foreign parent company who will act as a representative of the parent company and execute operations in the Singapore office.

3.4 Director, officer and shareholder liability

3.4.1 Sole proprietorship, partnership and LLP

Registration of sole proprietorship, partnership or LLP begins with a name application at a fee of SGD 15. Registration of the sole proprietorship, partnership or LLP with ACRA costs an additional fee of SGD 100. Such a registration can be completed within a day, provided all the supporting documents are lodged properly. However, if the nature of the business requires a referral to another authority, it may take up two months.

3.4.2 LP

Registration of an LP begins with a name application at a fee of SGD 15. Registration of the LP with ACRA costs an additional fee of SGD 100 for a one-year registration or SGD 160 for a three-year registration. Such a registration can be completed within a day, provided all the supporting documents are lodged properly. However, if the nature of the business requires a referral to another authority, it may take up to two months. LP registration must be renewed before it expires, and such a renewal with ACRA costs SGD 30 for a one-year registration or SGD 90 for a three-year registration.

3.4.3 Private company limited by shares

The process of incorporating a private company limited by shares begins with the applicant filing an application with ACRA for the approval of a proposed company name. The application fee for the company name is SGD 15. To complete the incorporation procedure, the applicant must provide information and documents, such as the principal activities of the company and a registered Singapore address, among others. Upon the population of the details on ACRA and payment of the registration fee of SGD 300, the company will be set up within the day.

3.4.4 Branch

Similar to the setting up of a private limited company, sole proprietorship and different forms of partnerships, the registration of a branch office begins with a name application. The application costs SGD 10 and can be processed within a day, but may take up to two months in the event of referrals to other authorities. Registration of a branch office on ACRA will cost an additional SGD 300, and the branch office may commence business upon registration unless additional licences or approvals are required due to the nature of the business.

3.4.5 Representative office

A foreign company that wishes to establish a representative office in Singapore must: (1) have been established in its home country for three years or more; and (2) have incurred a sales turnover of more than US$250,000.

A representative office must be registered with Enterprise Singapore. The documents required for the approval process with Enterprise Singapore include: (1) a completed application form (via Enterprise Singapore's online portal); (2) a copy of the parent company's Registration Certificate or Certificate of Incorporation; and (3) copies of the parent company's latest annual report and audited accounts.

For any document not in English, an official English translation must be submitted to the online portal pursuant to the application. The processing fee for setting up a representative office and renewing the representative office each year is SGD 200.

Chapter 4: Takeovers (friendly M&A)

Lee Kee Yeng, Allen & Gledhill, Singapore

4.1 Legal and regulatory framework

Where a public listed company is being acquired or taken over, such an activity is principally governed by an advisory body known as the Securities Industry Council (SIC). The SIC is the principal regulator that administers and enforces the Singapore Code on Take-overs and Mergers (the 'Takeover Code'). The SIC is made up of representatives from the government, MAS and private sector. The day-to-day business of the SIC is conducted by a professionally staffed full-time Secretariat.

The Takeover Code applies to the acquisition of voting control of public companies. It applies to corporations (whether local or foreign), business trusts and real estate investment trusts (REITs) with a primary listing of their equity securities in Singapore. It also applies to unlisted Singapore companies and unlisted registered business trusts or REITs with more than 50 shareholders or unit holders, and net tangible assets of SGD 5m. Although the Takeover Code does not have the force of law, its breach may result in the imposition of sanctions by the SIC.

Where either the acquiring company or the target company is a company listed on the Singapore Exchange (the 'SGX'), the SGX Listing Manual (the 'Listing Manual') also applies.

4.2 Merger control and statutory shareholding restrictions in specific industries

Section 54 of the Competition Act prohibits mergers that result, or may be expected to result, in a substantial lessening of competition within any market for goods or services in Singapore. Failure to follow merger control procedures where it would otherwise have been advisable to do so could result in financial penalties, or a direction for the merger to be unwound or for divestments to be carried out.

Other statutes relating to particular industries also govern takeover activity in Singapore insofar as they limit or require prior regulatory approval for share ownership in companies engaged in those industries. Those industries are generally industries perceived to be critical to national interests, for instance, banking, finance, insurance and media.

4.3 Types of takeover offers

4.3.1 Mandatory offers

A mandatory offer is triggered when an offeror acquires 30 per cent or more of the voting rights of the target company or, if it already holds between 30 and 50 per cent of the target company's voting rights, it acquires more than one per cent of the target company's voting rights in any rolling six-month period. In a mandatory offer, the offer price cannot be lower than the highest price paid by the offeror or its concert parties. The consideration paid in the mandatory offer should be in cash or be accompanied by a cash alternative. A mandatory offer is conditional upon the offeror obtaining acceptances that will result in the offeror, and persons acting in concert with it, holding shares carrying more than 50 per cent of the voting rights of the target company. Generally, no other conditions are permitted to be imposed in a mandatory offer.

Where an offeror acquires more than 50 per cent of the voting shares of a target company and, as a result, the offeror acquires or consolidates control of the public company because the target company itself had effective control of the public company, the offeror may be required to make a mandatory takeover offer for the public company.

4.3.2 Voluntary offers

A voluntary offer occurs where the offeror makes an offer for all the shares of the target company when the offeror has not incurred an obligation to make a mandatory offer. A voluntary offer must always be conditional on the offeror and its concert parties acquiring more than 50 per cent of the target company. In addition, the offeror may stipulate other objective conditions, such as a particular level of acceptances, shareholders' approval and certain regulatory approvals. In a voluntary offer, the offer price cannot be lower than the highest price paid by the offeror or any of its concert parties for any shares carrying voting rights in the target company during the offer period and within the three months leading up to the beginning of the offer period. The offer may be in cash or securities, or a combination thereof.

4.3.3 Partial offers

Partial offers are voluntary offers for less than 100 per cent of the outstanding shares in a target company. All partial offers must be approved by the SIC. Generally, the provisions in the Takeover Code applicable to a voluntary offer will also apply to partial offers, and the documents required for a partial offer will also be required in relation to a voluntary offer. Consideration for a partial offer may be in the form of cash or securities, or a combination of both.

4.3.4 Scheme of arrangement

An acquisition of a public company may also be effected through a scheme of arrangement provided for in section 210 of the Companies Act. In a scheme of arrangement, outstanding shares of the target company are either cancelled or transferred to the acquirer in consideration for cash and/or shares. Usually a scheme of arrangement is only used in a situation where the acquiror wishes to acquire all the shares of a target company and such acquisition is supported by the target company. All schemes of arrangement are subject to compliance with the Takeover Code. In accordance with Section 210 of the Companies Act, a scheme of arrangement requires the approval of a majority of members of the target company present and voting, representing at least 75 per cent in value of the shares voted at a scheme meeting. In the voting process, the acquiror and its related parties, as well as common substantial shareholders of the acquiror and the target company must abstain from voting. Furthermore, the scheme also requires the sanction of the High Court. Once an order for a scheme of arrangement has been approved by the High Court, it binds all shareholders, including those who objected to it at the scheme meeting or in the High Court.

4.3.5 Amalgamation process

As an alternative to the scheme of arrangement, an acquisition of a public company may be effected through an amalgamation process. Such a process may involve either two or more companies amalgamating and continuing as one company, or two or more companies amalgamating and forming a new company. The main difference in the amalgamation process is that it does not require the sanction of the High Court.

4.4 Directors' duties

The Takeover Code prevents a target company from frustrating a bona fide offer. When a target company's board of directors has been notified of a bona fide offer, or after the target's board has reason to believe that a bona fide offer is imminent, the board cannot, without shareholders' approval, take any steps that could effectively result in either the offer being frustrated, or denial of the target shareholders' opportunity to decide on the merits of the offer. The target company's board of directors must obtain the advice of an independent financial adviser when it receives an offer or is approached with a view to an offer being made, and must subsequently inform the shareholders of the substance of this advice. In addition, the directors of a company have a fiduciary duty under common law to act in the interests of the company and its shareholders as a whole.

4.5 Shareholder disclosures

The parties to a takeover and their associates are required to disclose shares, options or derivatives purchased or sold by them on their own account on a daily basis. The term 'associate' will normally include a holder of five per cent or more of the equity share capital of the offeror or target company. Disclosure must be made to the SGX and the SIC. Apart from the Takeover Code, shareholder disclosure obligations are found in the Companies Act and the SFA, and are required by the SGX with regard to listed companies. Disclosure obligations arise when a shareholder becomes a substantial shareholder, that is, a shareholder who has an 'interest' of five per cent or more of the total votes attached to all the voting shares in a company. Disclosure must subsequently be made if there is a change in the substantial shareholder's interest in voting shares in a company in threshold bands of one per cent.

4.6 Suspension of trading and compulsory acquisition

If the offeror and its concert parties should, as a result of the offer or otherwise, own or control above 90 per cent of the issued share capital of the target company, the SGX may suspend the listing of the shares in the target company. An offeror who acquires not less than 90 per cent of the issued target company shares pursuant to a takeover offer (excluding those shares held at the date of the offer by, or by a nominee for, the offeror or its holding company, subsidiary or fellow subsidiary) is entitled compulsorily to acquire any remaining target shares under section 215 of the Companies Act. Conversely, dissenting shareholders of the target company have a right to be bought out by the offeror if the offeror and its subsidiaries hold 90 per cent or more of the issued target company shares.

Chapter 5: Foreign investment

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5.1 Foreign investment control/restriction

5.1.1 Introduction

Singapore relies heavily on foreign investment to drive economic growth. As such, the Singapore government places strong emphasis on attracting foreign investment, and has set up various organisations to encourage foreign investment (eg, the Singapore Trade Development Board), offering an extensive range of tax relief, as well as low barriers to entry for foreign investment.

5.1.2 Foreign investment control

Singapore has relatively minimal foreign investment control. For foreign individuals or corporations who intend to invest in a Singapore company, there are no special post-closing or filing requirements. The Takeover Code is applicable to all offerors, whether they are persons or corporations (be they resident in Singapore or not), and does not impose different requirements for foreign offerors compared with offerors resident in Singapore.

5.1.3 Licensing and legislative restrictions

However, approval is required for foreign investment in specific sectors. The Singapore government controls these sectors through licensing regimes (applying both qualitative and quantitative criteria depending on the sector involved) and legislative restrictions.

5.1.4 Restrictions on investment in the broadcasting sector

One restricted sector that requires licensing in Singapore is broadcasting. A licence is needed to carry out licensable broadcasting activities in Singapore, and a broadcasting licence will not be granted by the IMDA (the main regulatory body for this sector) if the broadcasting company is directed, managed or controlled by any foreign source or if any foreign source holds not less than 49 per cent of the share capital or voting power in the company.

5.1.5 Restrictions on investment in the real estate sector

Another sector that is restricted by legislation in Singapore is real estate. The main regulatory bodies for this sector are the Singapore Land Authority, the Housing and Development Board (the 'HDB') and Jurong Town Corporation (JTC), depending on the type of real estate involved. In general, transfers of real estate in contravention of foreign ownership restrictions will be null and void, and any person who acts in contravention of such restrictions will be guilty of an offence.

Real estate in Singapore is divided into three types: residential property, commercial property and industrial property. Residential property is classified into two categories: public and private property. Generally, foreigners are not permitted to purchase public housing flats (ie, HDB flats) unless his or her spouse is a Singapore citizen.

Additionally, pursuant to the Residential Property Act (Cap 274) of Singapore, government approval is required before a foreigner may purchase certain types of residential property. These restricted residential property types include, inter alia, vacant residential land, terrace or semi-detached houses and strata-landed houses.

Foreigners who are eligible to purchase residential property are also liable to pay higher rates of Buyer's Stamp Duty (BSD) and Additional Buyer's Stamp Duty (ABSD) to the IRAS. However, pursuant to certain free trade agreements to which Singapore is a party, nationals of some countries are accorded the same stamp duty treatment as Singapore citizens.

It is also noteworthy that non-Singapore citizens and companies who are not tax residents in Singapore and who have been assessed as 'property traders' will be required to pay an additional WHT of 15 per cent of the entire sale price of the property.

Apart from residential property, foreign individuals or entities may also wish to invest in commercial or industrial property. Fortunately, there are no restrictions on the purchase of commercial or industrial property by foreign individuals or entities in Singapore.

However, it should be noted that as industrial property is generally managed and administered by the JTC, persons owning or operating industrial property will be required to comply with the JTC's prevailing policies. Such policies may include the requirement to apply for approval before subletting the property.

In terms of tax, BSD (but not ABSD) is payable in respect of commercial and industrial property to IRAS.

Apart from BSD and ABSD, government service tax (GST), property tax and Additional Conveyance Duties ('ACD') may also be imposed on the purchase of property. GST is payable in respect of, inter alia, the sale and lease of non-residential property. Property tax is payable by the registered proprietor of the property, which is determined based on a valuation of the said property. ACD is payable on qualifying acquisitions and disposals of equity interests in property-holding entities the primary tangible assets of which are Singapore residential property.

5.2 Foreign exchange control

5.2.1 MAS

The MAS is Singapore's central bank and integrated financial regulator. The MAS issues currency, oversees payment systems, and serves as banker to and financial agent of the government.

5.2.2 Capital injection and repatriation of funds

There are no foreign exchange or currency restrictions on the remittance or repatriation of capital or profits in or out of Singapore. Therefore, funds may be freely remitted into and out of Singapore.

The government imposes certain restrictions on the lending of the Singapore dollar to non-resident financial institutions to limit speculation in the country's currency market. However, these restrictions do not apply to the lending of Singapore dollars to individuals and non-financial institutions.

However, taxes that are applicable to businesses in Singapore affect the amount of profits that may be repatriated out of Singapore. For example, gains or profits accrued in, derived from or received in Singapore from outside the nation are subject to income tax, regardless of the tax residency status of the corporate entity. Additionally, certain types of income derived in Singapore and received by non-resident businesses may be subject to WHT.

5.2.3 Payment of dividends

In relation to dividends, Singapore operates a one-tier taxation system. This means that dividends are not subject to tax in the hands of the receiver. The amount from which the dividends are paid has already been subject to corporate tax on profit, and hence dividends paid to foreign corporate shareholders by a company tax resident in Singapore are not taxable.

However, dividends received from foreign companies are subject to income tax in Singapore if they are remitted to Singapore. Fortunately, taxpayers can claim an exemption from tax if: (1) the income has been taxed under the law of the territory from which the income is received; (2) the taxpayer receiving the income is resident in Singapore; (3) the comptroller of income tax is satisfied that the tax exemption is beneficial to the resident in Singapore; and (4) the highest tax rate in the territory from which the income is received is not less than 15 per cent.

5.3 Applicable tax incentive or grant

Singapore's tax incentive schemes are set out in the Income Tax Act (Cap 134) and the Economic Expansion Incentives (Relief from Income Tax) Act (Cap 86).

Tax incentive schemes are administered by a number of statutory agencies, including the Economic Development Board (EDB), Enterprise Singapore, the Maritime and Port Authority of Singapore (the 'MPA') and the MAS.

5.3.1 Key tax incentives offered by the EDB

To encourage businesses to grow capabilities, conduct new or expanded activities, and conduct headquarter activities in Singapore, the EDB's Pioneer Certificate Incentive (PCI) and Development and Expansion Incentive (the 'DEI') offer tax exemptions and concessionary tax rates of five per cent or ten per cent on qualifying income to approved companies for a period of five years.

The EDB also administers the Finance and Treasury Centre Incentive (the 'FTCI'), to encourage companies to base their treasury management activities in Singapore. Approved companies under the FTCI will be entitled to concessionary tax rates of eight per cent on qualifying income and an exemption on WHT on qualifying interest payments for a period of five years.

5.3.2 Key tax incentives offered by Enterprise Singapore

One of the key tax incentives offered by Enterprise Singapore is the Global Trader Programme (GTP). The GTP is targeted at companies engaged in the international trading of commodities or commodities derivatives. Approved companies under the GTP will be entitled to concessionary tax rates of five per cent or ten per cent on qualifying trading income.

Enterprise Singapore also administers the S13H scheme and the Fund Management Incentive (FMI) for venture capital and private equity funds and fund management companies, respectively. Approved venture capital and private equity funds under the S13H scheme are entitled to tax exemptions for up to ten years on qualifying investment income, while approved fund management companies under the FMI are entitled to a concessionary tax rate of five per cent for up to ten years on management fees and performance bonuses.

5.3.3 Key tax incentives offered by the MPA

The MPA administers tax incentives for the maritime sector, through its Maritime Sector Incentive (MSI).

The MSI is comprised of three awards granted for three types of activity: (1) the MSI – Approved International Shipping Enterprise Award is targeted at ship owning and operating companies, and entitles such companies to tax exemptions for periods of five or ten years; (2) the MSI – Maritime Leasing Award covers vessel and container financing, and entitles approved ship or container leasing or management companies to concessionary tax rates of ten per cent on qualifying leasing or management income for up to five years; and (3) the MSI – Shipping-related Support Services Award is granted to companies engaged in shipping-related support services, including shipbroking and management, freight forwarding and logistics, as well as crew and staff training and management. Approved companies under the MSI – Shipping-related Support Services Award are entitled to concessionary tax rates of ten per cent on qualifying income for five years.

5.3.4 Key tax incentives offered by the MAS

The MAS administers various tax incentives targeted at the financial sector, one of which is the Financial Sector Incentive (FSI). The FSI is offered to a range of financial institutions engaged in various activities, including banking, capital and derivatives market services, credit facilities syndication, fund management and trustee services. Approved financial institutions under the FSI are entitled to concessionary tax rates of five per cent, ten per cent, 12 per cent or 13.5 per cent for a period of five years.

The MAS also administers the Insurance Business Development Scheme (IBDS) for insurance and reinsurance companies. Approved insurers or reinsurers under the IBDS are entitled to concessionary tax rates of five per cent, eight per cent or ten per cent, depending on the type of risk they underwrite.

5.3.5 Grants

Grants may also be offered by various statutory agencies in Singapore.

The EDB offers a variety of grants, including the Research Incentive Scheme for Companies for research and development (R&D) projects; the Training Grant by Company for manpower training and development; and the Land Intensification Allowance for companies in the manufacturing and logistics sector looking to intensify their land use.

The MPA offers various grants to companies engaging in R&D projects relating to the maritime sector. These include the Maritime Innovation and Technology Fund, the Maritime Transformation Programme and the Singapore Maritime Institute Funds.

Finally, the MAS, under its Financial Sector Development Fund, issues grants for a range of financial sector activities, including bond issuance, listing on the SGX and the development of solutions or technology for the financial sector.

Chapter 6: Restructuring and insolvency

Andrew Chan, Allen & Gledhill, Singapore

6.1 Introduction

Insolvency law in Singapore is broadly divided into personal insolvency (or bankruptcy) and corporate insolvency. The main statutes governing these areas are the Bankruptcy Act and the Companies Act, respectively, although certain aspects of the Bankruptcy Act also apply to corporate insolvency.

Penalties for non-compliance with either the Bankruptcy Act or Companies Act can be imposed upon insolvent debtors for failure to comply with certain standards set by the statutes. Some acts of creditors are also prohibited in certain circumstances, but the penalties are largely civil rather than criminal.

A new omnibus act consolidating Singapore's personal and corporate insolvency and debt restructuring laws was gazetted on 7 November 2018. When it comes into force, the Insolvency, Restructuring and Dissolution Act, 2018 will modernise the law on corporate insolvency and strengthen debt restructuring regimes to provide greater opportunity for the rehabilitation of companies in financial distress.

Corporate insolvency can broadly be divided into the following four categories: liquidation, judicial management (JM), schemes of arrangement and receivership.

6.2 Liquidation

6.2.1 Description

'Liquidation' or 'winding up' refers to a process where the assets of a company are collected and realised. The resulting recoveries are used to pay the company's liabilities, with any surplus going to the shareholders. In the distribution of the company's assets among the non-preferential unsecured creditors of the company, the rule is usually distribution on a pro rata or *pari passu* basis. The end result of liquidation or winding up is usually the dissolution of the company.

6.2.2 Types of liquidation

There are two main types of liquidation: voluntary and compulsory. The main difference lies principally in the manner in which the liquidation process is initiated and the date of its commencement pursuant to the Companies Act. For a voluntary liquidation, the company generally initiates the process by passing a resolution in a general meeting of shareholders to liquidate the company. For a compulsory liquidation, the company, or some other party with the right (eg, a creditor) initiates the process by making an application to the court to liquidate the company. In the context of corporate insolvency, two common types of insolvent winding up are creditors' voluntary liquidation and compulsory liquidation pursuant to section 254(1)(e) of the Companies Act.

6.2.3 Effect of the commencement of liquidation

Regardless of whether liquidation is compulsory or voluntary, a number of consequences will follow once the process has commenced. In general, the consequences include the following:

- the company's business will generally cease;
- the powers of the company's directors will also cease;
- every invoice, goods order or business letter must include the words 'in liquidation' after the company's name to serve as a notice to all those dealing with the company; and
- any transfer of shares or alteration in the status of the members will be void.

6.2.4 *Avoiding liquidation consequences*

To avoid the consequences of a liquidation (ie, dissolution), an insolvent company has three options: (1) attempt to enter into a scheme of arrangement with its creditors; (2) seek to be put under JM; or (3) enter into an arrangement with its creditors under section 309 of the Companies Act.

6.3 Schemes of arrangement and compromise

Under a scheme of arrangement and compromise, which is outside of JM, a company must formulate a scheme proposal for consideration by its creditors. Typically, this will include a proposal for a compromise of the company's debts by way of various methods, such as payment of a reduced amount or issuance of equity for debt. The company must then seek the court's approval to call a meeting of its creditors. If approval is granted, the creditors will consider the proposal and vote on it at their meeting. If the requisite majority in number and value of creditors or class of creditors approve the scheme, the final step is for the court to sanction it. In making such a decision the court will consider whether the statutory requirements to effect a scheme have been complied with, whether sufficient information has been provided to the company's creditors, whether the terms of the scheme are reasonable and whether the terms of the scheme discriminate unfairly against any creditor or class of creditors. If the court sanctions the scheme and the order sanctioning the scheme is filed with the Accounting and Corporate Regulatory Authority, it becomes binding between the debtor company and its creditors. A scheme can also be sought in JM, and in general, the requirements for a binding scheme in JM are easier to satisfy as compared to one outside of JM.

On 23 May 2017 new provisions, including those adapting parts of Chapter 11 of the US Bankruptcy Code aimed at enhancing Singapore's restructuring framework and status as a centre for international debt restructuring, came into force. Key provisions include:

- moratorium: there is a limited automatic moratorium and the court may further order a moratorium in favour of a company that is proposing or intends to propose a new scheme, preventing creditors from, among other things, taking action against the company and giving the company breathing room to put forward its restructuring proposal;
- priority for rescue financing: the court is empowered to order that rescue financing be given equal or super-priority;
- cram-down provisions: the court may approve a scheme even if there are dissenting creditor classes, provided safeguards are met; and
- pre-packaged voting scheme: the court may dispense with calling creditor meetings if certain safeguards are met.

6.4 Judicial management (JM)

6.4.1 *Description*

An application may be made to the court to place a company under JM. The JM regime aims to provide a company that is or is likely to become unable to pay its debts as and when they fall due with some ‘breathing space’ so that it can either be nursed back to financial health or achieve a better realisation of its assets than it would in liquidation. When the new Insolvency, Restructuring and Insolvency Act comes into force, there will also be the possibility of an out-of-court JM process, and there are some parallels between the court and out-of-court process. Below is a description of the court-based JM process.

6.4.2 Commencing a court-based JM process

The court-based JM process begins with a court application made in a prescribed form. This will state, among other things, that the company is or is likely to become unable to pay its debts and that there is a reasonable probability of either rehabilitation for the company, preservation of its business as a going concern or a better serving of the creditors’ interests than in a winding up. The application may be made by the company, its directors, a creditor or creditors.

6.4.3 Granting a JM order

The court may make a JM order in relation to a company if it is satisfied that the company is or is likely to become unable to pay its debts and that there is a real prospect that the order will achieve one or more of the following three purposes:

1. survival of the company;
2. approval under the Companies Act of a compromise or arrangement between the creditors and/or members, or any class of them; or
3. a more advantageous realisation of the company’s assets than on a winding up.

The mere satisfaction of these conditions will not necessarily lead to the grant of a JM order and, exceptionally, if it is in the public interest to do so, the court may grant an order even if the conditions are not met.

6.4.4 Effecting a JM order

Unless discharged, a JM order will remain in force for 180 days (which may be extended by the court). A judicial manager will be appointed and empowered to do all things for the management of the company’s affairs, business and property, including any tasks which are necessary to achieve the JM purposes. The judicial manager must prepare and send proposals for achieving these purposes to the creditors within 60 days (which may be extended by the court) of the JM order. If the creditors approve the proposals, the judicial manager must then manage the company in accordance with them. Such proposals may include the company entering into a scheme of arrangement or selling any part of its undertaking that remains viable.

6.4.5 Discharging a JM order

The judicial manager is under a statutory obligation to apply for the discharge of a JM order when it appears that the purposes specified in it have either been achieved or are incapable of being achieved.

The result of a JM's successful completion largely depends on the judicial manager's proposals and the circumstances of each case. If the proposals lead to a scheme of compromise, this may result in part of the company's debts being extinguished or reduced in accordance with the scheme. The failure of JM will result in the company reverting to its pre-JM position. However, it may well lead to liquidation because one of the prerequisites for a JM application is a company's inability or likely inability to pay its debts, which is also a ground for liquidation.

6.5 Receivership

The appointment of receivers or receivers and managers is an alternative to the liquidation process. Although, in principle, receivers may be appointed in respect of individuals, more often than not they are appointed only in relation to companies. Going into receivership does not necessarily spell the end for a company; it can continue to exist as an entity.

A receiver can be appointed by a debenture holder and its key duty is to collect the assets that are the subject matter of the debenture, realise these assets and settle the dues of the creditors. Where the receiver is also appointed as manager, it will have additional power to manage the company's business.

Chapter 7: Employment, industrial relations, and work health and safety

Kelvin Wong, Allen & Gledhill, Singapore

7.1 Employees' rights and protection

7.1.1 Introduction

Employers and employees are generally free to agree on the terms of employment. Nevertheless, Singapore law sets out certain safeguards for employees. This section provides a summary of the regulatory framework surrounding employment in Singapore.

Employment law in Singapore is governed by both statute and case law. The regulatory framework for employment in Singapore is applicable to: (1) all employees who work in Singapore, including foreign employees; and (2) certain employees who work in foreign countries and have employment contracts governed by Singapore law.

7.1.2 Employees' rights and protection

Employment Act

The primary legislation for employment in Singapore is the Employment Act. The Employment Act applies to all employees, except seafarers, domestic workers and public servants, and sets out minimum terms relating to such matters as annual leave, sick leave, holidays, termination, salary payment and maternity benefits.

Employees who are regarded as more vulnerable receive additional levels of protection under the Employment Act. Such employees are:

- workmen (as defined in the Employment Act) who are in receipt of a salary not exceeding SGD 4,500 a month; and
- every employee, other than workmen or a person employed in a managerial or an executive position, who receives a salary not exceeding SGD 2,600 a month.

In relation to such employees, the Employment Act sets out further minimum terms relating to such matters as rest days, hours of work and overtime pay.

An employment contract that is less favourable to an employee than any of the minimum conditions prescribed by the Employment Act is illegal, null and void to the extent that it is less favourable. Employers who fail to employ on the minimum terms may be liable to fines and/or imprisonment.

Employees who have salary-related disputes or wish to bring wrongful dismissal claims may do so before the Employment Claims Tribunal.

7.1.3 Other statutory protections for employees

The Employment Act and the Child Development Co-Savings Act set out certain parental benefits and maternity protections for employees. These include maternity leave and adoption leave for female employees, paternity leave for male employees, and childcare leave and extended childcare leave for employees who have children. The Employment Act further provides that it is unlawful for an employer to give a female employee notice of dismissal while she is on maternity leave if she is eligible to take such leave and has given sufficient notice of such leave.

The Retirement and Re-employment Act (the ‘RRA’) provides for a prescribed minimum retirement age (currently 62 years old). Under the RRA, an employer is prohibited from dismissing on the grounds of age any employee who is below the prescribed minimum retirement age unless certain exemptions apply. An employer is also required to offer re-employment to any employee who has attained the prescribed minimum retirement age, as long as the employee fulfils certain eligibility criteria and is willing to continue to work.

The Workplace Safety and Health Act requires employers to take measures that are necessary to ensure the safety and health of employees at work. This includes ensuring a safe work environment and providing the necessary training and supervision for employees to perform their work.

The Work Injury Compensation Act requires employers to compensate an employee covered under the act if the employee suffers any personal injury by an accident arising out of and in the course of employment. Employers are also required to maintain insurance against all liabilities that may be incurred under the act, subject to certain exceptions.

7.1.4 Industrial relations

Singapore enjoys a relatively high degree of industrial harmony. Since gaining independence in 1965, Singapore has only experienced two major industrial actions. Most industrial disputes are resolved by conciliation in the Industrial Arbitration Court (IAC).

Every employee over the age of 16 has a right to be represented by a trade union in Singapore. Under the Industrial Relations Act (IRA), an employer is not permitted to dismiss or threaten dismissal of an employee on the ground of the employee becoming or proposing to become an officer or member of a trade union.

The IRA sets out the process by which a trade union may be recognised and thereafter negotiate a collective agreement with an employer. The collective agreement governs the terms of employment for the employees covered under the collective agreement. Once agreed upon between the trade union and employer, and certified by the IAC, the collective agreement is binding on the employer (or its successor), and on the relevant trade union and its members.

A collective agreement is valid for an operative period of not less than two years and not more than three years.

7.2 Statutory contributions and minimum wage

7.2.1 Central Provident Fund

The Central Provident Fund Act (CPFA) sets out a national savings scheme that applies to employees who are Singapore citizens or Singapore permanent residents. Under the CPFA, employers are required to make monthly contributions at prescribed rates to the Central Provident Fund (CPF) accounts of employees who are Singapore citizens or Singapore permanent residents. The contribution rates vary depending on factors such as the employee's age and salary and are set out in the First Schedule to the CPFA.

7.2.2 Minimum wages

There is no minimum wage in Singapore. However, progressive wage models apply to Singapore citizens and Singapore permanent residents employed in certain businesses in the cleaning, security or landscape sectors through various conditions at the licensing or registration stage.

7.3 Work permits

7.3.1 Work passes for foreign employees

Under the Employment of Foreign Manpower Act (the 'EFMA'), foreign employees (being employees who are not Singapore citizens or Singapore permanent residents) are required to obtain a valid work pass before they start work in Singapore. Working in Singapore without a valid work pass is an offence for both the employer and the foreign employee and may result in fines and/or imprisonment.

Work passes are issued by the Ministry of Manpower (MOM). The types of work passes available are set out in the Employment of Foreign Manpower (Work Passes) Regulations, 2012. They are as follows:

- work permit (including a training work permit);
- S pass;
- employment pass (including a training employment pass);
- personalised employment pass;
- Entre-Pass;
- work holiday pass;
- miscellaneous work pass; and
- letter of consent.

The relevant work pass for each employee depends on the employee's scope of work and professional qualifications. Generally:

- work permits are issued to unskilled or semi-skilled foreign workers in the construction, manufacturing, marine shipyard, processes or services sectors, as well as foreign domestic workers;
- S passes are issued to mid-skilled foreign employees who earn at least SGD 2,400 a month and meet certain criteria in qualifications and work experience;
- employment passes are issued to foreign professionals, managers and executives who earn at least SGD 3,600 a month and meet certain qualifications criteria. The MOM has recently announced an increase of this salary threshold to SGD 3,900 a month. This revision came into effect from 1 May 2020 for new employment pass applicants and will come into effect from 1 May 2021 for employment pass renewals; and
- personalised employment passes (PEPs) are issued to: (1) existing employment pass holders who earn a fixed monthly salary of at least SGD 12,000; and (2) overseas foreign professionals who have a last drawn fixed monthly salary of at least SGD 18,000.

Applications for work passes are generally carried out by the employer on the employee's behalf, except in the case of PEPs, which must be applied for by the foreign employee seeking to be a PEP holder.

The work pass issued to a foreign employee is specific to the foreign employee's particular employer and occupation (except in respect of PEP holders). Therefore, a foreign employee who wishes to carry out work for any other entity than the employer appearing on the existing work pass is required to obtain a new work pass to that effect.

Family members of eligible S pass or employment pass holders may join the S pass or employment pass holder in Singapore on a dependant's pass or long-term visit pass (LTVP). Upon obtaining the dependant's pass or LTVP, they may also apply for a letter of consent, which would allow them to work in Singapore.

For completeness, the number of work permit holders and S pass holders that may be hired by an employer is limited to a quota, known as the dependency ratio ceiling. This quota varies based on the sector. Employers of work permit holders and S pass holders are also subject to a foreign worker levy.

Chapter 8: Tax law

Sunit Chhabra, Allen & Gledhill, Singapore

8.1 Taxes applicable to individuals

Singapore tax-resident individuals are subject to tax on employment income on a progressive scale, with a maximum tax rate of 22 per cent. The employer is required to complete the annual Return of Employee's Remuneration (Form IR8A and accompanying appendices) and issue the completed form to the employee by 1 March each year, reporting all remuneration of the employee for the preceding calendar year, and the employee is required to include the information in the Form IR8A and its accompanying appendices in his or her income tax return to IRAS, unless the employer has arranged for such information to be transmitted directly to IRAS.

Most employers in Singapore come under the Auto-Inclusion Scheme (AIS) for Employment Income. Under the AIS, employers submit their employees' income information directly to IRAS electronically, and such income information is reflected on their employees' electronic income tax return (and automatically included in their income tax assessment).

Certain personal reliefs may be available to individuals to reduce chargeable income, including earned income relief, CPF relief and Working Mother's Child Relief, provided that the employee is a Singapore tax resident and satisfies the relevant qualifying conditions for such reliefs to apply.

8.2 Taxes applicable to businesses

The current tax rate for companies is 17 per cent, with a partial tax exemption for the first SGD 200,000 of annual chargeable income.

Companies are required to file a tax return declaring their income for each year of assessment ('YA') and submit supporting documents by 30 November (paper submissions) or 15 December (electronic submissions), as well as file an estimate of their income chargeable with tax for each financial year within three months from the end of the financial year. Companies are then required to pay income tax within one month from the date of the Notice of Assessment, unless such a company is paying via instalments through automatic deductions.

Losses incurred from a trade or business may be set off against income derived from other sources, and may, subject to certain conditions, be allowed to be carried forward or backward to be set off against income in another YA, or to be transferred to related Singapore-incorporated companies and set off against such a company's profits.

Dividends issued by Singapore tax-resident companies are exempt from tax, as Singapore operates a one-tier tax system on corporate profits.

WHT may be chargeable on certain payments, such as interest, royalties and directors' fees made by a Singapore tax-resident or Singapore-based entity to a non-tax resident person, at a rate between ten and 22 per cent, depending on the nature of such a payment. The rate may be reduced by an applicable tax treaty between Singapore and the country in which the recipient is a tax resident.

Aside from companies, a business in Singapore can be structured in various forms, including a partnership, LLP and LP. A partnership does not have a separate legal personality from its partners and is regarded as a tax-transparent entity such that the partners are taxed on their share of income from the partnership due to them for a basis period at their applicable income tax rates. An LLP has a separate legal personality from its partners, but is treated as a partnership for the purpose of income tax; that is, partners are taxed on their share of income from the LLP at their applicable income tax rates. However, there are certain deduction restrictions for partners in an LLP. Similarly, an LP is regarded as a tax-transparent vehicle, and a limited partner in an LP is also subject to certain deduction restrictions.

8.3 Other taxes

Stamp duty is generally payable on the contract or agreement for the sale of or the instrument for the transfer of immovable property in Singapore or shares registered in Singapore, as well as on mortgages and leases. The rate of Buyer's Stamp Duty is about three per cent (of the higher of the consideration or value of the property) for the transfer of immovable property, and the top marginal Buyer's Stamp Duty rate of four per cent will apply to the portion of residential property the value of which is in excess of SGD 1m. For a transfer of shares, stamp duty is payable at the rate of 0.2 per cent of the higher of the consideration or value of such shares. Generally, stamp duty is payable by the transferee of the property or shares. However, relief from stamp duty may be available in certain circumstances, subject to qualifying conditions.

Goods and services tax (GST) is imposed at a rate of seven per cent on any supply of goods or services in Singapore by a GST-registered person and on any import of goods into Singapore. The government has also announced that the rate of GST is proposed to be increased from seven per cent to nine per cent between 2022 and 2025. However, certain supplies, including prescribed financial services, are exempt from GST, and GST is chargeable at the rate of zero per cent for exports, as well as on the supply of certain international services. A person is generally required to register for GST, where such person makes, or intends to make, taxable supplies in the course or furtherance of a business exceeding SGD 1m over a 12-month period.

In addition, two new GST regimes have come into effect from 1 January 2020: the reverse charge regime and overseas vendor registration regime. Under the reverse charge regime, a GST-registered person is required to account for GST on the value of imported services provided by a supplier outside Singapore to such person through a business-to-business supply of services to the extent that such services fall within the scope of the reverse charge regime. Under the overseas vendor registration regime, a supplier outside Singapore who has or reasonably expects its global turnover and value of digital services supplies to non-GST registered persons belonging in Singapore for a calendar year or the next 12 months to exceed SGD 1m and SGD 100,000 respectively may be required to register, charge and account for GST on such services.

Chapter 9: Intellectual property

Ong Pei Ching, TSMP Corporation, Singapore

9.1 Patents

A patent is a right granted for the exclusive use of an invention. Patents can be granted in respect of 'patentable inventions', which can be a product or a process for industrial use. 'Patentable inventions' are inventions that are new, involve an inventive step and are capable of industrial application.

9.1.1 Registration and protection in Singapore

To enjoy protection in Singapore, a patent application may be filed directly with the Intellectual Property Office of Singapore (the 'IPOS'), or through the Patent Cooperation Treaty (PCT) National Phase Entry Route.

The PCT is administered by the International Bureau of the World Intellectual Property Organization (WIPO). It facilitates patent filings in multiple countries through a single application with a single office.

The date of the patent application is known as the priority date. Upon the grant of the patent, it will be protected for up to 20 years from the priority date, subject to the payment of annual fees from the fifth year of protection.

If the patent application was filed under the PCT National Phase Entry Route, the priority date will be backdated to the filing date of the foreign application. This applies if the application in Singapore was filed within 12 months from the date of the filing of the earlier foreign application.

Under the Patents Act, a patent can be granted to the inventor or joint inventors. Where there are two or more joint inventors, each inventor will have an equal undivided share in the patent, save for any agreement to the contrary. If the invention was made in the course of an employee's duties, the invention shall be taken to belong to the employer.

It may take about two to four years for a patent to be granted. This depends on the complexity of the invention. The IPOS Registry of Patents has a procedure for a patent to be granted within 12 months if certain requirements are met. These requirements include having the IPOS as the first or second office of filing, and having no deficiencies in the patent's formalities examination.

The IPOS also participates in international work-sharing programmes that accelerate the patent grant process. These include the following:

Patent Prosecution Highway

In this programme, if corresponding or related patent applications for the same invention are filed in the IPOS and a partner intellectual property (IP) office, the IP offices can refer to each other's patent examination results. This will help to expedite the examination process. The IPOS's partner IP offices include those in China, Europe, Germany, Japan, Korea and the US.

Association of Southeast Asian Nations (ASEAN) Patent Examination Cooperation

Nine Association of Southeast Asian Nations (ASEAN) member states are participating in this programme: Brunei Darussalam, Cambodia, Indonesia, Lao People's Democratic Republic (PDR), Malaysia, the Philippines, Singapore, Thailand and Vietnam. In this programme, the member states' respective IP offices share information regarding (among others) their patent search and examination results. This process also allows applicants a fast-track patenting process in the participating IP offices.

9.1.2 Infringement and defences

Patent infringement may occur in a number of ways:

- If the invention is a product, infringement may occur if a party, without the consent of the proprietor, makes, disposes of, offers to dispose of, uses or imports the product, or keeps it whether for disposal or otherwise.
- If the invention is a process, infringement may occur if a party:
  - uses the process or offers it for use in Singapore when he or she knows, or it is obvious to a reasonable person in the circumstances, that its use without the proprietor's consent would be an infringement of the patent; or
  - disposes of, offers to dispose of, uses or imports any product obtained directly by means of that process, or keeps any such product, whether for disposal or otherwise.

There are defences to patent infringement, including if the infringing act:

- was done privately, and not for commercial purposes;
- was done for experimental purposes relating to the subject matter of the invention; or
- consisted of the import, use or disposal of, or the offer to dispose of, any patented product that is produced by or with the consent of the proprietor of the patent granted in any country outside Singapore. This defence pertains to parallel imports.

9.2 Trademarks

A trademark means any sign capable of being represented graphically and that is capable of distinguishing goods or services dealt with or provided or in the course of trade by a person from goods or services so dealt with or provided by any other person. In other words, it is a badge of origin.

9.2.1 Registration and protection in Singapore

To enjoy statutory protection, trademarks may be registered under the Trade Mark Act. Upon registration, the initial length of protection is ten years. The protection may continue perpetually, so long as the registration is renewed for further periods of ten years.

A party can obtain protection of its trademark in Singapore through a domestic filing with the IPOS. Alternatively, if a party files its trademark application in another country, he or she can designate Singapore in an international registration under the Madrid Protocol. The Madrid Protocol is administered by the WIPO, and allows a trademark owner to seek protection of his or her trademark in multiple countries via a single application with a single office. Similarly, a party can file an international trademark application with the IPOS and designate multiple countries under the Madrid Protocol.

It may take about nine months for a trademark to be registered.

Well-known trademarks enjoy special protection under the Trade Mark Act. Many of the remedies available to registered trademarks under the Trade Mark Act apply to well-known trademarks, even if these trademarks are not registered and/or are not used in a business in Singapore.

9.2.2 Infringement and defences

Trademark infringement may occur in a number of ways, including:

- using a sign in the course of trade, without the consent of the proprietor, that is:
  - identical to the registered trademark in relation to goods or services identical to those for which it is registered;
  - identical to the trademark in relation to goods or services similar to those for which the trademark is registered, and is likely to cause confusion on the part of the public; and
  - similar to the trademark in relation to goods or services identical to or similar to those for which the trademark is registered and likely to cause confusion on the part of the public.

Other than civil liability, there may also be criminal liability for trademark infringers.

Registered trademarks may be used by others in non-infringing ways, such as if they are used to indicate the quality or the intended purpose of the goods or services. Fair use of registered trademarks in comparative commercial advertising, use for non-commercial purposes, or use for the purpose of news reporting or news commentary does not amount to trademark infringement.

Further, if a person has been continuously using an unregistered trademark before the date of registration of the registered trademark or before the registered proprietor's first use of the trademark, he or she will not have infringed the registered trademark.

A trader that uses an unregistered trademark may still have recourse under the common law tort of passing-off if another trader uses that unregistered trademark.

To establish passing-off, the claimant must show that: (1) there is goodwill in Singapore; (2) that the defendant has made a misrepresentation that his or her goods or services originate from the claimant, or are otherwise associated with the claimant; and (3) damage resulting from such a misrepresentation.

9.3 Copyright

Copyright is a bundle of property rights over original works or original expressions of ideas.

9.3.1 Protection in Singapore

There is no requirement of registration of copyright in Singapore to enjoy copyright protection.

Works that are protected include literary, dramatic, musical and artistic works, which are known as authors' works, and computer programs. Literary works include a compilation that, by reason of the selection or arrangement of its content, constitutes an intellectual creation. Artistic works include paintings, sculptures, drawings, engravings, photographs, buildings and models of buildings. Dramatic works include choreographic shows and scenarios for cinematograph films.

The Copyright Act also protects entrepreneurial works, namely sound recordings, cinematographic films, television broadcasts and sound broadcasts, cable programmes and published editions of works.

There are three prerequisites for copyright to subsist in an author's work in Singapore: the work must be connected with Singapore, must exist in some material form and must be original.

The central requirement to copyright protection is originality, which requires sufficient intellectual effort on the part of the author. However, artistic merit is not required.

With regard to the requirement for the work to be connected with Singapore:

- If the work is unpublished, it is sufficient if the author was a citizen or resident of Singapore or a member country of the Berne Union or the World Trade Organization (WTO) at the time the work was made.
- If the work is published, it is sufficient if the first publication took place in Singapore or a member country of the Berne Union or the WTO, or if the author was a citizen or resident of these countries when the work was first published.

By default, the author of the work is the copyright owner. However, the Copyright Act provides exceptions such as:

- when a work is commissioned by another, the commissioner rather than the author is the copyright owner; and
- when a work is produced in the course of employment pursuant to the terms of employment, the employer rather than the employee is the copyright owner.

The length of copyright protection varies depending on the type of work in question.

9.3.2 Infringement and defences

Generally, copyright infringement occurs when the protected work is reproduced in whole or in part. There is a nexus between the originality, skill and effort that goes into a work and the substantiality of copying required to establish infringement. The thinner the copyright protection, the more substantial the copying must be before a finding of infringement will be made.

Other than civil liability, there may also be criminal liability for copyright infringers.

There are defences to copyright infringement, including:

- fair dealing for any purpose, including research and study;
- fair dealing for the purpose of criticism or review; and
- fair dealing for the purpose of reporting current events.

9.4 Designs

Designs mean the features of shape, configuration, colours, pattern or ornament applied to any article or non-physical product that give that article or non-physical product its appearance. Under the Registered Designs Act, ‘articles’ are things that are manufactured, whether by an industrial process or otherwise. Thus, the protection provided under the Registered Designs Act is intended to cover designs in articles that are mass produced by a manufacturing process.

9.4.1 Registration and protection

To enjoy statutory protection, designs can be registered under the Registered Designs Act. The design must be new. The test for novelty is with reference to registered designs worldwide. A design will not be regarded as new if it is the same as a design, or differs in immaterial details or variants commonly used in the trade from a design that is:

- registered in respect of the same or any other article, non-physical product or set of articles and non-physical products in pursuance of a prior application; or
- published in Singapore or elsewhere in respect of the same or any other article, non-physical product or set of articles and non-physical products before the date of the first-mentioned application.

The Registered Designs Act has restrictions on registrable designs. Examples of designs that are not registrable include:

- a method or principle of construction;
- features of shape, configuration or colours of an article or a non-physical product that:
  - are dictated solely by the function that the article or non-physical product has to perform ('Functionality Exclusion');
  - are dependent upon the appearance of another article or non-physical product of which the article or non-physical product is intended by the designer to form an integral part ('Must-Match Exclusion'); or
  - enable the article or non-physical product to be connected to, or placed in, around or against, another article or non-physical product so that either article or non-physical product may perform its function ('Must-Fit Exclusion');
- features consisting of one or more colours that:
  - are not used with any feature of shape or configuration; and
  - do not give rise to any feature of pattern or ornament;
- designs that are contrary to public order or morality; and
- computer programs or layout designs of integrated circuits.

Apart from filing a domestic design application at the IPOS, an applicant can file a single design application under the Hague System with the IPOS to register his or her design in multiple countries.

If an applicant has filed an earlier design application in a Paris Convention country or a WTO member country, and files an application in Singapore within six months, he or she can use the earlier filed application to claim priority to the design. This similarly applies to design applications that are first filed in Singapore, in order to claim priority in subsequent applications filed in a Paris Convention country or a WTO member country.

Under the Registered Designs Act, the starting point is that the designer will be treated as the owner of the design. If there is more than one registered owner, each of them will be entitled to an equal undivided share in the rights of the design, subject to any agreement to the contrary. If the design was created in the course of his or her employment, there is a presumption that the employer is the owner of the design.

After registration, a design will be protected for an initial five years from the date of filing. Registration can be renewed every five years thereafter, up to a maximum period of 15 years.

Upon registration, the owner of the design enjoys exclusive rights in Singapore regarding any article in respect of which the design is registered and applied to, including:

- to make, import or use such articles for the purpose of trade or business; and
- to sell, hire, or offer or expose for sale or hire.

9.4.2 *Infringement and defences*

Infringement of a registered design occurs when a person, without the consent of the registered owner:

- does anything that is the aforementioned exclusive right of the registered owner;
- makes anything for enabling any article covered by the exclusive rights to be made in Singapore or elsewhere;
- does anything in relation to a kit that would constitute an infringement of the design if it had been done in relation to the assembled article, where a 'kit' is a complete or substantially complete set of components intended to be assembled into an article; and
- makes anything for enabling a kit to be made or assembled in Singapore or elsewhere, if the assembled article would be an article covered by the exclusive rights.

There are defences to infringement of a registered design. These include instances where the infringing act:

- was done for a private, non-commercial purpose;
- was done for the purpose of evaluation, analysis, research or teaching;
- consisted of the import, sale, hire, or offer or exposure for sale or hire of any article or non-physical product to which the design has been applied, and has been placed on the market, whether in Singapore or elsewhere, with the consent of the registered owner; this defence pertains to parallel imports;
- was done in good faith, and before the date of registration of the design; and
- involves the copying of a design that falls within the Functionality, Must-Match or Must-Fit Exclusions.

9.5 Other

The following statutes give specific IP protection to some other types of work:

- the Layout-Designs of Integrated Circuits Act protects, as the name suggests, the layout designs of integrated circuits;
- the Geographical Indications Act protects indications used in trade to identify goods as originating from a place, with a given quality, reputation or other characteristic of the goods essentially attributable to that place; and
- the Plant Varieties Protection Act protects a new plant group within a single botanical taxon of the lowest rank.

Some works may attract more than one type of IP protection. For example, a new plant group may attract protection under the Plant Varieties Protection Act in addition to the Patents Act.

Chapter 10: Financing

Francis Mok, Allen & Gledhill, Singapore

10.1 Licensing requirements for banks

10.1.1 Licensing requirements for banks

Banks in Singapore are supervised and regulated by the MAS. The MAS is Singapore's central bank and integrated financial regulatory authority for all financial institutions in Singapore. The regulatory framework for banks comprises the Banking Act and the MAS Act and the subsidiary legislation promulgated thereunder, as well as the notices, guidelines, circulars, and practice notes and codes issued by the MAS from time to time (collectively, the 'Banking Regulations').

It is a requirement to hold a bank licence in order to carry on any banking business in Singapore. 'Banking business' comprises deposit taking, the provision of cheque services and lending. Aside from banking business, banks are permitted to carry on most other types of business regulated by the MAS (or business that, if carried on in Singapore, would be regulated or authorised by the MAS), including financial advisory services, insurance broking and capital market services.

Generally, banks are prohibited from engaging in non-financial activities, but may conduct non-financial activities that are incidental to, related to or complementary to the banks' financial businesses.

10.1.2 Types of banks

The MAS currently issues two types of bank licences under the Banking Act: (1) a full bank licence; and (2) a wholesale bank licence.

Full banks may provide the whole range of banking business permitted under the Banking Act, including both SGD and non-SGD-denominated banking business. However, foreign banks with full bank licences are restricted in the number of branches and automated teller machines (ATMs) that they may operate. A small number of foreign full banks have been awarded qualifying full bank privileges, which permit them to operate at more locations, share ATMs among themselves, relocate their sub-branches freely and enter into an arrangement with local banks to let their credit card holders obtain cash advances through the local banks' ATM networks.

Wholesale banks operate within the Guidelines for Operation of Wholesale Banks issued by MAS. They may engage in the same range of banking business as full banks, except that they may not carry out SGD retail banking activities. Wholesale banks are only permitted to maintain one place of business in Singapore.

Besides licensed banks, financial institutions may be approved by MAS under the MAS Act to operate as merchant banks. The scope of activities a merchant bank may undertake is generally narrower than that for licensed banks: merchant banks can only conduct the activities listed in the MAS Guidelines for Operation of Merchant Banks (including asset management and lending in the institutional money markets), and are not allowed to accept deposits or borrow from the public (except from banks, finance companies, shareholders and companies controlled by shareholders).

However, a merchant bank may also apply to MAS for approval to operate an Asian Currency Unit (ACU) for its foreign currency activities, and this enables a merchant bank to compete with licensed banks in the non-SGD banking market. As the operation of an ACU is governed by the Banking Act, where a merchant bank operates an ACU, it would be required to comply with certain requirements in the Banking Act.

In the near future, the regulation of merchant banks will be consolidated into the Banking Act. Amendments to the Banking Act to include a new licensing framework for merchant banks have been passed by Parliament, but have not yet come into operation.

10.1.3 Bank representative office

Bank representative offices are also governed under the Banking Act. Bank representative offices must be registered, and are subject to such conditions of registration as the MAS may impose. Generally, a bank representative office may carry out liaison work, market research or feasibility studies, but is not allowed to transact any business in Singapore.

10.1.4 Licensing process and admission criteria

To apply for a bank licence, an applicant would need to submit prescribed application forms to MAS. Interested applicants are encouraged to contact MAS to discuss the licensing requirements prior to submitting a formal application. MAS usually takes approximately nine to 18 months to approve an application, during which it may ask follow-up questions or request further information on the application.

In assessing an application for a bank licence, MAS will take into consideration the following factors and/or require that the applicant demonstrates the following:

- the financial soundness, track record, world ranking and reputation of the applicant, its parent company and major shareholders;
- the strength of home country supervision, including the willingness and ability of the home supervisory authority to cooperate with MAS, and its framework for cross-border cooperation;
- written consent from the home country supervisory authority for the establishment of a banking operation in Singapore;
- a well thought-out strategy for banking and financial services in Singapore, and sound business plans to ensure sustained economic viability; and
- robust risk management systems and processes that are commensurate with the applicant's size and proposed business.

Applicants must also meet minimum capital requirements prescribed under the Banking Act, as follows:

- Singapore-incorporated full bank: paid-up capital and capital funds of at least SGD 1.5bn;
- Singapore-incorporated wholesale bank: paid-up capital and capital funds of at least SGD 100m; and
- foreign-incorporated full or wholesale bank: head office funds of at least the equivalent of SGD 200m.

A bank in Singapore must continue to comply with the minimum capital requirements and other conduct of business requirements under the Banking Regulations on an ongoing basis. These may include risk-based capital adequacy requirements, minimum leverage ratio requirements and capital liquidity requirements as prescribed by the MAS. In addition, banks in Singapore are also expected to follow industry guidelines issued by the Association of Banks in Singapore.

10.1.5 Digital banks

Apart from the traditional banking model, MAS has established an internet banking framework that allows Singapore-incorporated banking groups to set up banking subsidiaries to pursue new business models, including internet-only banks. Such digital bank subsidiaries require separate full bank licences, and are subject to the same prudential and regulatory framework as traditional banks (eg, the same licensing and admission criteria apply). However, for a banking subsidiary the Singapore-incorporated parent bank of which has already met the SGD 1.5bn capital requirement will be subject to a lower paid-up capital requirement of SGD 100m, provided that the parent bank has control over the subsidiary.

Separately, MAS announced in 2019 that it is prepared to grant up to two digital full bank licences and three digital wholesale bank licences, which will allow non-bank entities to conduct digital banking businesses in Singapore. The application window has closed and MAS is expected to announce the successful applications in the second half of 2020. A digital full bank will be allowed to take deposits from and provide banking services to retail and non-retail customer segments, while a digital wholesale bank may only serve businesses and other non-retail customer segments. Digital full banks will not be allowed to operate ATMs or cash deposit machines (CDM), or join any existing ATM/CDM networks. This is because the objective is for digital banks to adopt innovative digital ways of serving customers and supporting the future digital economy. Digital banks are required to meet the same minimum capital requirements as traditional banks.

Chapter 11: Privacy laws and data protection

Felicia Tan, TSMP Corporation, Singapore

11.1 Privacy laws

In the absence of any explicit provision for the protection of privacy as a fundamental right in Singapore's Constitution, any omnibus privacy legislation in the country's statutes, or any explicit pronouncement by Singapore courts that a *general tort of privacy* exists, the starting point in Singapore is not very different from the common law. The common law does not recognise a *general right* to privacy, but there exists today a framework of common law and statutory torts that collectively protect an individual's privacy. Individuals are therefore able to prosecute their claims for invasions into their privacy by private action before the civil courts much more effectively today than in the past.

While Singapore courts have not recognised the existence of a *general right* to privacy that is an actionable tort, or a fundamental right protected by the Constitution, that is not to say that Singapore's laws do not protect different aspects of privacy. Singapore's Personal Data Protection Act, 2012 (PDPA) protects informational privacy. The PDPA will be discussed in the next section.

Another aspect of privacy is the right to seclusion, which addresses intrusions into a victim's private space or affairs. Singapore has enshrined the tort of harassment, which deals with this aspect of privacy, by enacting the Protection from Harassment Act (Cap 256A) (the 'POHA') in 2014. The POHA also introduced a statutory tort of unlawful stalking.

Other aspects of privacy include the right to prevent the publication of private communication, the right to control the commercial exploitation of one's fame or identity (also sometimes referred to as the right of publicity, or false publicity), and those rights are protected by laws such as the law of breach of confidence, law of passing off, and defamation and malicious falsehood laws.

11.2 Data protection

Personal data in Singapore is protected under the PDPA. 'Personal data' refers to data, whether true or not, about an individual who can be identified from that data, or from that data and other information to which the organisation has or is likely to have access.

The PDPA applies to 'any individual, company, association or body of persons, corporate or unincorporated, whether or not – (a) formed or recognised under the law of Singapore; or (b) resident, or having an office or a place of business, in Singapore'.

The PDPA establishes a data protection law that comprises various rules governing the collection, use, disclosure and care of personal data. It recognises both the rights of individuals to protect their personal data, including rights of access and correction, and the needs of organisations to collect, use or disclose personal data for legitimate and reasonable purposes. In the development of this law, references were made to the data protection regimes of key jurisdictions that have established comprehensive data protection laws, including Australia, Canada, the EU, Hong Kong, New Zealand and the UK, as well as the Organisation for Economic Co-operation and Development (OECD) Guidelines on the Protection of Privacy and Transborder Flow of Personal Data, and the Asia-Pacific Economic Cooperation (APEC) Privacy Framework.

The PDPA continues to be developed to address any gaps in the personal data protection regime. For instance, under the Advisory Guidelines on the PDPA for National Registration Identity Card (NRIC) and Other National Identification Numbers, with effect from 1 September 2019 an organisation may only collect, use or disclose an individual's NRIC number, birth certificate number, foreign identification number or work permit number if it is either required by law, or it is necessary to establish or verify an individual's identity to a high degree of accuracy. This has significantly raised public awareness in Singapore of the importance of personal data, and the country has seen a radical change in how organisations collect, use and disclose personal data.

The PDPA also provides for the establishment of a national Do Not Call (DNC) Registry. The DNC Registry allows individuals to register their Singapore telephone numbers to opt out of receiving marketing phone calls and mobile text messages from organisations.

The PDPA is enforced by the Personal Data Protection Commission (PDPC). The PDPC investigates complaints, and its powers include the power to require the production of documents and information, enter premises with or without warrant for inspection, issue directions for compliance with the PDPA and sanction errant entities. Sanctions include financial penalties and/or imprisonment. The PDPC publishes its decisions relating to organisations that are found to have contravened the data protection provisions under the PDPA and also takes a proactive approach in assisting organisations to comply with the PDPA through conducting outreach activities and issuing advisory guidelines.

In addition to the PDPA, the Singapore data protection regime consists of various other guidelines (which may be general or sector/industry-specific) issued by either the PDPC or other government agencies or commissions. For instance, the Tripartite Alliance for Fair and Progressive Employment Practices (the 'TAFEP') has published several guidelines relating to employment practices, including advisories on the type of information that prospective employers should not take into account during pre-employment checks. The latest in the list would be applicants' mental health conditions. As of January 2020, it is discriminatory to obtain declarations of mental health conditions of job applicants. While such PDPC or TAFEP guidelines are advisory in nature and not legally binding, these guidelines are edifying of the manner in which the relevant commission or agency may interpret the PDPA and data protection laws, and should not be neglected.

An individual has two avenues through which he or she may address his or her concerns of a breach of the PDPA by an organisation. The individual may submit a complaint to the PDPC, or where the individual has suffered loss or damage directly as a result of the contravention, he or she may commence civil proceedings against the organisation under section 32 of the PDPA.

For businesses operating outside Singapore or companies not registered in Singapore, it is important to bear in mind that the PDPA has *extraterritorial* effect, which means it applies to all organisations collecting, using or disclosing personal data in Singapore, whether or not the organisation itself has a physical presence or is registered as a company in Singapore.

The PDPA obligations do not apply to the public sector. Other laws in place criminalise unauthorised disclosure of data by public agencies and their officers, such as the rules under the Government Instruction Manual 8, the Official Secrets Act and the Public Sector (Governance) Act.

Other relatively sector-specific legislation in Singapore that regulates the collection, use and/or disclosure of data by private sector organisations includes, for instance:

- the Banking Act, which prohibits the disclosure of customer information by a bank or its officers;
- the Computer Misuse and Cybersecurity (Amendment) Act, 2017, which criminalises unauthorised access or modification to computer systems, thus dealing with (though not limited to) computer system hackers;
- the Electronic Transactions Act regulates the security and use of electronic transactions; and
- the Telecom Competition Code issued under the Telecommunications Act requires licensees under the act to take reasonable measures to prevent the unauthorised use of end-user service information.

Chapter 12: Competition law

Daren Shiau, Allen & Gledhill, Singapore

12.1 Introduction

The Competition Act is the principal statute governing the competition law regime in Singapore. The provisions of the Competition Act are administered by the Competition and Consumer Commission of Singapore (CCCS).

The CCCS is the most active competition regulator in the ASEAN region, leading in cartel and dominance investigations, as well as the calling-in and investigating of mergers with an effect in Singapore.

12.2 Cartel regulation

12.2.1 Application

Section 34 of the Competition Act prohibits agreements between undertakings, decisions by associations of undertakings or concerted practices that have as their object or effect the prevention, restriction or distortion of competition within Singapore (the 'Section 34 Prohibition').

The term 'agreement' in the Section 34 Prohibition covers both legally enforceable and non-enforceable agreements, including informal understandings and gentlemen's agreements.

12.2.2 Prohibited matters

Under the Competition Act, agreements, decisions or concerted practices that may have the object or effect of preventing, restricting or distorting competition within Singapore include:

- directly or indirectly fixing purchase or selling prices, or any other trading conditions;
- limiting or controlling production, markets, technical development or investment;
- sharing markets or sources of supply;

- applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage; or
- making the conclusion of contracts subject to acceptance by the other parties of supplementary obligations that, by their nature or according to commercial usage, have no connection with the subject of such contracts.

As set out in the CCCS Guidelines on the Section 34 Prohibition, other typically prohibited activities include: bid-rigging (collusive tendering); joint purchasing or selling; sharing information; exchanging price and non-price information; restricting advertising; and setting technical or design standards.

The CCCS takes a hard-line approach to information exchange between competitors. A passive mode of participation in a discussion or the fact that an undertaking does not act on the confidential information received does not relieve the undertaking of liability under the Section 34 Prohibition, unless it has publicly distanced itself from the anti-competitive discussion.

12.2.3 Vertical agreements

Pure vertical agreements are excluded from the Section 34 Prohibition. Pure vertical agreements are narrowly defined as agreements between parties who operate at a different level of the production or distribution chain and relating to the conditions under which the parties may purchase, sell or resell certain products.

However, a vertical relationship and/or having a diagonal agreement does not preclude the finding of a concerted practice that infringes the Section 34 Prohibition, for example agreements of a hub-and-spoke nature. In addition, vertical agreements are not excluded from the Section 47 Prohibition.

12.2.4 Infringement decisions

To date the CCCS has issued three international cartel decisions concerning the freight forwarding industry, the machinery and industrial equipment industry, and the industry for electronic circuitry components. The CCCS has also conducted dawn raids and investigations within and outside Singapore in a wide range of industries, including the autoparts, consumer electronics, financial services, fast-moving consumer goods (FMCG), logistics, petrochemicals, precision manufacturing and shipping industries.

12.3 Abuse of dominance

12.3.1 Application

Section 47 of the Competition Act prohibits any conduct on the part of one or more undertakings that amounts to the abuse of a dominant position in any Singapore market (the ‘Section 47 Prohibition’). In assessing whether the Section 47 Prohibition applies, a two-stage test is applied: (1), whether the undertaking is dominant in the relevant market; and (2), whether it is abusing that dominant position.

12.3.2 Definition of 'dominance'

An undertaking will be dominant for the purposes of Singapore competition law if it has substantial market power. Market power arises where an undertaking does not face sufficiently strong competitive pressure and can be thought of as the ability to profitably sustain prices above competitive levels or to restrict output or quality below competitive levels. Generally, as a starting point, the CCCS will consider a market share above 60 per cent as likely to indicate that an undertaking is dominant in the relevant market. However, the CCCS has indicated in its Guidelines on the Section 47 Prohibition that this starting point does not preclude dominance being established at a lower market share. This position has been taken by the CCCS in *Re Abuse of a Dominant Position by SISTIC.com Pte Ltd* [2010] SGCCS 3 and upheld by the Competition Appeal Board in *Re Abuse of a Dominant Position by SISTIC.com Pte Ltd* [2012] SGCAB 1.

Market definition is also relevant in the assessment of whether an undertaking is dominant. In this regard, the extent to which there are constraints on an undertaking's ability to profitably sustain prices above competitive levels will be considered. Such constraints include the extent of existing and potential competition and other factors, such as the existence of powerful buyers and economic regulation.

12.3.3 Definition of 'abuse'

It is noteworthy that the Section 47 Prohibition also applies to undertakings in a dominant position outside Singapore that abuse their dominant position in a market in Singapore. The Section 47 Prohibition will apply where the conduct is engaged in by entities that form a single economic unit, where that single economic unit is dominant in a relevant market. Collective dominance can also be established between two or more economic entities that are legally independent of each other. Under the Competition Act, conduct may constitute an abuse if it consists of:

- predatory behaviour towards competitors;
- limiting production, markets or technical development to the prejudice of consumers;
- applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage; or
- making the conclusion of contracts subject to acceptance by the other parties of supplementary obligations that, by their nature or according to commercial usage, have no connection with the subject of the contracts.

Other categories of conduct that may amount to abuse include pricing below cost, certain discount schemes, certain cases of price discrimination, margin squeezes, vertical restraints, exclusive purchasing agreements, refusals to supply and refusals to allow access to an essential facility.

12.3.4 Notification

An undertaking that is unsure whether its agreement, decision or conduct infringes the Section 34 and/or Section 47 Prohibitions may notify the CCCS either for guidance or a decision. Generally, the

CCCS will take no further action once it has provided guidance or a decision unless certain matters are brought to its attention, such as complaints from third parties.

The fast-track procedure for cases involving the Section 34 and/or Section 47 Prohibition allows businesses under investigation to enter into an agreement with the CCCS where the business will admit its liability early by acknowledging its participation in an anti-competitive activity. In return, it will receive a reduction on the financial penalty to be imposed.

12.4 Merger control

12.4.1 Application

Section 54 of the Competition Act prohibits mergers (including the creation of full-function joint ventures) that result, or may be expected to result, in a substantial lessening of competition within any market for goods or services in Singapore (the 'Section 54 Prohibition'). The Section 54 Prohibition may apply even where a merger party is located outside Singapore, so long as the merger has effect on any market in Singapore.

12.4.2 Notification

The CCCS requires all merger parties to conduct a mandatory self-assessment on whether a merger filing is necessary. A merger control filing to the CCCS is expected and advisable if the findings of the self-assessment are that the merger exceeds the quantitative thresholds.

In considering whether to notify a merger in Singapore, merger parties and their advisors should be aware of the following features of Singapore's risk-based merger control regime:

- the CCCS has an active market intelligence function keeping markets under review to ascertain which M&As are taking place and not notified to the CCCS;
- there are no jurisdictional safe harbours where mergers that do not trigger specified quantitative thresholds are exempt or excluded from the Section 54 Prohibition;
- in the absence of a merger notification, parties bear an evergreen antitrust risk; and
- where the CCCS investigates, the CCCS would already have formed its theories of harm, and the burden of proof will be on the merger parties to demonstrate why the CCCS is wrong.

In addition, the recent CCCS decision in CCCS Case No 500/001/18 – *Grab/Uber* in 2018 provides two significant risks that undertakings ought to take note of:

- undertakings that have conducted a self-assessment may still be found to have intentionally or negligently infringed the Section 54 Prohibition if they proceed to close a transaction without notifying the CCCS: despite the parties in *Grab/Uber* having conducted a self-assessment, the CCCS disagreed with the findings of the self-assessment and found that the parties had intentionally or negligently infringed the Section 54 Prohibition by failing to notify the transaction; and

- the CCCS may reject undertakings' post-completion merger control filings and instead conduct an investigation: while the Singapore merger control regime allows for post-completion merger control filings, the CCCS prefers pre-completion filings and may reject post-completion filings or call-in unnotified transactions, opting instead to investigate the merger.

The CCCS has stated that if a merger results in the indicative quantitative notification thresholds (the 'Quantitative Thresholds') being crossed, the CCCS is likely to give further consideration to the merger before being satisfied that it will not result in a substantial lessening of competition. The Quantitative Thresholds are:

- a post-merger combined market share of the three largest firms of at least 70 per cent and the merged undertaking has a market share of at least 20 per cent; or
- a merged undertaking with a market share of at least 40 per cent.

The CCCS may also, and as a matter of practice does, call-in and investigate transactions that fall below the Quantitative Thresholds. The test as to the existence of a substantial lessening of competition is qualitative rather than quantitative. Qualitative factors include the ease and speed of supply-side substitution, countervailing buyer power, market transparency and cost stability in the market. In particular, the CCCS has also investigated transactions six years after the transaction was completed.

The CCCS has, to date, issued one infringement decision for a completed transaction, and issued four provisional decisions to block transactions. The rapid succession of merger decisions by the CCCS in the past few years requiring commitments, in addition to prohibition of transactions, signals its increasingly aggressive enforcement towards merger control. The CCCS has also been stepping up its enforcement of gun-jumping, specifically, information sharing prior to the consummation of a merger, and ancillary restrictions, such as non-compete obligations and supply restrictions, in the merger context.

12.5 Consequences of infringement

If the CCCS decides that there has been an infringement of any of the above prohibitions, it may direct that the infringement be brought to an end and, where necessary, specify a particular course of action to eliminate the harmful effect of the infringement and prevent its recurrence. To illustrate, the CCCS has, pursuant to its merger control powers, issued three proposed decisions to block a merger and accepted commitments in six merger decisions to date.

In addition, if the CCCS is satisfied that the infringement has been committed intentionally or negligently, it may impose a financial penalty of up to ten per cent of the Singapore undertaking's turnover for each year of infringement, up to a maximum of three years. The financial penalty is calculated based on the relevant turnover for the financial year preceding the date when the undertaking's participation in the infringement ended.

Chapter 13: Dispute resolution

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13.1 Structure of the courts

13.1.1 Introduction

Singapore's legal system is consistently ranked highly by both regional and international bodies. Singapore's excellent dispute resolution services are not confined to the judiciary. In the 2007 UK House of Lords case of *West Tankers v RAS Riunione Adriatica di Sicurta SpA* [2007] UKHL 4, Lord Hoffmann stated in his judgment that Singapore stands as one of the world's 'leading centres of arbitration'.

13.1.2 Litigation

COURT STRUCTURE

The legal profession in Singapore is fused as lawyers are not divided into barristers and solicitors. The civil court structure comprises two tiers: the Supreme Court and the state courts.

The principal courts under the state courts are the Magistrates' Courts and District Courts. The Magistrates' Courts generally hear disputes in which the amount claimed or the value of the subject matter in dispute does not exceed SGD 60,000. The District Courts generally hear cases where the amount claimed or the value of the subject matter in dispute does not exceed SGD 250,000. The state courts also consist of specialised courts that deal with specific types of claims. For example, Small Claims Tribunals provide a quick and inexpensive forum for the resolution of small claims that fall within certain categories, such as disputes arising from contracts for the sale of goods or the provision of services. Employment Claims Tribunals provide a speedy and low-cost forum for the resolution of employment-related disputes within prescribed claim limits.

The Supreme Court comprises the High Court and Court of Appeal. The High Court consists of the Chief Justice and the Judges of the High Court, while the Court of Appeal consists of the Chief Justice and the Judges of Appeal. The High Court has original jurisdiction to hear disputes where the amount claimed or the value of the subject matter in dispute is greater than that which the state courts have jurisdiction to hear. The High Court also hears appeals from District Courts and Magistrates' Courts. The Court of Appeal hears appeals from the High Court.

In January 2015 the SICC was launched as a division of the High Court. The SICC is designed to deal with transnational commercial disputes where the claim in the action is of an international and commercial nature. It addresses the increase in commercial litigation in Singapore, such as cross-border commercial disputes governed by foreign law.

Trial process

With a view to improving the efficiency of court proceedings, Singapore became the first country in the world to introduce a compulsory, nationwide paperless court filing system in 2000. The electronic filing system made provision for documents to be filed, served, delivered or otherwise conveyed using electronic service. In January 2013 an integrated electronic litigation system (eLitigation) was launched as an enhanced version of the electronic filing system to provide law firms and court users with an integrated platform for the filing and service of court documents, and active management of case files throughout the litigation process. In addition, Singapore courts actively manage cases with a focus on the expeditious conduct of claims. Pre-trial conferences are scheduled shortly after the commencement of proceedings for parties to update the court on the proceedings' status and for the court to set timelines. As a result, it is not uncommon for a trial to be concluded within six to 12 months of proceedings being commenced.

Enforcement of foreign judgments

It is worth noting that a judgment creditor who has obtained a judgment from a foreign court may enforce that judgment in Singapore by a suit on a debt under the traditional common law position, or pursuant to statute, provided that the relevant criteria for enforcement have been fulfilled.

One such key statute is the Choice of Court Agreements Act, which entered into force on 1 October 2016. This act implements the Convention on Choice of Court Agreements concluded at The Hague on 30 June 2005. Among other things, the Convention requires contracting states to recognise and enforce judgments of the courts of other contracting states designated in exclusive choice of court agreements in international civil or commercial cases, subject to the exceptions in the Convention. The Convention counts Singapore, Mexico and all the EU member states (except Denmark) among its contracting parties. Under the act, the foreign judgment will be generally recognised and enforced if it has effect and is enforceable in the state in which the judgment originated. This development also strengthens Singapore's position as a dispute resolution hub in Asia by enhancing the international enforceability of Singapore court judgments.

13.1.3 Expert determination

Expert determination is a means by which parties to a contract instruct a third party to decide an issue. The third party is ordinarily an expert chosen for their expertise in relation to the issue between the parties. Singapore courts have decided that where the expert's determination has been agreed between the parties as final, that expert's determination will be binding on them. This dispute resolution tool has proven very useful in shipping cases, particularly when highly technical matters are at issue.

13.2 Use of arbitration

13.2.1 Arbitration

Singapore courts encourage the use of arbitration as a means to resolve disputes and this is evidenced by the fact that they recognise arbitration agreements and have stayed legal proceedings because of such agreements. Statutory rules have been enacted in the form of the Arbitration Act (which deals with domestic arbitration), as well as the International Arbitration Act (which deals with international arbitration) to provide for the said stay of legal proceedings in such cases.

The legislative framework concerning arbitration in Singapore has been frequently revisited by the Singapore government (amendments were made in 2010 and 2012) in order to ensure that the arbitration regime is on par with other jurisdictions and that Singapore remains an attractive venue for arbitration.

The SIAC was established in July 1991 as a not-for-profit, non-governmental organisation to meet the demands of the international business community for a neutral, efficient and reliable dispute resolution institution in Asia. The SIAC comprises a Court of Arbitration, which oversees the case administration and arbitral appointment functions of the SIAC; and the Board of Directors, which oversees its corporate and business development functions. On 30 December 2016 the SIAC announced the official release of the first edition of the Investment Arbitration Rules of the Singapore International Arbitration Centre, a specialised set of rules to address the unique issues present in the conduct of international investment arbitration. The SIAC Investment Arbitration Rules 2017 came into effect on 1 January 2017.

In addition, an arbitration facility centre (Maxwell Chambers) was launched in 2010 with the government's support. There are many arbitration bodies represented in Singapore, such as the International Court of Arbitration of the International Chamber of Commerce (ICC), the International Centre for Dispute Resolution (ICDR) (the international division of the American Arbitration Association (AAA)), the Arbitration and Mediation Centre of the WIPO, the Singapore Chamber of Maritime Arbitration (SCMA) and the Singapore Institute of Arbitrators.

Further strengthening Singapore's attractiveness as an arbitration hub is the fact that Singapore is a signatory to the New York Convention, affording ease of enforcement of arbitral awards. The judiciary has also consistently delivered pro-arbitration decisions with a policy of minimal curial intervention.

In *Aloe Vera of America, Inc v Asianic Food (S) Pte Ltd & Anor* [2006] 3 SLR(R) 174, the Singapore court expressly opined that the courts should give effect to foreign arbitration awards.

The Civil Law Act was amended on 1 March 2017 to enact a framework for third-party funding in Singapore, providing businesses with an additional financing option for international arbitration. Third-party funding is already available in other international arbitration centres and its introduction in Singapore strengthens the country's position as a key arbitration seat in the world. Entities that provide third-party funding must meet certain specific criteria set out in regulations.

13.3 Other forms of dispute resolution

13.3.1 Mediation

Mediation forms a part of Singapore's full suite of dispute resolution services, one which serves to complement court litigation and arbitration. It is cost-effective, flexible and fast. Mediation services are offered by the Singapore Mediation Centre (SMC) and the Singapore International Mediation Centre (SIMC), as well as the State Courts Centre for Dispute Resolution (SCCDR).

The Singapore International Mediation Institute (SIMI) and the SIMC were officially launched on 5 November 2014 with a view to develop Singapore into a centre for international commercial mediation. As a professional standards body for mediation, the SIMI implements and maintains a credentialing scheme for mediators, and audits and ensures that high standards are met with registered partners who run training and/or mediation services.

The SIMC focuses on mediating international commercial disputes with a panel of internationally respected mediators. The SIMC has signed Memoranda of Understanding with other mediation centres in the region to promote and develop mediation in Asia.

The SMC focuses on domestic commercial mediation, and also provides other dispute resolution services, such as adjudication. The SMC has a panel of highly qualified mediators and neutrals, which includes retired Supreme Court Judges, Members of Parliament, former Judicial Commissioners, Senior Counsel, and leaders from different professions and industries.

The SCCDR employs a judge-led court dispute resolution process to ensure that cases in the state courts are managed robustly. In addition to judge-led case management, the SCCDR also conducts neutral evaluation, judicial mediation and conciliation to facilitate the resolution of disputes without trial.

On 1 November 2017 the Mediation Act came into force. The Mediation Act strengthens the enforceability of mediated settlements in providing a legislative framework for mediation. It also provides much-valued certainty for cross-border mediation users in areas where the common law position is unclear or differs from jurisdiction to jurisdiction.

The Mediation Act allows parties to apply to court to have their settlement agreement recorded as a court order in order to strengthen its enforceability. It also provides that communications made in mediation cannot be disclosed to third parties to the mediation and cannot be admitted in court or arbitral proceedings as evidence, except under the circumstances set out in the Mediation Act. For example, a person may disclose a mediation communication to a third party to the mediation if the disclosure is made with the consent of all the parties to the mediation (including the maker of the communication). The Mediation Act also allows parties to apply to court to stay ongoing court proceedings in relation to the same dispute.

On 7 August 2019 a treaty to facilitate the enforcement of settlement agreements that have been entered into with the assistance of mediation was signed. This is known as the UN Convention on International Settlement Agreements Resulting from Mediation (the 'Singapore Convention on Mediation'). To date, 52 countries have signed the Singapore Convention on Mediation, which will come into force on 12 September 2020, following the deposit of the instruments of ratification by Fiji, Qater and Singapore.

The Singapore Convention on Mediation seeks to promote the use of mediation as a key means to resolve commercial disputes more amicably, quickly and cost-effectively. Where a written settlement agreement is entered into between two or more parties who have their place of business in different states that have acceded to or ratified the Singapore Convention on Mediation, the party seeking enforcement may apply directly to the courts of the state where the assets are located. This obviates the need of first obtaining judgment on the dispute before being able to seek enforcement.

In addition, the enforcement procedure is simple. The party seeking enforcement need only provide the following to the relevant authority in the state where enforcement is sought:

- a copy of the signed settlement agreement; and
- evidence that the settlement agreement resulted from mediation.

To give effect to the convention, the Singapore Convention on Mediation Act, 2020 was enacted to provide the legislative framework for a party to enforce or invoke an international settlement agreement in Singapore. This will come into force on 12 September 2020.

South Korea

Chapter 1: Introduction

Chris Chang Hyun Song, Shin & Kim, Seoul

South Korea has been a hot spot for foreign investors and has shown great resilience in its economic performance during the past few decades. The GDP in South Korea expanded approximately two per cent year-on-year in 2019, and the combined export-and-import trading volume has exceeded $1tn for three consecutive years since 2017, despite escalated trade tensions between the US and China, the North Korean missile crisis and the unpredictable unfolding of geo-politics in the Asia Pacific region.

During the past three years, the Korean government has eagerly pushed for implementing socio-economic policies under the leadership of President Moon Jae-in. This has inevitably been followed by substantial changes to legislation and legal enforcement practices in South Korea. In light of this, there are some notable developments in South Korea for investors to consider.

Firstly, the Korean government is keeping a closer eye on the overreaching exercise of managerial power by controlling shareholders of certain large business conglomerates; in particular, the failure of respective boards of directors to check and supervise the activities of such controlling shareholders, despite the fact that the majority of such boards are composed of outside directors. Starting from early 2020, the disqualification criteria for outside directors of Korea Exchange (KRX)-listed companies has been greatly expanded and must be publicly disclosed in detail as a way to limit the influence of controlling shareholders over the selection of outside directors. While such measures are expected to help enhance the transparency and soundness of board governance, companies are, to some extent, beginning to worry about a shrinking pool of outside director candidates because those measures are somewhat rigorous and required to be implemented immediately upon the announcement of the relevant legislation. Moreover, the Korean government has been encouraging the National Pension Service and other government-supervised funds actively to monitor and exercise voting rights at general meetings of shareholders of companies in which they hold shares. Since the National Pension Service holds substantial voting shares in many Korean listed companies, its tendency towards the active exercise of shareholder rights would surely affect the dynamics of corporate governance in South Korea.

Secondly,, private equity funds (PEFs) and hedge funds are greatly boosted by an incremental upgrade of laws and guidelines issued by the Korean government. PEFs are a robust player in the Korean M&A markets and a frequent member of buyer consortiums to fund large transactions. In some cases, PEFs are partnering with conglomerate companies to consummate cross-over deals. With deal experience and sophistication accumulated over many years, PEFs are expected to sponsor mega-deal M&As and contribute to the active and stable growth of the M&A markets in South Korea.

Thirdly, while the total amount of overseas investment by Korean companies has greatly exceeded that of inbound investment by foreign companies in recent years, South Korea continues to attract FDI, especially from multinational corporations. South Korea has provided superior infrastructure and resources, such as highly educated skilled workers, relatively cheap electricity bills and a well-established judicial system compared with its competing peer countries. The Moon Jae-in administration has been driving new policies, such as educational reform, to reduce the burden of educational costs for parents; changes to the energy policy towards a lesser dependence on nuclear power; and reshaping judicial bodies by nominating new justices. Investors should closely watch how those policies affect the overall business and legal environment in South Korea.

Further, President Moon's government has assiduously pushed for labour market reform. Two signature policies, among others, are noteworthy. These include the increase of minimum wages from KRW 6,470 in 2017 to KRW 8,590 in 2020, and capping the maximum working hours per week to 52 hours from the previous 68 hours. These policies are controversial, and often criticised for being undue burdens to companies and negatively affecting job growth. Having heard such criticism, the government indicated its intention to slow down the drive. It set a mild annual increase of the minimum wage of 2.9 per cent in 2020 compared with a 10.9 per cent increase in 2019, and proposed alternative working-hour arrangements to alleviate the woes of companies under the 52 working-hour ban. These changes are expected to help boost business activity and thus induce companies to hire more staff for the benefit of the whole nation.

Over the past three years the government has also emphasised higher taxes for individuals with high incomes and profitable companies to fund its social and welfare programmes. While such policies prevail, the government has amended tax codes to reduce the taxes of SMEs. For example, starting from 2020, the scope of deductible liabilities and expenses increased for SMEs and a new incentive for tax credits is allowed for the R&D activity of companies in the material, parts and equipment (MPE) industry. Such an amendment clearly shows the government's policy to further the growth of SMEs and encourage R&D in companies in the MPE industry. It is partly a strategic response to Japan's export embargo of critical industrial materials against South Korea, which has been imposed since 2019 amid diplomatic disputes over the forced labour of Korean workers during the Second World War. As the heads of both countries seem to know that a souring relationship will not help either county, breakthroughs are expected.

Moreover, amendments to three major data laws became effective in July 2020. New amendments allow companies to use more broadly personal data, pseudonymised data and anonymised data, while companies are required to take heightened measures to protect such datasets. Although South Korea has been a leader in IT, semiconductor and 5G industries, with the great potential to develop artificial intelligence (AI) capacity, it oddly lags behind the US and other advanced economies in terms of AI and data science, partly due to strictly set legal limits on the use of personal information. New data laws are expected to promote the growth of the data industry through the encouragement of sharing and utilising data among various entities. Moreover, under the upgraded data protection policy, South Korea is on the right course to receive an adequacy decision (under the GDPR) from the EU.

Also, the Korea Fair Trade Commission (KFTC), which is the country's antitrust authority, has recently been stepping up its enforcement action against market concentration issues. The KFTC carefully reviews merger control and suspicious cartels, and is quite ready to take remedial measures against alleged wrong-doers while diligently coordinating with authorities in other countries. Multinational corporations that have substantial business operations in South Korea should closely follow up with the KFTC's enforcement policies and should report their overseas M&As to the KFTC if such M&As have any potential bearing on the Korean market.

Lastly, many foreign companies now seem increasingly comfortable with adopting Korean laws as governing law and for a Korean court to hear disputes concerning commercial contracts. This trend is fortified by the stable, well-established judicial system, and belief in the high quality and independence of judges. On the other hand, many Korean companies have been accustomed to arbitration procedures, and they are more likely to accept arbitration clauses in contracts with foreign investors. The growing build-up of trust in the dispute resolution system in South Korea will help to encourage foreign investment into and trade with Korean partners.

The spread of Covid-19 at the beginning of 2020 gradually hurt business operations and economic activity in South Korea. The outbreak of the infectious disease has disrupted global supply chains, on which many Korean companies depend, and even caused a partial factory shut-down of some Korean companies. Due to the uncertainty of Covid-19's long-term impact over the business environment, governmental organisations and credit-rating firms have forecast negative growth for South Korea for 2020. As South Korea proved its capability to overcome obstacles and overhauled its system during the Asian financial crisis in the late 1990s, it will surely utilise this challenging moment to reorganise and reshape its governance, labour relations and management practices, and ultimately elevate itself to become a reliable and strengthened business partner of foreign investors.

Chapter 2: General business environment

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'The world's only divided country', '[a] lonely peninsula encircled by four powerful nations: China, Japan, Russia, and the United States', but at the same time, 'the country that achieved the "Miracle on the Han River"'. These phrases refer to the Republic of Korea. South Korea, which had a national per capita income of only $45 in the 1950s, has now seen this figure grow to over $30,000 within 50 years, and today is ranked 12th in the world economic (GDP) rankings. Furthermore, since 2014 Korea has been ranked first in the Bloomberg Innovation Index until just this year (finishing second). People who hailed the growth of Korea's economy as a miracle continue to tout the 'miracle of new investment' going forward. So why did Korea become such an attractive investment destination?

As an investment destination, there are three major advantages enjoyed by Korea.

Firstly, Korea has geographical advantages, which it has carefully exploited for its continued development as a logistics hub for Northeast Asia and Eurasia. South Korea is located in the heart of the Northeast Asian market, which accounts for about 25 per cent of global GDP, lying between China and Japan, two of the world's largest economies. Along with this, Korea has an excellent logistics industry infrastructure, such as Incheon International Airport and Busan Port (both consistently achieving top global rankings), and a 'mega free trade agreement' network signed with 52 countries, making it an ideal investment destination for direct participation in the global market.

Secondly, South Korea is arguably the best 'test bed' market to predict global marketability. Although South Korea is small in territory, it boasts a diverse, savvy and dynamic consumer population of over 50 million that seeks efficiency and makes uniquely quick decisions as proud early adopters.

In practice, leading companies in various fields use the country as a test bed. In particular, global companies in the digital and IT fields, such as Google and Microsoft, actively use South Korea as a test bed for their product launches. This is because 5G, the revolutionary wireless mobile communication network, can be readily accessed anywhere by anyone in the country, and the world's fastest internet speeds are currently found in South Korea.

Thirdly, South Korea has an excellent business infrastructure. In 2019 the World Bank's *Doing Business 2020* ranked South Korea fifth among 190 countries, first among G20 countries and third among OECD countries. As an example of South Korea's business environment, the expansion rate of Starbucks outlets has progressed rapidly compared with other countries, such that the number of directly managed stores reached 1,300 in a very short time (the fifth-highest number globally). A major reason why Starbucks has been able to expand its brand so rapidly is due to South Korea's 'e-government system', which provides government administration tasks to the public quickly by utilising modern information and communication technology. Other reasons for South Korea's sound business environment include its sizeable pool of highly skilled workers, a product of its emphasis on education, and evidenced by high university entrance rates, excellent living conditions marked by safe and orderly cities, convenient transportation infrastructure, accessible residential settings, and affordable rates for food, healthcare and utilities (water and electricity).

On the other hand, because South Korea has achieved phenomenal growth in such a short period of time, the usually rosy portrayal is often marred by intense competition, squabbling among vested interests and discontent about societal ills, particularly wealth inequality. As a result, there are also multiple obstacles for investors to consider, such as corporate regulations and exceedingly worker-friendly regulations aimed at reducing income inequality.

With recent revisions to the labour law, labour costs have risen, and the spectre of increased production costs has similarly risen. While the minimum wage has increased by approximately 33 per cent from 2017 (KRW 6,470) to today (KRW 8,590), at the same time, work hours have been mandatorily reduced, with the 52-hour workweek system in the process of being implemented incrementally based on the number of employees. However, due to the excessive burden such changes are imposing on employers, in particular smaller businesses, it seems that there is considerable room for future policy changes.

Moreover, major legislative and policy changes are increasingly being implemented at breakneck speed. For example, in 2017 the current government suddenly moved governmental policy away from nuclear energy and decisively towards green energy initiatives, and as a result, Korea is now faced with the need to raise electricity rates due to the 'energy conversion policy', which aims to phase out nuclear energy altogether over the next four decades. Most notably, since 2018 the current government has increased the tax burden on large corporations from 22 per cent to 25 per cent, and discussions on further increases are ongoing. In addition, various new regulations are being created in new technological fields, such as 'Industry 4.0'. There is considerable public opposition to such legislative and policy changes, often resulting in sudden reversals due to the government's sensitive reactions to societal opposition (eg, on a single day in 2018, different governmental authorities first banned and then expressed support for cryptocurrency exchanges). Therefore, investors need to be cautious and aware of how such legislation and policies might trend in the future, requiring careful preliminary review by those with expertise and experience in the relevant fields, including those who can help in successfully navigating the country's legal/regulatory framework.

Overall, South Korea has a demonstrably good business environment that is conducive to investment, but there are various factors, such as the regulatory environment and changes in social mood, to bear in mind before deciding whether and how to invest. Risk checks for such factors should be made in advance in order to identify and adapt to the opportunities and threats both currently in place and anticipated going forward. As always, sound preparation with professional support will be key to investor success.

Chapter 3: Business and corporate structures

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Under Korean law, foreign investors may choose from a range of legal entities, including a joint stock company (*chusik hoesa*), limited company (*yuhan hoesa*), limited liability company (*yuhan chaekim hoesa*), general partnership (*hapmyung hoesa*) and limited partnership (*hapja hoesa*).

Among such choices, joint stock companies comprise the vast majority, accounting for over 90 per cent of corporations that filed a corporate tax return in 2018, and as a result, enjoy somewhat of an advantage in terms of general market perception. That said, foreign and domestic investors are increasingly adopting the limited company or the limited liability company due to their distinct characteristics, including exemption from public reporting obligations that normally depend on the size of the relevant company. In particular, the limited liability company, which was introduced in South Korea relatively recently, is increasingly gaining interest from foreign investors – compared with joint stock companies or limited companies – in light of its exemption from public reporting requirements under the Act on External Audit of Stock Companies (the 'Act on External Audit'). Converting one legal entity into another (eg, conversion of a joint stock company into a limited company) is permissible under Korean law, subject to certain conditions and restrictions.

The following is a more detailed explanation of the three types of companies most commonly used by foreign investors.

3.1 Joint stock company (chusik hoesa)

3.1.1 Incorporation

For joint stock companies, investors are free to determine the amount of capital to be invested; however, in order to qualify as a 'foreign investment' under the Foreign Investment Promotion Act (which may enjoy certain benefits, such as tax reductions, cash grants and industrial site support), an investment of at least KRW 100m per investor is required. The overall incorporation procedures for a joint stock company consist of the following: (1) preparation of articles of incorporation (AoI);

(2) election of one or more directors, representative directors and statutory auditors; (3) payment of the subscription price; and (4) registration with the court and the local business/tax office.

3.1.2 Management and statutory auditors

A minimum of one director is required (or if the registered capital is KRW 1bn or more, then a minimum of three directors is required, one of whom includes the representative director), and there are no nationality or residency requirements. A board of directors is only essential if there are three or more directors (in which case the majority rules, in principle). As for the internal statutory auditor (which is different from an external auditor and does not need to be a certified accountant), at least one statutory auditor is required if the registered capital is KRW 1bn or more (or, as an alternative, an audit committee consisting of three or more directors is possible in lieu of the statutory auditor).

3.1.3 Shareholders

A minimum of one shareholder is required, and each share has one vote unless the articles of incorporation provides for shares that are wholly or partially (depending on the matter) non-voting. Shares may be freely transferred unless the articles of incorporation requires the approval of the board of directors of the relevant company (or if no board of directors exists, then the articles of incorporation may require the approval of the shareholders).

3.1.4 Public reporting and audits

The annual balance sheet as approved by the shareholders must be published in accordance with the methods stipulated in the articles of incorporation. External audits are required for: listed companies, companies that desire to be listed in the current or following fiscal year, and companies having total assets or total sales of KRW 50bn or more, or that otherwise satisfy certain criteria under the Act on External Audit.

3.2 Limited company (*yuhan hoesa*)

3.2.1 Incorporation

The incorporation procedures of a limited company are generally the same as those of a joint stock company, although electing a representative director (if so provided in the articles of incorporation) or a statutory auditor is optional. In addition, instead of ‘shareholders’, the investors are known as ‘members’, and instead of ‘shares’, a limited company has ‘contribution units’.

3.2.2 Management and statutory auditors

A minimum of one director is required and there are no nationality or residency requirements. In principle, a director represents the company, but if there are two or more directors, then a representative director should be elected, unless otherwise stipulated in the articles of incorporation. A board of directors for a limited company is not mandatory.

3.2.3 Members

The minimum number of members is one and the members may adopt a written resolution if all members of the company consent (such written resolutions are only permitted for a joint stock company with registered capital of less than KRW 1bn, and only if all shareholders consent). Each contribution unit is counted as one vote, unless otherwise provided in the articles of incorporation. The transfer of contribution units may be restricted if such a restriction is stipulated in the articles of incorporation.

3.2.4 Public reporting and audits

The publication of annual balance sheets is not required. However, due to recent amendments in the Act on External Audit, limited companies are also subject to mandatory audit by an external auditor if they satisfy certain criteria thereunder similar to those applicable to joint stock companies.

3.3 Limited liability company (*yuhan chaekim hoesa*)

3.3.1 Incorporation

The incorporation procedures for limited liability companies are also substantially similar to those of a joint stock company. Like limited companies, instead of 'shareholders', the investors are known as 'members', and instead of 'shares', a limited liability company has 'contribution units'.

3.3.2 Management and statutory auditors

In limited liability companies a minimum of one manager should be elected under the articles of incorporation and assume the role of the representative director. It is noteworthy that a legal entity (as opposed to an individual person) may act as the manager of a limited liability company – something that is not allowed for a director of a joint stock company or a limited company – and both a member and a non-member may act as the manager. In addition, no board of directors and no statutory auditor are required.

3.3.3 Members

The minimum number of members is one and each member has one vote at the meetings of members. A new member may be registered through an amendment of the articles of incorporation, which requires the agreement of all the existing members. Members may not transfer their contribution units without the approval of other members (in particular, if there is any member acting as the manager, then the approval of such a member, and if there is no member acting as the manager, then the approval of all the members), unless otherwise provided in the articles of incorporation.

3.3.4 Public reporting and audits

Limited liability companies are exempt from any mandatory publication of balance sheets and from external audits under Korean law (in particular, the Act on External Audit).

Chapter 4: Private M&A

Sedong Min, Lee & Ko, Seoul

4.1 Restrictions or controls on foreign investment

Foreign investment in South Korean companies is regulated in certain industries, including telecommunications, broadcasting, banking, marine, aviation, agriculture and natural resources. In these sectors, foreign ownership may be restricted in its entirety or allowed only a ceiling percentage, or be subjected to regulatory approval. Foreign investment in a designated defence industry contractor or a company possessing national core technologies may also be subject to regulatory review and approval. As a procedural reporting requirement, foreign investment requires reports to competent government authorities (eg, the Bank of Korea and Korea Trade-Investment Promotion Agency (KOTRA)) or designated institutions (eg, foreign exchange banks) under the Foreign Investment Promotion Act or under the Foreign Exchange Transaction Act.

4.2 Most commonly used acquisition structure

The acquisition of shares is the most common structure for acquisition in South Korea. Business or assets sales and purchases are less common and are generally only used to purchase part of a company's assets or business. Mergers can apply, but are not commonly used in an M&A context between unrelated parties. In general, the share purchase structure is preferred due to its simplicity (ie, execution of a share purchase agreement and delivery of the share certificates between the seller and buyer except consent requirements by change of control provisions), whereas business or asset transfer entails a more complicated closing procedure (eg, registration for the title transfer of assets; obtaining consent for the transfer of liabilities; and reporting or registration for the transfer of permits or licences, and transfer of employees, business contracts, etc).

4.3 Sale via auction process

A sale through an auction process is frequently used in private M&A. The bigger the deal size, the more common it is to use the bidding process. Although there are some variations, the bidding process generally used in South Korea includes: (1) distribution of a teaser and information memorandum; (2) preliminary bid; (3) selection of bidders to participate in the final bid; (4) due diligence by selected bidders; (5) final bid; (6) selection of a preferred bidder; (7) negotiation and execution of the definitive agreement; and (8) closing.

4.4 Key terms of the acquisition agreement

Typical key terms of a share purchase agreement in Korea are: (1) purchase price and advance payment deposit; (2) price adjustment; (3) closing and closing deliverables; (4) representations and warranties (R&W); (5) covenants; (6) conditions to closing; (7) indemnification; (8) terminations; (9) non-competition; and (10) governing law and dispute resolution.

In South Korea, an advance payment deposit is occasionally requested by the seller to secure certainty for deal closing and potential breach of the buyer, and various price adjustment mechanisms are often used (eg, net cash/debt, working capital adjustments, locked box and earn-outs). As the Korean Commercial Code requires the delivery of share certificates for title of shares to be transferred (in the case that the share certificates are issued), the closing procedure usually contains delivery of the share certificates and wiring the purchase price into the seller's bank account.

In terms of R&W of the target company, fairly extensive R&W are usually sought by the purchaser (eg, capitalisation, permits and licences, financial statements, absence of undisclosed material liabilities, compliance with law, taxes, no proceeding, material contracts, insurance, labour issues, and anti-corruption and environmental issues) and specific coverage of R&W is one of the heavily negotiated issues in general. The right to access the target company's books and records and other information before closing is usually requested by the purchaser, which might sometimes raise a 'gun-jumping' issue (especially in a situation of acquisition between competitors).

Relating to indemnification from a breach of R&W, various limitations, such as overall cap, deductible, basket, *de minimis* and time limits, are commonly utilised. The seller's non-competition for a certain period after closing is generally requested by the purchaser. Generally, such a non-compete covenant should be reasonable as to the scope, period and area in consideration of the total circumstances.

Korean law is generally used as the governing law for M&A transactions in the country. A foreign governing law (eg, New York State law) may be selected by the parties; however, irrespective of such a foreign governing law, the mandatory requirements of Korean law, such as the method of transfer of title and regulatory approvals, may apply.

The typical key terms of a business (or asset) transfer are similar to those in a share purchase agreement, except for some differences (eg, transferred assets, liabilities, contracts, permits and licensed employees, and specific transfer methods).

4.5 Anti-competition report and clearance

If an M&A transaction meets certain thresholds, the acquirer must file a business combination report to obtain clearance from the KFTC. In a share purchase transaction involving 20 per cent (15 per cent in the case of a listed company) of outstanding voting shares of a company, the requirement for a business combination report will be triggered if one party to a transaction has total assets/annual turnover equal to or greater than KRW 300bn (including its worldwide affiliates), while the other party has total assets or annual turnover equal to or greater than KRW 30bn (including its worldwide affiliates). The filing of the business combination report is generally required within 30 days from the closing date ('post-closing report'). Nevertheless, if one party to the transaction has total assets or annual turnover equal to or greater than KRW 2tn (including its worldwide affiliates), a per-closing report will be required, in which case, the parties will not be permitted to close the transaction until clearance relating to the report is obtained from the KFTC. In a business or asset transfer, the business combination report requirements and procedure are similar to those in the case of a share transfer transaction, other than the requirements on the purchased business/assets (ie, the purchaser acquires all or a substantial part of the business or assets of the seller; a substantial part is where it: (1) can be operated as an independent business unit, or can cause a significant decrease in the seller's revenue following the transfer; and (2) has a transfer price of at least ten per cent of the seller's total assets, or at least KRW 5bn).

4.6 Employee-related issues

As a matter of law, there is no obligation to obtain consent from employees or labour unions on either a share sale, or an asset or business transfer; *provided, however,* these obligations have not been set out in employment contracts, employment rules or collective bargaining agreements. In the case of a business transfer, employees who work for the transferred business will transfer from the seller to the purchaser unless the employees object to the transfer. Practically, it is necessary to inform the employees of the proposed transfer to ensure they have sufficient opportunity to consider opting out. Even though there is no legal obligation in M&A transactions, employees/labour unions have a tendency to request an M&A bonus (especially in the case where the seller earns huge capital gains from the transfer) in practice, and there are some cases where M&A bonuses have been paid to facilitate the employees' cooperation in due diligence and smooth closing procedures.

4.7 Taxes related to M&A transactions

On a share sale, securities transaction tax is payable by the seller at 0.5 per cent (0.45 per cent from 1 April 2020) of the transfer price. If the seller is a foreign entity with no permanent establishment in South Korea, the purchaser is required to withhold and pay the securities transaction tax on behalf of the seller. Also, if the purchaser acquires more than 50 per cent of the equity of a company holding real estate, a deemed acquisition tax is payable by the purchaser. Tax is calculated as the acquisition proportion of 2.2 per cent of the book value of certain assets (eg, the real estate).

On a business and asset sale, a number of taxes are payable: (1) acquisition tax is payable by the purchaser on the acquisition of certain assets (eg, 4.6 per cent of the purchase price for real estate, but 9.4 per cent of the purchase price for those located in Seoul Metropolitan areas; 3.4 per cent of the purchase price for mechanical equipment; and two percent to seven per cent of the purchase price for vehicles). In addition, the purchaser may also be required to purchase a certain amount of housing bonds, depending on the value of the real estate. If an asset/business sale is a comprehensive business transfer, no VAT is imposed. Otherwise, the seller must collect and pay VAT at ten per cent of the purchase price allocated to the assets subject to VAT, which includes inventory, machinery and equipment, buildings and goodwill. However, land and accounts receivable are not subject to VAT. The buyer is generally able to credit VAT paid against its VAT payable (or obtain a refund if there is a shortfall) when it files a VAT return.

If a seller earns capital gains from the M&A transaction, the seller will be subject to paying taxes (when the seller is a corporate entity, as corporate income tax). However, if the seller is a foreign entity with no permanent establishment in Korea, it is subject to CGT at the lower of 11 per cent of the transfer price or 22 per cent of the capital gains, in each case including surtax. The purchaser is required to withhold and pay such CGT on the seller's behalf, unless the seller is exempt under an applicable tax treaty.

Chapter 5: Foreign investment

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5.1 Foreign investment control/restriction

5.1.1 Forms of foreign investment

ACQUISITION OF INTEREST IN A DOMESTIC COMPANY

The 'acquisition of interest in a domestic company' refers to a foreigner's purchase of interest (eg, stocks or shares) of a Korean company (including a company in the process of being established) or a company run by a Korean national through any one of the following means for the purpose of establishing continuous economic relations with the company through participation in management activities:

- acquisition of newly issued stocks or shares of a Korean company or a company managed by a Korean national; or
- acquisition of existing stocks or shares of a Korean company or a company managed by a Korean national.

To be recognised as a foreign investment, the investment amount should be at least KRW 100m per foreigner and the foreigner should own at least ten per cent of either the total number of voting shares issued by a Korean company (including a company in the process of being established) or an enterprise (eg, a sole proprietorship or corporation) run by a Korean national, or its total equity investment. Also, when a foreign investor of a registered foreign-invested company (ie, a company in which a foreign investor has invested, or a non-profit organisation (NPO) to which a foreign investor has contributed) makes an additional investment, no limit shall be imposed on the investment amount or investment ratio. If there are two or more foreign investors involved, each investor should satisfy the above conditions to be eligible as a foreign investor.

While no exceptions are recognised with regard to the investment amount, some exceptions may apply to the foreign investment ratio. Even if the foreign investment ratio is less than ten per cent with the amount of foreign investment being KRW 100m or more, the investment may be exceptionally recognised as foreign investment in the following case: where a foreign investor dispatches or appoints an executive to the domestic company concerned ('executive' refers to directors, representative directors, unlimited liability partners, statutory auditors or persons corresponding thereto holding the right to participate in important management decisions).

LONG-TERM LOANS

Loans with a maturity of not less than five years (based on the loan maturity prescribed in the first loan contract) made to a foreign-invested company by the following entities are recognised as foreign investment:

- an overseas parent company of the foreign-invested company;
- a certain affiliate company of the overseas parent company;
- a foreign individual investor; or
- a certain affiliate company of a foreign individual investor.

Contributions to an NPO

A contribution to an NPO is recognised as foreign investment when the foreign contribution amount is at least KRW 50m and accounts for at least ten per cent of the total contribution amount; the NPO has independent research facilities in the field of science and technology; and the NPO meets any one of the following conditions:

- the number of research staff members who are full-time employees is five or more persons, consisting of persons with a master's degree or higher in the field of science and technology, or persons with a bachelor's degree in the field of science and technology with a research career of not less than three years; or
- the NPO's business should be classified as 'research and experimental development on natural sciences and engineering' under the Korean Standard Industrial Classification.

Other contributions to an NPO by a foreigner are recognised as foreign investment if they: (1) are not less than KRW 50m; (2) account for ten per cent or more of the total contribution amount; (3) are recognised as foreign investment by the Foreign Investment Committee; and (4) meet one of the following conditions:

- an NPO established for the purpose of the promotion of science, art, medical services or education, and which continues to conduct its business with the objective to develop professionals in the relevant fields and to expand international exchanges; or
- an NPO that is a regional office of an international organisation that engages in cooperative international business between civilians or governments.

5.1.2 Restrictions and prohibitions on foreign investment

Out of a total of 1,196 categories of business listed under the Korean Standard Industrial Classification, foreign investment is not permitted in 61 categories, including public administration, diplomacy and national defence (the 'unpermitted categories of business'). Among the 1,135 categories of business in which foreign investment is permitted, restrictions on the investment ratio apply to 29 categories (the 'restricted categories of business').

Meanwhile, prior authorisation from the Minister of Trade Industry and Energy is required for foreign investment in the form of purchasing the shares of defence industry companies.

Unpermitted categories of business

The categories of business in which foreign investment is not permitted generally have public features. Some of the unpermitted categories of business are as follows:

- postal services, central banking, individual mutual aid organisations, pension funding, administration of financial markets and activities auxiliary to financial service activities;
- legislative, judiciary, administrative bodies, foreign embassies, and extraterritorial organisations and bodies;
- education (eg, pre-primary, primary, secondary, higher education, universities, graduate schools and schools for the disabled); and
- artist, religious, business, professional, environmental advocacy, political and labour organisations.

Restricted categories of business

Some examples of restricted categories of business are as follows:

- nuclear power generation, radio broadcasting and over-the-air broadcasting: prohibited;
- hydroelectric/thermal/solar and sunlight/other power generation: the sum of power plant facilities purchased by foreigners from the Korea Electric Power Corporation or its subsidiaries must not exceed 30 per cent of the total domestic power plant facilities;
- farming of beef cattle, wholesale of meat, publication of newspapers, publication of magazines and periodicals and passenger/freight air transport: permitted where the foreign investment ratio is less than 50 per cent (less than 30 per cent for daily newspapers); and
- news agency business: permitted where the foreign investment ratio is less than 25 per cent.

5.1.3 Acquisition of real estate

With the exception of certain real estate that requires government permission for purchase (eg, land in a military base or a military facility protection area), a foreign individual, foreign corporation, foreign organisation, or a corporation or organisation with foreign shareholdings of 50 per cent or more ('foreign party') may acquire land in Korea by following certain procedures and reporting the acquisition to the appropriate authorities.

Reporting obligations under the Act on Report on Real Estate Transactions, Etc

Where a foreign party has concluded a contract for the acquisition of real estate in South Korea, the contract shall be reported to the relevant *city (Si)* mayor, *county (Gun)* governor or head of the relevant *Gu* office within 60 days of the contract's execution date. However, in the case of real estate sales contracts prepared by a practising licensed real estate agent, such a real estate agent should file the report.

Under the Foreign Exchange Transactions Act, non-resident foreigners must first notify the acquisition of real estate to the head of a foreign exchange bank when bringing in funds for real estate acquisition. Afterwards, the real estate acquisition should be notified to the competent *Si/Gun/Gu* office (the same as reporting obligations under the Act on Report on Real Estate Transactions, etc above) and the transfer of ownership should be registered in accordance with the Act on Report on Real Estate Transactions.

5.2 Foreign exchange control

5.2.1 Capital injection/monetary loan

If a foreign parent company wants to increase the capitalisation of its Korean subsidiary through a capital increase: (1) a change of corporate registration must be filed with the court; and (2) a foreign investment report; and (3) change of foreign-invested company registration (or change of such a report and/or registration, if a foreign investment report has already been filed) must be filed with KOTRA or a foreign exchange bank.

If a foreign parent company wants to provide a loan to its Korean subsidiary with a maturity period of five years or longer, a foreign investment report must be filed with KOTRA or a foreign exchange bank (as stated above). Any other type of monetary loans to a Korean subsidiary or a Korean branch office requires the filing of a report of the borrowing of foreign currency funds with a designated foreign exchange bank, but if the amount of borrowing exceeds $30m (including the aggregate amount of borrowing during the period of one year prior to the date of the report), such a report must be filed with the Minister of Strategy and Finance via a designated foreign exchange bank.

5.2.2 Repatriation of funds/payment of dividends

With regard to: (1) proceeds from shares acquired by a foreign investor; (2) proceeds from the sale of shares; and (3) the principal, interest and service charges paid in accordance with the loan contract as prescribed by the Foreign Investment Promotion Act, their remittance to foreign countries shall be guaranteed in accordance with the details of the notified or authorised foreign investment at the time when the said remittance is made.

With regard to loans from a foreign parent company to a Korean subsidiary, the Korean subsidiary may pay the principal and interest back to the foreign parent company upon showing that the reporting requirements pursuant to the Foreign Investment Promotion Act or the Foreign Exchange Transactions Act had been fulfilled at the time of the initial loan transaction.

5.2.3 Settlement of funds in local/foreign currency

The payment currency for ordinary transactions between residents and non-residents (ie, agreements for trade in goods or services) may be decided by agreement between the parties. However, the payment currency for capital transactions (eg, cash loans or stock purchases) must be in accordance with the submission filed with and approved by either the Ministry of Strategy and Finance, the Bank of Korea or the relevant foreign exchange bank.

5.3 Applicable tax incentive or grant

5.3.1 Types of business that can benefit from tax incentives

Type A businesses are:

1. businesses accompanying new growth driver industry technology;
2. companies in a foreign investment zone, which is separately designated upon the individual requests of foreign investors; and
3. companies in areas that have undergone deliberation and received approval by the relevant government committees, such as FTZs, the Saemangeum project area, the Jeju advanced science and technology complexes, and the Jeju investment promotion zone.

Type B businesses are:

1. businesses in free economic zones and those in the Saemangeum project area, which satisfy certain criteria (eg, type of business and investment amount) stipulated under the Restriction of Special Taxation Act and its Enforcement Decree;
2. free economic zone development project entities and development project entities in the Saemangeum project area, which exceed a threshold investment amount or ratio stipulated under the Restriction of Special Taxation Act and its Enforcement Decree;
3. development project entities in the Jeju investment promotion zone, which exceed a threshold investment amount or ratio under the Restriction of Special Taxation Act and its Enforcement Decree;
4. companies in a foreign investment zone (complex type), which satisfy certain criteria under the Restriction of Special Taxation Act and its Enforcement Decree (eg, type of business and investment amount);
5. companies in an enterprise city development zone, which satisfy certain criteria under the Restriction of Special Taxation Act and its Enforcement Decree (eg, type of business and investment amount);
6. development project entities in enterprise city development projects, which exceed a threshold investment amount or ratio stipulated under the Restriction of Special Taxation Act and its Enforcement Decree; and
7. manufacturing businesses (investment amount: US$1m or more) and logistics businesses (investment amount: US$5m or more).

5.3.2 *Tax reductions and exemptions*

Corporate income tax

Corporate income tax reduction/exemption for foreign investment was repealed in 2019 (however, customs duty and local tax reduction/exemption are still in effect), and applies only to foreign-invested companies that applied for corporate income tax reduction/exemption on or before 31 December 2018.

Local tax

With regard to property acquired or held by a foreign-invested company, in order to engage in a business entitled to tax reduction or exemption, local tax is reduced or exempted, or deducted from the tax base as follows.

For Type A:

- acquisition tax and property tax: the amount calculated by multiplying the computed tax amount on the properties concerned by the foreign investment ratio (tax amount subject to reduction or exemption) shall be exempted for five years from the date of commencing business, and reduced by 50 per cent for two years thereafter; and
- property tax on land: the amount calculated by multiplying the tax base of the properties concerned by the foreign investment ratio (tax amount subject to reduction or exemption) shall be deducted from the tax base for five years from the date of commencing business, and 50 per cent of the amount shall be deducted from the tax base for two years thereafter.

For Type B:

- acquisition tax and property tax: the amount calculated by multiplying the computed tax amount on the properties concerned by the foreign investment ratio (tax amount subject to reduction or exemption) shall be exempted for three years from the date of commencing business, and reduced by 50 per cent for two years thereafter; and
- property tax on land: the amount calculated by multiplying the tax base of the properties concerned by the foreign investment ratio (tax amount subject to reduction or exemption) shall be deducted from the tax base for three years from the date of commencing business, and 50 per cent of the amount shall be deducted from the tax base for two years thereafter.

Customs duties, etc

Under the Restriction of Special Taxation Act, customs duties, individual consumption tax and VAT are exempted for the following capital goods that are used directly in a business that is subject to reduction or exemption of corporate income tax or income tax, and are notified as foreign investment through the acquisition of newly issued stocks or shares:

- capital goods brought in by a foreign-invested company in exchange for a foreign or domestic means of payment it obtained as equity investment from a foreign investor; or
- capital goods that are brought in by a foreign investor as an object of investment.

The above exemptions shall only be applied to capital goods for which an import declaration under the Customs Act has been completed within five years of the date on which the foreign investment notification was filed.

For businesses falling under Type A, customs duties, special excise tax and VAT shall be exempted. For businesses falling under Type B (excluding categories (5) and (6) under Type B in section 5.3.1 above), only customs duties will be exempted.

5.3.3 Cash grant

For foreign investment that satisfies certain conditions, the central and local governments of South Korea may provide cash grants for certain purposes, such as the establishment of a factory. The Korean government takes into account various factors, including the following: whether the relevant foreign investment involves new growth driver industry technology; the effect of technology transfer; the scale of job creation; whether the foreign investment overlaps with domestic investment; and the ownership of the location in which the foreign investment is to be made.

QUALIFICATIONS

Foreign investment with a ratio of 30 per cent or higher falling under one of the following is eligible for a cash grant:

- where a new factory is installed or an existing factory is expanded (or a business establishment in the case of a non-manufacturing business) for the management of a business accompanying new growth driver industry technology;
- where a new factory is built or an existing factory is expanded for the production of parts and materials stipulated under the Act on Special Measures for the Promotion of Specialised Enterprises, etc for materials and components that satisfy one of the following conditions:
  - parts and materials that contribute significantly to the added value of the final product;
  - parts and materials that require advanced technology or core high technology and have a high technology spillover effect or create significant added value; or
  - parts and materials that act as the basis of an industry or have high inter-industry linkage effects;
- where a foreign-invested company that creates new jobs in excess of a certain number opens a new factory (a business establishment in the case of non-manufacturing businesses) or expands an existing factory;
- where a research facility is newly opened or expanded for R&D activities for a business accompanying new growth driver industry technology, or where an NPO receiving a contribution

that is considered FDI newly establishes or expands a research facility. The research facility should have five or more full-time researchers with a master's degree in a relevant field or a bachelor's degree in a relevant field supplemented with at least three years of research experience; or

- where an investment that makes significant contributions to the domestic economy relative to the amount of investment meets one of the following conditions and is recognised by the Foreign Investment Committee as an investment that needs support in regard to the qualifications required for foreign investors:
  - where a foreign company establishes a regional headquarters having control over two or more countries in Korea (the regional headquarters should hire ten or more employees, invest KRW 100m or more, and obtain the recognition of the Foreign Investment Committee); also, the parent company's stake should be at least 50 per cent and the parent company's average annual sales for the past five years should be KRW 3tn or more (alternatively, the Foreign Investment Committee must determine that the parent company is a leading company in the global market upon considering factors such as its asset size and global market share); or
  - where a foreign company is engaged in a regional strategic industry as stipulated in Article 2(iv) of the Special Act on Balanced National Development or a regional leading industry stipulated in Article 2(v) of the same act, and where it is recognised that the relevant industry will contribute to the development of the local economy.

Maximum amount of a cash grant

The maximum amount of a cash grant shall be decided by a committee comprised of five or more persons from the central government, local government, KOTRA and the private sector. The cash grant amount shall be decided within the maximum amount through negotiations with the foreign investor.

Usage of cash grant

A foreign-invested company should use a cash grant only for the following purposes:

- to purchase or lease land or a building for the installation of a factory or research facility;
- to construct a factory or research facility;
- to purchase capital goods and research equipment to be used in a factory or research facility for business or research purposes;
- to install infrastructure facilities, including power/communication facilities, required for building a factory or research facility; or
- employment subsidies or education and training subsidies.

Chapter 6: Restructuring transactions

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This chapter seeks to provide a general overview of the following transaction structures, which are frequently utilised in restructurings in South Korea: merger, business transfer, spin-off, liquidation and sale of shares.

6.1 Merger

6.1.1 Overview

Similar to many other jurisdictions, a merger in Korea is effected such that one of the merged companies survives, and all assets and liabilities of the counterparty company are comprehensively transferred to the surviving company by operation of law.

In general, a merger is effected through: (1) a resolution of the board of directors and the GMS; (2) the execution of a merger agreement; (3) the exercise of appraisal rights by dissenting shareholders; (4) a one-month creditor protection procedure; (5) the GMS at which the merger is reported to the shareholders; and (6) the registration of a merger. The timeline for the entire process varies, but in general takes approximately two months for unlisted, private companies.

6.1.2 Transfer of legal relationships

In a merger all rights and obligations of the merged company are automatically transferred, without consent or a separate transfer process, to the surviving company by operation of law. However, if any contract of the surviving or the merged company provides for a consent right or a default (or termination) in respect of the merger, the consent of the contract counterparty would be required for the merger to proceed without breach of the relevant contract.

In principle, permits and licences are also automatically transferred to the surviving company. However, the relevant laws and regulations, or the permit or licence registration requirements, may require the transfer of permits or licences from the merged company to the surviving company to be reported and registered with the relevant authority.

6.1.3 Creditor protection procedure

Following the resolution and approval of the merger by the board of directors and shareholders of the surviving and merged companies, individual and public notices are required to be provided to creditors of the merger parties, and the creditors have the right to file an objection and receive repayment or collateral in respect of their claims against the merger companies for at least one month.

In practice, the merger companies typically discuss and commercially resolve the claims of potential objecting creditors prior to the statutory one-month creditor protection period, to avoid the burden and pressure brought by objections from large creditors.

6.2 Business transfer

6.2.1 Overview

Similar to many other jurisdictions, a business transfer involves the assignment and assumption of physical assets, liabilities and human resources, as well as the legal relationships concerning all or part of the business, of the transferor to the transferee.

A business transfer is effected through: (1) a resolution of the business transfer by the board of directors and/or the general meeting of the shareholders of the transferor and/or the transferee, depending on the size of assets and liabilities of the transferor or the transferee as compared against the assets and liabilities of the business transferred in the business transfer; (2) the execution of a business transfer agreement; (3) the exercise of appraisal rights by dissenting shareholders; and (4) the closing of the business transfer. The timeline for the entire process varies, but in general takes approximately two months for unlisted, private companies.

6.2.2 Transfer of legal relationships

A business transfer requires the transferor to transfer its individual assets, liabilities, contracts and personnel to the transferee. Unlike a merger, a business transfer does not benefit from the automatic transfer of assets, liabilities and contracts by operation of law. This means that counterparty consent is required for the transfer of contracts and obligations of the transferor, and the consent of transferor employees is required for their employment transfer to the transferee. Accordingly, a business transfer requires more time and resources to process and effect the transfer of assets, liabilities and contracts compared with transfers in the context of a merger or spin-off, where the legal titles and relationships are comprehensively transferred.

6.3 Spin-off

6.3.1 Overview

A spin-off may be effected in the form of: (1) a vertical spin-off, where the spun-off business becomes a wholly owned subsidiary of the existing company; or (2) a horizontal spin-off, where the spun-off business becomes a sister company of the existing company.

The spin-off is generally effected through: (1) a resolution of the board of directors and the GMS; (2) the public notice of a spin-off plan; (3) the one-month creditor protection procedure, which may be omitted if the existing company and the spun-off company bear joint and several liabilities for all liabilities of the existing company as of the time of the spin-off; (4) the GMS at which the spin-off is reported to the shareholders; and (5) the registration of the spin-off. The timeline for the entire process varies, but in general takes approximately two months for unlisted, private companies.

6.3.2 Transfer of legal relationships

Similar to a merger, and unlike a business transfer, the transfer of individual assets, liabilities, contracts and personnel is effected by operation of law, subject to consent or other requirements under the individual contracts of the existing company.

Further, similar to a merger, the company should undergo a creditor protection procedure, unless the existing company and the spun-off company opt to bear joint and several liabilities for all liabilities of the existing company as of the time of the spin-off.

6.4 Liquidation

6.4.1 Overview

Liquidation refers to a process to dispose of and terminate a company's existing legal relationships to extinguish its legal personality. Liquidation is conditioned upon the company's ability to repay the existing debts in full. If the company is unable to repay its existing debts in full, the company will need to undergo an insolvency proceeding, as opposed to liquidation.

The liquidation of a company requires: (1) the resolution of dissolution by the board of directors and the GMS of the company, appointment of a liquidator, and registration and report thereof; (2) the public notice and individual notices (at least two months prior to liquidation) to creditors of the company to allow the creditors to file claims; (3) the survey and report of properties subject to liquidation; (4) the closure of the company's existing businesses, recovery of claims, repayment of debts and distribution of residual assets; (5) the submission and approval of report on final accounts; and (6) the registration of liquidation. This process generally takes approximately three months.

6.4.2 Key liquidation issues

Termination of agreements

The termination of contracts of the liquidated company may trigger a prepayment or termination fee or compensation of damages. Accordingly, the liquidated company should consider in advance whether, separate and apart from monetary compensation, any affiliated company may offer to step into the shoes of the liquidated company to continue with the terms of the relevant contracts.

Labour

If the liquidation of a company requires the lay-off of existing employees, the company should comprehensively review and plan for the dismissal and/or early retirement programme of its employees (including any deemed employees, such as dispatched workers and in-house subcontractors) in compliance with applicable Korean labour laws and regulations, the rules of employment (ROE) of the company, any effective collective bargaining agreement and any applicable employment agreement.

The liquidation of a company may not be completed and effected until all pending litigations are resolved. Accordingly, any company purporting to commence liquidation should review the status of its potential and pending litigations.

6.5 Key restructuring considerations

6.5.1 Transaction structure

The optimal restructuring transaction structure may vary depending on the purpose and background of the restructuring, targeted timeline, status of permits and licences, contractual relationships and (in the case of mergers and business transfers) dissenting shareholders or (in the case of mergers and spin-offs) creditors. Several factors and considerations are as follows:

- A merger filing (eg, the submission of a business combination report in Korea) may be required for a merger or business transfer (depending on the total assets and sales revenue of the concerned companies).
- The transfer of a company's business or business permits and licences may require an approval of the supervisory governmental authority.
- Based on the transaction structure, the transfer of employees would require one of the following: (1) consent from the transferred employees; (2) consultation with the transferred employees; or (3) automatic transfer of the relevant employees. For example: (i) in the case of a merger, the employment of the officers and employees of the merged company is comprehensively transferred without separate consent; (ii) in the case of a spin-off, the consent of the transferred employees is not required, as long as the company engages in and completes 'sufficient consultation' with the transferred employees; and (iii) in the case of a business transfer, the employees subject to the transfer have the right to refuse and reject the employment transfer.
- Under applicable collective bargaining agreement or agreement(s) with the labour union, the transferred employees may have the right to consent, consult or claim compensation benefits.

6.5.2 Transaction with an insolvent company

The board of directors of a company seeking to transact with an insolvent company should conduct an enhanced review of the appropriateness and fairness of the proposed transaction, taking into account their fiduciary duties towards the company.

For example, the board of directors of a company seeking to merge with an insolvent company should carefully examine the business necessity and the fairness of the merger ratio for the proposed merger, given that the appropriateness of the merger and valuation of the merged companies are more likely to be challenged or questioned later in the process. Further, the business transfer (ie, the sale of a business) of an insolvent company is more likely to be subject to challenge, including legal action seeking to cancel or unwind the business transfer, for fraudulent conveyance.

Chapter 7: Employment and labour law

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This chapter sets forth a brief overview of the key employment and labour law concepts vital to doing business in South Korea, from start to finish, with all the intricacies in-between.

7.1 Starting a business

If you plan to start a business in South Korea, you will need people to help you to execute the business. Accordingly, you should become familiar with the Korean Labor Standards Act (LSA). The LSA is the foundational document governing employment relationships in South Korea and prescribes various minimum conditions of work, including allowances and benefits, which supersede any provisions of employment contracts, work rules or collective bargaining agreements less favourable to employees.

However, many of the most onerous provisions to employers only apply when the workplace has five or more employees. Before that threshold, the employer has significant flexibility to structure the employment relationship as it sees fit, including with regard to the setting of working hours and compensation for any overtime, provision of paid holidays and establishing standards for the termination of employment.

It is worth noting that a written employment agreement is not mandatory for full-time, regular employees; however, for certain specific provisions relating to wages/compensation, work hours, holidays, annual leave and so on, written terms must be provided to the employee at the time of entering into the employment arrangement. Therefore, it may be a helpful exercise to spend some time up front to draft a well-considered employment agreement, which is likely to make potential subsequent issues less confusing.

7.2 Winding up a business

Choosing to cease doing business in South Korea is a management prerogative. Therefore, liquidating a local entity and closing up shop also entitles the employer to terminate employment relationships with relative ease. Assuming there are no other contractual obligations, company policies or collective agreements to the contrary, an employer can terminate an employment relationship in connection with winding up a business by providing 30 days' advance notice or payment in lieu thereof.

Employers who did their homework up front by investing in a well-considered employment agreement would also know that termination of employment in South Korea (regardless of the reason for the termination) entitles employees to their retirement benefit. What kind of retirement benefit differs depending on what system was implemented earlier in the process (ie, company pension or statutory severance), but the benefit to the employee or cost to the employer is approximately one months' pay per year of service of the particular employee.

7.3 All the intricacies in-between

While it is not possible here to address all the issues that may arise in-between, the below is a helpful tool for understanding the top five action items for your business to maintain a healthy and compliant workplace.

7.3.1 Establish a retirement benefit

It is a legal requirement for all new companies to set up a retirement pension within one year of establishment. If this is not established, the default retirement benefit will be the traditional statutory severance (see section 7.2 above).

7.3.2 Prepare the ROE

Once the workplace reaches ten or more employees, the employer is obligated to prepare and file the ROE with the Ministry of Employment and Labor. The ROE is intended to be a set of work rules governing general working terms, such as the calculation and method of payment of wages, working hours, holidays, annual paid leave and severance pay. Under the LSA, an employment contract must not diverge from the work rules to the employee's disadvantage, and will be found invalid to the extent that it does.

7.3.3 Strictly observe disciplinary procedures and the 'just cause' standard for termination

Once the company reaches the five-employee threshold, it will no longer have the flexibility to terminate employees without 'just cause'. In practice, this is generally a very high standard to meet. In cases of dismissal for disciplinary reasons, labour authorities and courts consider the totality of the circumstances, including the severity and frequency of the alleged misconduct or poor performance, and whether or not the employee was given an opportunity to improve. Even where the substance of the wrongdoing is sufficiently severe, procedural failures (eg, did not provide due process rights or violated notice requirements) may prevent the finding of 'just cause'. The burden of proof rests with the employer to show just cause, if contested.

A 'dismissal for managerial reasons' under the LSA is also contemplated (and 'just cause' is deemed to exist) if the situation satisfies special conditions, including the standard of 'urgent business necessity'. However, in practice, just like the 'just cause' standard, the 'urgent business necessity' standard is very difficult to achieve.

Accordingly, it would not be unusual for companies to negotiate mutual separation agreements and/or implement voluntary resignation programmes, often associated with additional remuneration (eg, retirement bonus), to resolve the complications posed by the 'just cause' and 'urgent business necessity' standards.

7.3.4 To maximise employment flexibility within the 'just cause' framework, evaluate alternative employment options and understand their limitations

Global organisations will be well accustomed to the use of a contingent workforce, also sometimes referred to as outsourced workers. While such equivalents do exist in South Korea, specific legal limitations may apply depending on the type of contingent workforce/outsourced worker being contemplated. Accordingly, it is very important to understand and apply the correct concept to your particular business. For example, are you referring to part-time employees; fixed-term contract employees; dispatched workers from manpower companies; or independent contractors either from a subcontractor or as individuals? Failure to satisfy the relevant requirements may render the contingent workforce/outsourced worker a regular employee entitled to rights and benefits under the LSA, as well as subject the involved companies to criminal penalties under applicable legislation.

7.3.5 Establish a labour management council

Once the company reaches the 30 employee threshold, it will be required to establish and conduct regular meetings of the labour management council. Unlike a union, which is established by the employees, a labour management council is intended to be a cooperative body shared between the employees and management. By-laws will need to be filed with the Ministry of Employment and Labour.

Chapter 8: Tax law

Yong Whan Choi, Yulchon, Seoul

8.1 Taxes applicable to individuals

8.1.1 Income tax

TAXPAYER

An individual is subject to income tax in South Korea on income derived from sources in South Korea, whether a resident or non-resident. Resident individuals are taxed on worldwide income. A resident is a person who maintains a domicile or has resided in South Korea for 183 days or longer during one taxable year.

TAXABLE INCOME

Income tax is levied on items of taxable income specifically listed in the tax code. Income is categorised as global income (interest, dividends, business income, wages and salaries, pension income and other income), retirement income and capital gains. Global income is aggregated and taxed at regular IIT rates. Dividend and interest income amounting to less than KRW 20m are taxed separately. Retirement income and capital gains are also taxed separately.

Non-resident taxpayers are required to file a Korean IIT return for income associated with a Korean place of business or Korean real estate. All other forms of Korea-sourced income attributable to non-resident individuals is subject to WHT at the source.

TAX RATES AND CREDITS

Global income is taxed at progressive tax rates, as follows:

- six per cent of the tax base up to KRW 12m;
- 15 per cent of the excess over KRW 12m up to KRW 46m;
- 24 per cent of the excess over KRW 46m up to KRW 88m;
- 35 per cent of the excess over KRW 88m up to KRW 150m;
- 38 per cent of the excess over KRW 150m up to KRW 300m;
- 40 per cent of the excess over KRW 300m up to KRW 500m; and
- 42 per cent of the excess over KRW 500m.

CGT rates vary depending on the type of asset. Residents are generally able to claim tax credit for wage and salary income, child tax credit and credit for contributions to eligible pension accounts. Individuals with business income may claim tax credit for casualty losses. A foreign tax credit is generally available for residents paying foreign taxes on global income or retirement income.

WITHHOLDING TAX

Interest, dividends, wage and salary income, and 'other income' is subject to WHT, whether derived by a resident or non-resident. The withholding agent collects the tax at the time of payment and submits it to the district tax office by the tenth day of the following month.

8.2 Taxes applicable to businesses

8.2.1 Corporate income tax

TAXPAYER

Domestic and foreign corporations are both subject to corporate income tax. A domestic corporation is defined as a corporation with its head or main office or place of effective management in South Korea. A foreign corporation is a corporation established outside South Korea with its head or main office in a foreign country. Domestic corporations are liable to corporate income tax on worldwide income. Foreign corporations are liable to corporate income tax on domestic source income. State and local governments are not subject to corporate income tax.

Taxable income

Income subject to corporate income tax includes gross business income derived during the tax year, income from the sale of real estate and liquidation income, less all associated deductible expenses.

A foreign corporation is liable to tax on domestic source income recognised during the tax year. Domestic NPOs are liable to tax on revenue derived from profit-making activities during the tax year. Foreign corporations and NPOs are not subject to tax on liquidation income.

Tax rates and credits

Corporate income is taxed at progressive tax rates, as follows:

- ten per cent of the tax base up to KRW 200m;
- 20 per cent of the excess over KRW 200m up to KRW 20bn;
- 22 per cent of the excess over KRW 20bn up to KRW 300bn; and
- 25 per cent of the excess over KRW 300bn.

Tax credits include foreign tax credit, tax credit for disaster losses and tax credit for R&D.

Withholding tax

Taxpayers paying interest, as prescribed by the Financial Investment Services and Capital Markets Act, to domestic corporations are required to withhold corporation tax on such interest at 14 per cent (for non-commercial loans, the withholding rate is 25 per cent). The withheld taxes are paid to the government by the tenth day of the following month.

8.3 Other taxes

8.3.1 VAT

Ten per cent VAT is levied at each stage of the supply chain for both goods and services, whether or not the transacting parties are engaged in non-profit activities. VAT is levied on the supply of goods or services, or who imports the goods. Zero-rate VAT is available for eligible export goods and services.

8.3.2 Securities transaction tax

Securities transaction tax is levied on the value of stock transferred (based on the fair market value at the time of alienation). The securities transaction tax rate is currently 0.5 per cent (0.45 per cent from 1 April 2020).

8.3.3 Local tax

Ten per cent VAT is levied at each stage of the supply chain for both goods and services, whether or not the transacting parties are engaged in non-profit activities. VAT is levied on the supply of goods or services, or who imports the goods. Zero-rate VAT is available for eligible export goods and services.

Acquisition tax

Taxpayers acquiring real estate, motor vehicles, heavy equipment, trees, boats, aircraft, golf membership, condominium membership, health club membership, mining rights and fishery rights through purchase or inheritance are subject to local tax. The tax base is generally the acquisition cost, and the tax rates vary depending on the type of asset and business purpose.

Registration and licence tax

A taxpayer registering real estate, vessels, aircraft, automobiles and heavy equipment, and obtaining certain licence is subject to licence tax. The rate of the tax varies depending on the type of asset or licence.

Property tax

A taxpayer who owns real estate, vessels or aircraft is subject to property tax, which is due on 1 June each year. The rate of property tax varies depending on the type of asset.

Local income tax

Taxpayers who are subject to corporate income tax or IIT are also subject to local income tax. The tax base for local income tax is generally the same as for corporate income tax or IIT, and the rate is ten per cent of the corporate income tax or IIT amount.

Chapter 9: Intellectual property

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9.1 Overview of the intellectual property rights system

Intellectual property refers to the knowledge, information or technology; expression of an idea or emotion; mark of a business or product; type or genetic source of an organism; or other intangible object created or discovered through human creative activity or experience whose value as property could be realised. Intellectual property rights refer to the rights to intellectual property that are recognised or protected under laws and regulations or treaties.

In Korea, intellectual property rights are broadly classified into industrial property rights, which are managed by the Korean Intellectual Property Office, and copyright, which is managed by the Ministry of Culture, Sports and Tourism. Meanwhile, well-known marks or trade secrets, which have become subject to protection as a result of the prohibition of unfair competition and trade secret infringement under the Unfair Competition Prevention and Trade Secret Protection Act (UCPA), are now being perceived as new types of intellectual property.

When conducting business in South Korea, it is crucial to understand the types of intellectual property and protected subject matter, protection requirements and protection periods to determine how to manage and use one's intellectual property.

Table 1

	Protected subject matter	Protection requirements	Protection period
Patent rights **(utility model rights)**	Inventions (creation of a technical idea using the rules of nature)	Industrial applicability/novelty/inventive step	From the registration of the establishment of patent rights to 20 years after the filing date of the patent application
Design right	Designs (shape, pattern or colour of a product, or the combination thereof)	Industrial applicability/novelty/creativity	From the registration of the establishment of design rights to 20 years after the filing date of the design application
Trademark rights	Trademarks (a mark that is used to distinguish one's products from the products of others)	Intention to use, distinctiveness and lack of reasons for trademark registration refusal	Ten years from the registration of the establishment of trademark rights (renewals are possible)
Other protected subject matter under the UCPA	(1) Marks that are widely known in South Korea (2) Trade secrets	(1) Well-known (2) Not generally known or readily ascertainable, independent economic value and maintain confidentiality	Period during which the protection requirements are satisfied
Copyright	Works (creative work expressing human idea or emotion), computer programs, edited works or databases	Creativity	During the author's lifetime and for 70 years after his/her death

Intellectual property rights aim to protect intellectual property by granting exclusive rights to the right holders. However, the Monopoly Regulation and Fair Trade Act (MRFTA) aims to prevent monopolies and promote competition, thereby conflicting with the purpose of intellectual property rights. In contemplating such a situation, Article 59 of the MRFTA stipulates that 'this Act shall not apply to any act that is deemed the legitimate exercise of any right under the Copyright Act, Patent Act, Utility Model Act, Design Protection Act or Trademark Act'.

9.2 Patents

9.2.1 Patentable subject matter and patentability requirements

As a patentable subject matter, an 'invention' refers to an advanced creation of a technical idea using the rules of nature. In order for an invention to be registered as a patent, it: (1) should be applicable to an industry (industrial applicability); (2) cannot be technology that is already publicly known before its patent application (novelty); and (3) cannot easily be invented from prior art, even if it differs from prior art (inventive step).

9.2.2 Employee inventions

The 'right to obtain a patent' originally belongs to the inventor upon the completion of an invention, and such a principle also applies to an employee who creates an invention in connection with his/her duties at the employer company. However, the employer company has a non-exclusive licence to the patent held by its employee by law and should provide proper compensation to the employee if it succeeds the employee's 'right to obtain a patent' or patent right, or if it obtains an exclusive licence to the patent of the relevant employee invention by contract or employment policy. In such a case, the appropriateness of the compensation is determined by considering, among others, benefits to be obtained by the employer from such an invention and the respective contribution levels made by the employer and the employee to the completion of such an invention.

9.2.3 Patent application and registration

If there are two or more patent applications for the same invention, only the first person to file the application may obtain the patent. However, a person who intends to obtain a patent should submit a patent application form, detailed description of the invention, specification setting forth the claims, required drawings and abstract. The patent application will be examined only when a request for examination is made within three years from the date of application, and if no request for application is made within such a period, the application will be deemed to be withdrawn. Before refusing an application, the examiner notifies the applicant of the ground for refusal in order to provide the applicant with the opportunity to revise the application and submit an opinion, and determines whether or not to grant a patent by following this procedure. A person whose patent application has been refused may request a trial seeking the cancellation of the refusal decision by claiming the illegitimacy of such a decision at the Intellectual Property Trial and Appeal Board (IPTAB).

If a decision to grant a patent is rendered, the applicant should register the establishment of the patent right by paying the registration fee, and such a patent right will then be created. The content of the application of the registered patent will be publicly disclosed via the patent registration gazette. Upon the registration of its patent, the patent holder will have the exclusive right to use the patent invention as a business from the date of patent registration until 20 years from the date of patent application.

9.2.4 Patent infringement and relief

If: (1) a valid patent right exists; (2) the infringing product or method falls under the scope of protection of the patent invention; and (3) the infringer uses the infringing product or method as a business, despite the fact that it lacks legitimate authority to use the patented invention, this constitutes patent infringement. If a patent dispute arises, the relevant parties may seek relief through various methods.

A patent holder may argue that the infringing product falls under the scope of protection applicable to the patent that it owns and thereby request a positive confirmation trial for the scope of the right at the IPTAB. A relatively more proactive method would be to file a suit for injunction against patent infringement, which aims to suspend the act of patent infringement together with a suit for damages.

There are various presumptive provisions in the Patent Act due to the practical difficulty of proving the amount of compensation in a damages suit resulting from patent infringement. In 2019 the Patent Act was amended to introduce a 'punitive damages system' where a person who intentionally infringes another person's patent will be liable to pay up to three times the recognised amount of damages. Thus, it has become slightly easier for patent holders to receive compensation for damages.

Meanwhile, a person accused of patent infringement may argue that its product does not fall under the scope of protection of the patent held by the counterparty and thereby request a defensive confirmation trial for the scope of the right at the IPTAB. A more proactive measure would be to request a patent invalidation trial by arguing that the relevant patent has been registered, despite its failure to satisfy the patent requirements.

9.2.5 International application system

The PCT is a multilateral treaty executed in 1970. The PCT came into effect in 1978 to unify and streamline the international application procedures for patents and utility models. As South Korea has been a contracting state to chapters I and II of the PCT since 1984 and 1990, respectively, a patent applicant who intends to obtain a Korean patent may file an international application with the WIPO or directly with the Korean Intellectual Property Office.

When selecting South Korea (Republic of Korea) as the designated state, the applicant should be cautious not to select North Korea (People's Republic of Korea). There have been instances of applicants only becoming aware of such an error after the deadline for correcting the designated state has elapsed or after entering the South Korean procedure. In such a case, the application cannot be submitted again as a new application in South Korea because it has lost novelty.

9.3 Design

9.3.1 Concept of design and design rights

A 'design' is the shape, pattern or colour of a product (including a part or the font type of a product) or the combination thereof that creates an aesthetic impression. A person who registers a design, that is, a creative work related to the product appearance, may enjoy exclusive rights to such a registered design. The basic framework of design registration is similar to that of patents.

9.3.2 Registration requirements of a design

Similar to patents, the registration requirements of a design are industrial applicability, novelty and inventive step; the only difference is that a design also requires creativity. However, even if a design satisfies all such requirements, its registration would not be permitted for the reason of public interest if it contravenes public order or morality. Also, only those designs without any concern of causing confusion with a product related to another person's business may be registered.

Industrial applicability means the ability to produce the design using industrial methods. An artwork, for example, which cannot repeatedly be produced in a simple manner cannot be subject to a design right, and an abstract design, musical note, ore or scent, etc cannot be registered as a design right either.

Furthermore, a design should have a fixed form. It cannot be continuously changing objects, such as neon advertisements and colours of a flame. In addition, a design should be creative. A design that can be easily created using a shape, pattern or colour, or the combination thereof, that is widely known domestically or internationally, cannot be registered as it lacks creativity.

9.3.3 Unique systems under the Design Protection Act

RELATED DESIGN SYSTEM

This system pre-emptively prevents the infringement and imitation of a registered design by allowing a person who has already registered or filed an application for a design (principal design) to change such a design by modifying the shape, pattern, colour and so on of the product and to register such a changed design as a related design.

SET ITEM DESIGN SYSTEM

To register a design, an application should be filed per design. However, in case two or more articles compose one set, the design of the entire set may be registered as one design if the design of the entire set constitutes a coordinated whole.

SECRET DESIGN SYSTEM

If an applicant applies for a secret design when filing a design application, the secrecy of its design will be maintained without being disclosed through the design gazette for up to three years from the registration of the establishment of the design right.

9.4 Trademarks

9.4.1 Source indicator protection system

A 'trademark' is a mark used to distinguish one's own product from the products of others. Deceiving consumers through the unauthorised use of another person's source indicators, including trademarks and stealing the reputation and credibility of the owner of such a source indicator, violates the law and is therefore not permitted. In order to prevent such conduct, the UCPA, which is the general law on the protection of source indicators, prohibits the act of confusing consumers by using a mark that is identical or similar to a well-known mark, thereby protecting well-known marks. On the other hand, the Trademark Act protects source indicators in a more efficient way by granting trademark right holders exclusive rights to their registered trademarks.

9.4.2 Registration requirements of a trademark

To obtain a trademark right under the Trademark Act, a trademark should be registered. The requirements of trademark registration are: the intention to use, distinctiveness and the lack of reasons for trademark registration refusal. The Trademark Act lists the following as marks lacking distinctiveness: common name of goods; mark customarily used on goods; mark describing the features of goods; mark consisting of a conspicuous geographical name and so on; and simple and commonplace names and signs. Further, the reasons for trademark registration refusal include the following: trademark that includes the name of a famous person other than the applicant; trademark that is identical or similar to a well-known trademark; and trademark with an unlawful purpose.

While there is no need to prove the intention to use the trademark at the time of trademark application and registration, not using the registered trademark on the designated product for at least three consecutive years before an objection is raised may result in the cancellation of the trademark registration. Trials seeking the cancellation of unused trademarks are a commonly used solution against trademark brokers that register famous foreign trademarks in South Korea in advance.

9.4.3 Effect of a trademark and trademark infringement

A trademark right is created upon the registration of its establishment and is effective for ten years, which can be renewed. The holder of a registered trademark right has the exclusive right to use such a registered trademark on the designated product. Therefore, the act of using an identical or similar trademark on an identical or similar designated product constitutes trademark infringement, and the holder of the trademark right may file a suit for injunction against trademark infringement and a suit for damages.

However, the Trademark Act also stipulates the scope in which a registered trademark is ineffective. More specifically: (1) a trademark that indicates one's own name, trade name and so on pursuant to business practice; (2) a trademark that indicates the common name, place of production, quality and so on in a common manner; (3) a trademark with an undistinctive three-dimensional shape; (4) a trademark consisting of a geographical name; or (5) a functional mark is not subject to the effect of a trademark right and, therefore, does not constitute trademark infringement.

Meanwhile, a concerned party may request a trademark registration invalidation trial even after a trademark has been registered, claiming that such a trademark does not satisfy the registration requirements.

9.4.4 Doctrine of the exhaustion of trademark rights

If the holder of a trademark right or a person authorised by such a right holder transfers products indicated with a trademark registered in South Korea, the trademark right on such products will be exhausted as it has achieved it purpose, and the effect of such a trademark right will not affect the use, transfer or lending of such products.

Meanwhile, as the scope of a non-exclusive licence, including the designated product, survival period and region, depends on the relevant non-exclusive licence agreement, the use of a trademark by a non-exclusive licensee exceeding such a scope may be deemed to be an unauthorised use of such a trademark. However, the Korean Supreme Court recently held that the doctrine of exhaustion of trademark rights cannot be deemed inapplicable to all cases where the non-exclusive licensee transfers products in breach of an ancillary condition under the agreement, which is an unauthorised use of a trademark.

9.5 Protection under the Unfair Competition Prevention and Trade Secret Protection Act

9.5.1 Prohibition of acts of unfair competition

The Unfair Competition Prevention and Trade Secret Protection Act (USPA) protects source indicators, consumer trust and safety of transactions by stipulating and prohibiting certain types of conduct as acts of unfair competition, including those that cause confusion about the source or mislead consumers about the place of origin. The acts of unfair competition prohibited by the UCPA are as follows:

- causing confusion with another person's products by using a mark identical or similar to another person's product mark or business mark that is widely known in South Korea or selling, distributing, importing or exporting products bearing such a mark;
- damaging the distinctiveness or reputation of another person's mark by using a mark identical or similar to another person's product mark or business mark or selling, distributing, importing or exporting products bearing such a mark, as mentioned above;
- falsely marking the place of origin on products or by means of advertisements, or misleading consumers about the place of origin related to a product's place of production, manufacture or processing;
- falsely assuming another person's products or advertising, or marking on products or advertisements thereof, in a way that misleads consumers about the product quality and so on;
- act by a current or former agent of the relevant trademark right holder under the Paris Convention using a trademark identical or similar to the relevant trademark without a justifiable reason;
- unfairly obtaining a domain name in advance;
- transferring, lending, displaying, importing or exporting products that imitate the shape/form of products produced by another person;
- unfairly using economically valuable information that includes a technical or business idea of another person obtained in the course of negotiating or transacting with the other person for its own or a third party's business benefit in breach of the purpose of provision; and
- infringing the economic benefit of another person by the unauthorised use of output achieved as a result of the considerable effort and investment of the other person and so on for its own business in breach of fair business practice or competition order.

Based on the 2018 amendment of the UCPA, the 'overall appearance of a business place, including signs, exterior appearance and interior decorations' became expressly included in a 'mark indicating another person's business that is widely known in Korea' prescribed in Article 2(i)(b) and (c) of the UCPA. Therefore, it has become easier to impose legal sanctions against a competitor who copies trade dress, such as the interior of a business place, with the enforcement of the foregoing amendment of the UCPA.

9.5.2 Prohibition of trade secret infringement

The unauthorised use of intellectual property developed by an investment made by another person also falls under an act of unfair competition in a broad sense. Under the UCPA, 'trade secret' is defined as production methods, sales methods or any other useful technical or business information in other business activities that are not publicly known, have independent economic value and have been kept confidential.

In order to protect its economically valuable technical or business information from competitors, after applying for and registering a patent, after which the information will be publicly disclosed, a company should decide whether to license the patent or maintain/manage the information as a trade secret. If the company decides to maintain and manage the information as a trade secret, for the company to maintain the confidentiality of the information, it is common practice to have employees who could access such information sign a non-disclosure agreement together with a non-compete agreement.

However, it should be noted that court precedents have held as follows: even if a non-compete agreement exists between an employer and its employees, if such a non-compete agreement excessively limits the employees' freedom to choose an occupation and right to engage in work guaranteed by the Korean Constitution or excessively restricts free competition, then such an agreement falls under juristic acts contrary to good morals and other social order under Article 103 of the Korean Civil Code and, therefore, is null and void. In order to determine the validity of a non-compete agreement, the following should be considered: (1) the employer's benefits worthy of protection; (2) the position of the employee before his/her resignation; (3) the period, region and business type subject to the non-compete agreement; (4) whether compensation was given to the employee; (5) circumstances that led to the employee's resignation; and (6) the public interest and the relevant circumstances.

9.6 Copyright

9.6.1 Concept and establishment of a copyright

A 'work' refers to a creative product that expresses human ideas or emotions. There is a wide variety of works, including literary works, music, art, architecture, cinematographic works and computer programs. A copyright is established once the author creates a piece of work, and no procedure or form is needed to establish such a right. Thus, although there is a separate system for registering copyrights, the registrant is merely presumed to be the copyright holder. Meanwhile, unlike inventions, the copyright to works is reserved to the employer company of the original creator of such works.

Copyright can be broadly classified into the author's economic rights and the author's moral rights. The author's moral rights, including the right of disclosure, right of attribution and right of integrity, cannot be transferred as they are personal rights attached to the author. On the other hand, the author's economic rights, including the right of reproduction, right of public performance, right of broadcasting, right of exhibition, right of distribution, right of lending and right of the production of derivative works, are transferable and may be assigned or inherited.

9.6.2 Protection of programme formats

As the subject matter for copyright protection is limited to specific creative external expressions of human ideas or emotions using speech, letters, musical notes or colours, among others, ideas do not receive legal protection. However, it has been a seriously debated issue whether the law could prevent a third party committing the unauthorised use of a significant constituent element/component that forms the identity of the relevant company's representative game or television programme as a format and developing a work that copies the original with some modifications to the method of expression. The Korean Supreme Court has recently rendered a decision regarding this issue that increases the likelihood of such legal protection.

More specifically, the Korea Supreme Court held as follows in a case where the plaintiff ('King.com'), which developed and released a mobile game with a match-three game format, claimed that the defendant's mobile game infringed its copyright and sought an injunction:

> 'On the basis of the game development experience and knowledge accumulated by the plaintiff developer, the plaintiff selected elements that were deemed necessary in light of the characteristics of the game and arranged/combined those elements at its discretion according to the intention of game development. Apart from the issue of creativity of each element, the game possesses a sufficiently creative characteristic that distinguishes it from other existing games, wherein such creative characteristic was manifested by selecting, arranging and organically combining its major elements that were converted into a digital format pursuant to the specific intention of game development and scenario. Therefore, this game is a work entitled to protection under the Copyright Act.'

After rendering such a decision, the Korean Supreme Court found that these games were substantially similar and recognised that there was copyright infringement by the defendant.

9.6.3 Effect and limitation of a copyright

A copyright is protected during the lifetime of the author and for 70 years after his/her death. During such a period, the copyright holder reserves the exclusive right to use the work.

However, the author's economic rights are not limitless; there exist certain limitations as set forth below. In each of the following cases, a user may use a work without having to obtain the author's permission, and such use will not constitute a copyright infringement:use of public works:

- use for the purpose of a trial proceeding, political speech, school education, press release and so on;
- reproduction of current event articles and commentaries;
- quotation of publicly disclosed works – in the case in which works are being quoted for the purpose of media reporting, review, education and research within a legitimate scope pursuant to fair practices;

- performance or broadcasting for a non-profit purpose;
- reproduction for private use;
- reproduction at a library, reproduction as test questions or reproduction for the visually or hearing impaired and so on; or
- temporary audio/video recording by a broadcaster or temporary reproduction during the process of using the works.

Aside from the foregoing provisions, comprehensive fair use of works provisions were incorporated in the Korean Copyright Act (Article 35-3) during the process of executing the United States–Korea Free Trade Agreement in 2011. Such provisions provide the following standards for determining fair use: (1) purpose and nature of use; (2) type and purpose of the work; (3) proportion of the used part from the entire work and importance thereof; and (4) impact that the use of the work will have on the current or potential market, or value of such a work.

Therefore, if the defendant in a copyright case produced or handled a work that is identical or substantially similar to the works of the plaintiff without obtaining the permission of the plaintiff, that is, the copyright holder, there is no legitimate reason for the limitation of rights to take effect, and the defendant will be deemed to have committed copyright infringement if it cannot prove that it independently produced the work. In such a case, the plaintiff may file for an injunction and claim damages against the copyright infringer, and even file a criminal complaint.

Chapter 10: Financing

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10.1 Banking and finance

10.1.1 Financial regulatory framework

In order to conduct financial business in South Korea, a financial business licence or financial business registration is required. Korean financial institutions are subject to the supervision of the Financial Services Commission and its administrative body, the Financial Supervisory Service.

10.1.2 Banking regulations

The primary statute governing the banking industry in South Korea is the Bank Act, which provides for licensing requirements for and regulations on the banking business. A Korean bank must comply with prudential regulations on its banking activity, including capital adequacy, loan loss provisions, limitation on credit exposure to a single customer, loan-to-deposit ratio, and liquidity and risk management. Currently, there are no legal controls on interest rates on bank loans, except for the cap of 24 per cent per annum on interest rates under the Act on Lending Business.

10.1.3 Types of financial products

Under the Financial Investment Services and Capital Markets Act (FSCMA), financial products are broadly classified into two categories, 'securities' and 'derivatives', depending on the nature of the risk of loss involved. A 'security' is an investment product that carries a possibility of loss up to the amount of the investment principal. A 'derivative' is an investment product that carries a possibility of loss over and above the amount of the investment principal.

10.1.4 Foreign exchange regulations

All transactions between residents and non-residents of South Korea are subject to regulations under the Foreign Exchange Transaction Act, and depending upon the nature of the relevant transaction: (1) such a transaction can be freely made without any approval or reporting requirements (eg, a Korean won or foreign currency-denominated loan from a Korean bank to a resident of South Korea or a foreign currency-denominated loan from a Korean bank to a non-resident of South Korea without any guarantee or collateral provided by a resident); or (2) a report to a foreign exchange bank, the Bank of Korea or the Ministry of Finance and Economy (eg, a foreign currency-denominated loan from a Korean bank to a non-resident with a guarantee or collateral for the benefit of such a non-resident borrower, a Korean won-denominated loan from a Korean bank to a non-resident to an amount exceeding KRW 1bn (equivalent to US$800,000) or the issuance of securities by a non-resident of South Korea).

10.2 Equity financing

10.2.1 Public offering

The FSCMA defines the 'public offering' of securities as the offering of securities to 50 or more of offerees (including the total number of offerees for the same kind of securities privately placed during the past six months). The number of offerees does not include certain related persons of the issuer and professional investors as designated under the FSCMA. Even if the number of offerees is less than 50: (1) the offering of newly issued shares of a Korean issuer will be deemed as a public offering of securities where: (i) the issuer has conducted the public offering of the shares in the past; or (ii) the shares of the issuer are listed on KRX; and (2) the offering of newly issued shares of a non-Korean issuer will be deemed as a public offering in the case where: (i) the securities (including the shares and the debt securities) issued by the issuer are listed on the KRX; or (ii) Korean residents own 20 per cent or more of the total issued shares of such an issuer as of the most recent fiscal year end.

A public offering of securities with an aggregate offering amount of KRW 1bn or more, including: (1) the total amount of the same kind of securities publicly offered without filing a registration statement during the past year; and (2) the total amount of the same kind of securities privately offered during the past six months, requires the filing of a registration statement with the FSC. A failure to file the registration statement may result in the imposition of an administrative sanction and/or criminal sanction, including imprisonment or the imposition of a criminal fine.

10.2.2 Listing

A company must apply to list its shares on the KRX. In the case of a non-Korean company, it should conduct a prior consultation with the KRX at least one month prior to filing the application for a preliminary eligibility review. As part of the consultation process, the non-Korean applicant must submit its constitutive document incorporating certain mandatory matters under Korean law as prescribed in the KRX rules for investor protection. The KRX will notify the result of its decision on application for the preliminary eligibility review within 60 days. If the applicant satisfies the preliminary eligibility review requirements (including the quantitative and qualitative criteria), it can proceed with the public offering of the shares and submit the primary listing application to the KRX. The shares of the applicant will be traded on the KRX once the KRX grants its listing approval. The company, the shares of which are listed on the KRX, will be subject to various disclosure requirements under the FSCMA and the KRX rules.

Chapter 11: Privacy laws and data protection

Taeuk Kang, Bae, Kim & Lee, Seoul

The legal framework of privacy in South Korea consists of the Personal Information Protection Act (PIPA) as the overarching law, accompanied by various industry-specific laws, including the following key legislation:

- the Act on Promotion of Information and Communications Network Utilisation and Information Protection (the 'IT Network Act'), which generally regulates the processing of personal information collected online by IT service providers (ie, service providers conducting business online);
- the Act on the Protection, Use, etc of Location Information, which regulates location information of things and natural persons; and
- the Credit Information Use and Protection Act, which specifically regulates credit-related information of a person and industries that process such credit-related information.

Unless otherwise provided for in industry-specific laws, the protection of personal information is governed by PIPA. In early January 2020, major amendments to the Korean data privacy laws were passed, which are set to take effect on 5 August 2020. As the specific rules and regulations pertaining to the amendments will become available in the coming months, close monitoring of the legal developments on this front is necessary for a full appreciation of the practical implications of these amendments.

11.1 Personal Information Protection Act

PIPA applies generally to the collection and processing of personal data. The term 'personal data' refers to information pertaining to a living person (ie, a data subject), such as the name, resident registration number and images by which the individual in question may be identified (including information by which the individual in question cannot be identified, but can be identified through a simple combination with other information) (Article 2.1 of the PIPA).

11.2 Key principles

11.2.1 Lawful bases for collection and processing

The collection and processing of personal data must have a lawful basis, and this generally means explicit, opt-in consent unless another lawful basis is applicable. To be valid as consent, the data subjects must be notified of and consent to the following prior to the collection and processing of their personal data: (1) the purpose for which the data will be collected and used; (2) the items of personal data to be collected; (3) the length of time the personal data will be retained and used; and (4) the fact that data subjects have the right to refuse consent to having their personal data collected and used and the consequences of refusing consent.

Other instances of lawful bases include where: (1) the collection is necessary to enter into or to perform a contract with the data subject; (2) the collection is necessary to protect the data handler's legitimate interests (which take precedence over the data subject's rights), provided that the information is substantially relevant to the data handler's legitimate interests and the scope of the collection is reasonable; (3) the collection is necessary to comply with law or to fulfil a legal obligation; or (4) the collection of personal data is clearly necessary for the protection of life, personal or proprietary interests of the data subject or a third party, but where it is not possible to obtain informed consent from the data subject or his/her legal guardian due to: (i) the data subject's inability to express his/her intentions; or (ii) the data subject's address is unknown and so on (Article 15.1 of the PIPA).

Further, separate consent is required for any third-party transfer of personal data from the data handler to the recipient, for which consent must be obtained after notifying the data subject of the following: (1) the name or title of the third party; (2) the purpose of the transfer of personal data; (3) the items of personal data to be transferred; (4) the length of time the personal data will be retained and used by the third party; and (5) the right of refusal by the data subject and the consequences of refusal.

11.2.2 Purpose limitation

A data handler must clearly identify the purpose of data processing (Article 3.1 of the PIPA). At the time of the collection of personal data, the data handler must inform the data subject of the purpose of the collection and obtain the data subject's consent thereto (Article 15.2 of the PIPA). In order to use personal data outside the scope of the intended purpose or to transfer personal data to a third party, the data handler must inform the data subject of such a purpose and obtain the data subject's consent thereto. Moreover, particularly for the processing of personal data for marketing purposes, the following additional restrictions apply:

- in order to obtain the data subject's consent for the collection and use of personal data for the purpose of publicising or soliciting the sale of goods or services, the personal data handler must notify the data subject thereof, so that the data subject can clearly understand the purpose (Article 22.3 of the PIPA); and
- in order to outsource the affairs of publicising or soliciting the sale of goods or services, the data handler must inform the data subject of the details of the entrusted (outsourced) affairs and the entrustee (ie, the outsourcing entity) (Article 26.3 of the PIPA).

11.2.3 Retention

Prior to collecting and using any personal data, the data handler must notify the data subject of the purpose of the collection and use of the collected data, as well as the period during which such data would be retained by the data handler. Upon the achievement or exhaustion of the specific purpose, or the expiration of the retention period for the collected data, the data handler must destroy the personal data without delay.

11.3 Major amendments to data privacy laws

At the start of 2020, South Korea passed major amendments to key statutes governing the protection of personal data, which will enable and largely free up the use of pseudonymised personal data, help further clarify the latitude for the use of personal data, enhance the right of the data subject and provide consolidation of the regulatory authority. These amendments will take effect on 5 August 2020.

11.3.1 Consolidation of the related laws

The majority of data protection-related provisions in the IT Network Act will be consolidated into the PIPA, thereby making the PIPA the primary data privacy law applicable to the handling of personal data by IT service providers.

11.3.2 Use of pseudonymised personal data

The amended PIPA allows pseudonymised personal data to be used – without the need for the individuals' consent – for the purpose of generating statistical information, scientific research or public record-keeping. The statute will also allow the compilation of pseudonymised personal data (sourced from different data controllers) by specialised institutions, designated for such purposes by the Personal Information Protection Commission and other central government agencies. Meanwhile, it should be noted that the amended PIPA does not expressly allow for the use of pseudonymised personal data for commercial purposes.

11.3.3 Expanded latitude for the use of personal data

Filling what had been a significant gap in the PIPA framework, the amendments provide that personal data may be used without need of further consent from the data subject, 'within a scope reasonably related to the original purpose of collection' of the personal data, subject to factors including the absence of detriment to the data subject, the taking of necessary security measures (eg, encryption) and other criteria. These provisions are modelled after Article 5(1)(b) and Article 6(1)(f) of the EU GDPR. The scope of such permitted use needs further definition, however, and this will be forthcoming in the Presidential Enforcement Decree, which will be issued at some point before the effective date of the amendments.

11.3.4 Consolidation of the regulatory authority

Currently, regulatory oversight of data protection is divided among the Ministry of Interior and Safety, the Korea Communications Commission and the Personal Information Protection Commission (PIPC). This includes such functions as monitoring and policing compliance, and promulgating recommended practices and privacy policy terms. Under the amended PIPA, however, these functions will all be entrusted to the PIPC. The nine-member PIPC will be comprised of government officials and various law and policy experts. This change in the regulatory apparatus is evidently intended in part to meet GDPR standards for an 'independent regulator', so as to help obtain an 'adequacy' decision from the European Commission, which would relax the data flow from the EU to South Korea.

11.3.5 Data subject prerogatives augmented, including data portability

Individual data subjects will enjoy portability rights, including to require financial institutions (as well as public sector bodies) to transfer their credit personal data to various kinds of credit personal data management companies and other financial institutions, or to the data subjects themselves. Aiming to bolster data subjects' autonomy when it comes to personal data, the law will introduce a right to respond to automated assessments, including requiring the financial institution to explain the results and to furnish, correct or delete relevant data. The amended framework in this respect will, clearly, entail a host of ensuing rules and standards. Giving effect to these data subject prerogatives will also result in a considerable scope of expense and technical/system implementation, including, for example, protocols and tools to minimise bias/error in AI-based assessment processes.

Chapter 12: Competition law

Seung Hyuck Han, Yulchon, Seoul

12.1 Business establishment: merger control

Under the Monopoly Regulation and Fair Trade Act (MRFTA), the merger filing obligation to the KFTC is triggered if the following thresholds are satisfied:

- the type/size-of-transaction test:
  - a merger with another company;
  - acquisition of all, or a substantial part, of another company's business or assets for business;
  - acquisition of 20 per cent (or 15 per cent for domestic listed companies) or more of voting shares;
  - share acquisition whereby a company, having 20 per cent or more of shares in another company (or 15 per cent for a domestic listed company), becomes the largest shareholder in that company;
  - participation in the joint establishment of a new company (ie, establishment of a joint venture); or
  - creation of an interlocking directorate relationship;
- the size-of-party test:
  - worldwide assets or turnover of at least one of the parties (including its affiliates) is KRW 300bn (approximately €229.8m/$257.2m) or more; and
  - worldwide assets or turnover of the other party (including its affiliates) is KRW 30bn (approximately €22.9m/$25.7m) or more; and
- local nexus test:
  - If both parties to the transaction are foreign companies, each party's turnover in South Korea must be KRW 30bn (approximately €22.9m/$25.7m) or more.

The MRFTA prohibits a merger that substantially restricts competition in a certain market.

12.2 Conducting business operations

12.2.1 Cartel

A company shall not agree with other companies by contract, agreement, resolution or any other means to jointly engage in, or solicit any other companies to perform, any of the following conduct, if such conduct unfairly restricts competition:

- fixing, maintaining or changing prices;
- determining terms and conditions of trade;
- restricting production or distribution of goods or services;
- market allocation;
- jointly carrying out the main parts of a business, or jointly establishing a company for the same purpose;
- bid rigging; and

- any other practices that substantially restrict competition in a particular market by interfering with other companies' businesses.

The KFTC may impose penalties for any cartel activities, such as remedial orders, administrative fines (up to ten per cent of the sales of the relevant goods or services), or may make a criminal referral against an individual or company that engages in such activities.

12.2.2 Abuse of dominance

A company with a dominant market position must not engage in any of the following:

- unfairly determining, maintaining or changing the price of goods or services;
- unfairly controlling the sale of goods or the provision of services;
- unfairly interfering with the business activity of any other company;
- unfairly interfering with market entry of another company;
- unfairly excluding competitors; or
- other business activity that may substantially undermine consumer interests.

A market dominant position is presumed if:

- a single company owns more than a 50 per cent market share; or
- three or fewer companies collectively own more than a 75 per cent market share.

Otherwise, dominance is determined based on factors such as: (1) concentration of the market; (2) entry barrier; (3) possibility of collusion among competitors; (4) similarity between products or adjacent markets; and (5) relative size of competitors.

The KFTC may impose penalties for any abuse of dominance, such as remedial orders, administrative fines (up to three per cent of the sales of the relevant goods or services), or may make a criminal referral against an individual or company that engages in such activity.

12.2.3 Resale price maintenance

No company may engage in resale price maintenance, except for the maximum price maintenance with justifications.

12.2.4 Unfair trade practice

A company shall not engage in the following unfair trade practices:

- unfairly refusing to transact or do business with others or discriminating against certain companies;
- unfairly excluding competitors;
- unfairly soliciting or coercing customers from other companies;
- unfairly abusing one's superior bargaining position in a transaction;

- imposing unfair terms and conditions that restrict the business activity of another company or otherwise disrupting the business activity of another company;
- providing funds, assets, manpower and so on to other companies or specially related companies under commercially unreasonable terms and conditions; or
- other business activity that may restrain competition and fair trade.

Special regulations may apply prior to the MRFTA for abuse of superior bargaining power among certain business relationships:

- Fair Transactions in Subcontracting Act (applies to a subcontract transaction with small to medium-sized subcontractors);
- Franchise Business Promotion Act (applies to franchisor-franchisee relationships and transactions);
- Act on Fair Transactions in Large Retail Business (applies to transactions between a large retail business and a supplier); and
- Fair Agency Transactions Act (applies to transactions between a supplier and an agency).

Chapter 13: Initiating and conducting a civil action

Tony Kang, Bae, Kim & Lee, Seoul

Civil litigation is the most favoured method of dispute resolution for sizable commercial disputes in South Korea notwithstanding the fact that various ADR methods have grown increasingly popular in recent years. This chapter on dispute resolution seeks to provide a brief overview of initiating and conducting civil litigation in South Korea.

13.1 General overview

13.1.1 Legal system

Originally modelled on the German legal system, South Korea adopts a civil law litigation procedure designed primarily to be adversarial, although it also has some inquisitorial components. For instance, Article 136(1) of the Civil Procedure Act explicitly allows the judge to assume an active and inquiring role by directly asking parties questions on or requesting them to prove factual or legal matters.

13.1.2 Court structure and composition

South Korea has a three-tiered judicial system: (1) the courts of first instance; (2) the courts of the appellate level; and (3) the Supreme Court. As South Korea is not a federal state, it has a single judicial system across the nation. The district and high courts of appeal are subdivided into individual courts that hear civil, criminal, family, juvenile, administrative, intellectual property and bankruptcy matters.

13.2 Pre-action conduct

Compared to courts in other jurisdictions, South Korean courts are known to be more willing to allow interim measures, such as preliminary attachments and provisional injunctions.

13.2.1 Preliminary attachment

An applicant requesting a preliminary attachment, which is a widely sought form of measure, must satisfy the following: (1) establish a *prima facie* case; (2) prove that the assets are owned by the debtor; and (3) prove that the enforcement of the judgment would be difficult, if not impossible, unless the order is granted by the court.

13.2.2 Summary motion

Pre-action motion, such as a motion for summary judgment or motion to dismiss, are not available in South Korea.

13.3 Initiation of a civil action

13.3.1 Process

As in most jurisdictions, a civil action in South Korea commences with the filing of a complaint with the court that has jurisdiction over the case. It should be noted that class actions are not available in South Korea, except under the Securities-Related Class Action Act for disputes involving securities transactions. Save for the aforementioned exception, each claimant, therefore, should file an individual action.

Service of process is carried out only by the court. Unless served via public notice, a defendant is allowed 30 days from the receipt of the complaint to file a statement of defence.

13.3.2 Fees and third-party funding

Court costs generally consist of the following: (1) stamp fees or filing fees (approximately 0.5 per cent of the total claim amount); (2) service of process fees; (3) other out-of-pocket expenses such as *per diem* fees for witnesses; and (4) attorneys' fees.

There are currently no Korean laws or regulations on third-party funding. It should, however, be noted that Article 32 of the Attorney-at-Law Act prohibits an attorney from becoming an assignee of any right in a legal dispute.

13.4 Conduct of a civil action

13.4.1 Evidence gathering

Compared with the discovery process in common law jurisdictions (eg, the US), the discovery process in South Korea is extremely limited in its manner and method. For instance, a party seeking certain documents should make an application to the court rather than making requests through direct *inter partes* communication. Further, a party cannot make general applications for documents, but should identify specific documents sought. For instance, Article 345 of the Civil Procedure Act provides that a document production request should include the following: '(i) indication of the document; (ii) purport of the document; (iii) holder of the document; (iv) facts to be proved; and (v) causes of an obligation to submit the document'. After such a specific request has been submitted, the presiding judge has full discretion to accept or reject the application, and determine the scope and method of discovery, if such an application is accepted. In this way, all of the discovery process is conducted under the direct supervision of the court.

13.4.2 Evidentiary standard

The evidentiary standard in a civil litigation in South Korea is 'preponderance of evidence', while the 'beyond reasonable doubt' standard is used for criminal cases.

13.4.3 Hearing

In lieu of concentrated hearings (ie, hearings for a set period of consecutive days or weeks), a civil action in South Korea proceeds by holding multiple hearings generally in four-week to six-week intervals. As the entity with sole and exclusive authority to manage a litigation case, South Korean courts determine the procedural timetable of a given case, including the submission dates of various briefs and court hearings. Generally, a written judgment is rendered approximately four to eight weeks after the closing of the last hearing.

13.4.4 Confidentiality

Save for exceptional instances in which a court determines that a public hearing would be detrimental to national security or public policy, all civil case hearings are not confidential and are open to the public.

13.4.5 Jury trial

A limited number of criminal cases have adopted some aspects of a jury trial. As for civil actions, however, there is no jury trial.

13.4.6 Duration of a civil action

The duration of a civil action understandably depends on the nature and complexity of the given case. Generally speaking, the timeframe could be estimated as follows: (1) six to 18 months at the first instance court; (2) six to 12 months at the appellate level; and (3) four months to two years at the Supreme Court level.

13.5 Grounds and standard of review for appeals

Korean civil procedure allows for broad grounds for appeals.

13.5.1 An appeal to a High Court of Appeal

An appeal to a High Court of Appeal could be made on both points of law and fact. During the appeal, parties are allowed to submit new evidence and arguments. As to the standard of review, the appellate level reviews the judgment rendered by the court of first instance *de novo*.

13.5.2 An appeal to the Supreme Court

The judgment of the appellate level, on the other hand, can only be brought before the Supreme Court on questions of law.

13.6 Judgment and enforcement

13.6.1 Available final remedies

In a civil action in South Korea, the parties can seek and the courts can grant the following remedies: (1) specific performance; (2) expression of intention constituting a juridical act; (3) damages; (4) injunction; and (5) declaratory relief.

13.6.2 Allocation of costs

South Korean courts determine the allocation of costs incurred by the parties in a civil action. In principle, the court orders the losing party to bear all litigation costs.

13.6.3 Enforcement

After the issuance of a final judgment on monetary claims, the prevailing party can enforce the judgment against the property or assets of the losing party by requesting the court to place the property or assets in a public auction and to distribute the proceeds from the foregoing process.

13.7 Settlements

Both out-of-court and in-court settlements are available. Parties may opt for settlement at any stage of the civil proceedings. In the event that the parties settle their dispute through an in-court settlement, it will be recorded in the court protocol. Having the identical effect of a final judgment, the recorded settlement becomes fully enforceable.

The Philippines

Chapter 1: Introduction

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The Republic of the Philippines (the 'Philippines') is an archipelago in Southeast Asia comprising 7,107 islands. The Philippines is geographically divided into three major island groups: Luzon, Visayas and Mindanao, and its capital city is Manila. The official languages are Filipino and English.

The Philippine legal system is a hybrid of the civil law and common law traditions, originating from the country's Spanish and American colonisation. The civil law tradition applies in areas such as family relations, property, succession, contract and criminal law. Meanwhile, principles of common law are apparent in constitutional law, procedure, corporation law, taxation, insurance, labour relations, banking and currency.

Chapter 2: The business environment

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2.1 Government structure

The Philippines is a unitary presidential constitutional republic, with the President of the Philippines acting as both the head of state and the head of government.

There are three branches of government in the Philippines: the executive branch, headed by the President; the legislative branch, composed of a bicameral Congress; and the judicial branch, headed by the Supreme Court of the Philippines.

Congress has the legislative power to make laws with respect to foreign investment. This power is limited by the 1987 Constitution of the Philippines, which states that it shall be the policy of the state to pursue an independent foreign policy. The state is also enjoined by the Constitution to protect Filipino enterprises against unfair foreign competition and trade practices.

2.2 Legal system

The primary sources of law under the Philippine legal system are the following: the Constitution, statutes, international treaties and conventions, and judicial decisions that interpret the aforementioned laws.

Chapter 3: Business and corporate structures

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3.1 Common forms of legal entities

Common forms of legal entities in the Philippines include corporations, branches of foreign corporations, partnerships, associations, joint ventures and sole proprietorships. Subject to certain limitations on foreign ownership, foreign investors are allowed to establish any of these legal entities.

The recently enacted Revised Corporation Code (RCC) also allows for the creation of a one-person corporation (OPC) with a single stockholder. However, only a natural person, trust or estate may form an OPC.

3.2 Incorporation process

The Securities and Exchange Commission (SEC) has jurisdiction and supervision over all corporations, partnerships and associations. The SEC has the power to grant franchises and give legal existence to these entities. The SEC has promulgated rules and regulations governing the incorporation process.

3.3 Ongoing reporting and disclosure obligations

All corporations must annually submit a General Information Sheet to the SEC, in the form prescribed by the SEC, within 30 calendar days from the anniversary date of the issuance of their SEC licence (for branches of foreign corporations) or within 30 calendar days from the actual annual stockholders' meeting (for domestic corporations).

In addition, all corporations must submit their audited financial statements annually to the SEC, stamped 'received' by the Bureau of Internal Revenue (BIR) or its authorised banks, unless the BIR allows an alternative proof of submission for its authorised banks (eg, bank slips). Corporations must file their audited financial statements on the dates designated by the SEC, based on the memorandum circular that the SEC issues annually.

3.4 Management structures

In the Philippines the general rule is that the board of directors exercises corporate powers, conducts all business and controls all properties of the corporation. Under the previous Corporation Code, a corporation had to have a minimum of five board members and a maximum of 15. Under the RCC, however, a corporation can have just two directors, while the maximum remains at 15.

Directors are elected for a term of one year from among the holders of stocks registered in the corporation's books. Each director is to hold office until his or her successor is elected and qualified. A director must own at least one share of stock to qualify to be a director.

Some corporations vested with public interest are required to have independent directors constituting at least 20 per cent of their board. These include, among others, banks, quasi-banks, and public and publicly listed corporations under the Securities Regulation Code (SRC).

Typically, a corporation would have a president, corporate secretary and treasurer, all voted upon by the board of directors immediately after its election. A corporation may also have other officers. The treasurer chosen must be a Philippine resident, while the corporate secretary must be a resident and citizen of the Philippines.

In an OPC the single stockholder is also the president and sole director of the corporation. Furthermore, within 15 days from its incorporation, an OPC may appoint a treasurer, corporate secretary and other officers as it may deem necessary, and notify the SEC within five days from appointment. The single stockholder must also designate a nominee and an alternate nominee who, in the event of the single stockholder's death or incapacity, is to take the place of the single stockholder as director and manage the corporation's affairs.

3.5 Director, officer and shareholder liability

Under the RCC, the directors/trustees or officers of a corporation who act within their authority and in good faith do not become personally liable for the acts of the corporation, except in the following instances:

- they vote or assent to patently unlawful acts of the corporation;
- they act in bad faith or are guilty of gross negligence in directing the affairs of the corporation;
- they have conflicting interests with the corporation, in violation of their duties as directors;
- they consent to the issuance of watered stocks, or despite having knowledge of this, do not file their written objection with the corporate secretary;
- they consent to being held personally liable; or
- by provision of law, directors are made to be liable for the acts of the corporation.

Except in instances of fraud or alter ego piercing,[1] Philippine law generally considers a corporation to have a separate and distinct personality from its shareholders. Shareholders enjoy limited liability, and are exposed to the corporation's liability only to the extent of their shareholdings.

1 Alter ego piercing is when a corporation's separate juridical personality is disregarded when a corporation is found to be an alter ego of a person or of another corporation (ie, organised, controlled and its affairs conducted so as to make it merely an instrumentality or conduit of another person or corporation), and is used to commit fraud, illegal acts or inequity against third parties.

Chapter 4: Takeovers (friendly M&A)

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The RCC states that a private corporation may invest its funds in any other corporation or business, or for any purpose other than the primary purpose for which it was organised, when approved by the majority of the board of directors or trustees and ratified by the stockholders representing at least two-thirds of the outstanding capital stock, at a meeting duly called for the purpose. Notice of the proposed investment and the time and place of the meeting is to be addressed to each stockholder at the place of residence as shown in the books of the corporation, and deposited to the addressee at a post office with postage prepaid, served personally or sent electronically in accordance with the rules and regulations of the SEC on the use of electronic data messages, when allowed by the corporation's by-laws or done with the consent of the stockholders. However, where the investment by the corporation is reasonably necessary to accomplish its primary purpose as stated in the articles of incorporation, the approval of the stockholders is not necessary. There are no board or stockholder approval requirements for the investee corporation.

As for mergers and consolidations, the RCC provides that two or more corporations may merge into a single corporation, which will be one of the constituent corporations, or may consolidate into a new single corporation, which will be the consolidated corporation.

The board of directors of each corporation, and party to the merger or consolidation, must first approve the plan of the merger or consolidation, setting forth:

- the names of the corporations proposing to merge or consolidate, referred to as the 'constituent corporations';
- the terms of the merger or consolidation and the mode of carrying it into effect;
- a statement of the changes, if any, in the articles of incorporation of the surviving corporation in the case of a merger; and, in the case of consolidation, all the statements required to be set forth in the articles of incorporation under the RCC; and
- any other provision with respect to the proposed merger or consolidation as are deemed necessary or desirable.

Upon approval of the merger or consolidation plan by the majority vote of each of the board of directors of the constituent corporations, the plan will be submitted for approval by the stockholders of each corporation at separate corporate meetings duly called for the purpose. Notice of the meetings must be given to all stockholders of the respective corporations. The notice shall state the purpose of the meeting and include a copy or summary of the plan of the merger or consolidation.

The affirmative vote of stockholders representing at least two-thirds of the outstanding capital stock of each corporation is necessary for the approval of the plan.

After receiving approval from the stockholders, articles of merger or articles of consolidation will be executed by each of the constituent corporations, to be signed by the president or vice-president and certified by the secretary or assistant secretary of each corporation, setting forth:

- the plan of the merger or the plan of consolidation;
- the number of shares outstanding;
- for each corporation, the number of shares or members voting for or against the plan, respectively;
- the carrying amounts and fair values of the assets and liabilities of the respective companies as of the agreed cut-off date;
- the method to be used in the merger or consolidation of accounts of the companies;
- the provisional or *pro forma* values, as merged or consolidated, using the accounting method; and
- other information as may be prescribed by the SEC.

The articles of merger or consolidation, signed and certified, are then submitted to the SEC for its approval. However, in the case of the merger or consolidation of banks or banking institutions, loan associations, trust companies, insurance companies, public utilities, educational institutions and other special corporations governed by special laws, the favourable recommendation of the appropriate government agency must first be obtained.

If the SEC is satisfied that the merger or consolidation of the corporations concerned is consistent with the provisions of the RCC and existing laws, it will issue a certificate approving the articles and plan of the merger or consolidation, at which time the merger or consolidation will be effective.

Where the entity to be acquired is a listed company, certain rules regarding tender offers apply under the SRC and its implementing rules:

- Any person or group of persons acting in concert, who intends to acquire 15 per cent of equity securities in a public company in one or more transactions within a period of 12 months, must file a declaration to that effect with the SEC.
- Any person or group of persons acting in concert, who intends to acquire 35 per cent of the outstanding voting shares or such outstanding voting shares that are sufficient to gain control of the board in a public company in one or more transactions within a period of 12 months, must disclose such an intention and contemporaneously make a tender offer for the percentage sought to all holders of such securities within the said period. If the tender offer is oversubscribed, the aggregate number of securities to be acquired at the close of such tender offer must be proportionately distributed across selling shareholders with whom the acquirer may have been in private negotiations, and other shareholders. For the purposes of the rules of the SRC, the last sale that meets the threshold must not be consummated until the closing and completion of the tender offer.

- Any person or group of persons acting in concert, who intends to acquire 35 per cent of the outstanding voting shares or such outstanding voting shares that are sufficient to gain control of the board in a public company through the Philippine Stock Exchange (the 'Exchange') is not required to make a tender offer, even if such a person or group of persons acting in concert acquire the remainder through a block sale if, after acquisition through the Exchange trading system, they fail to acquire the target of 35 per cent or such outstanding voting shares that are sufficient to gain control of the board.
- Any person or group of persons acting in concert, who intends to acquire 35 per cent of the outstanding voting shares or such outstanding voting shares that are sufficient to gain control of the board in a public company directly from one or more stockholders is required to make a tender offer for all the outstanding voting shares. The sale of shares pursuant to the private transaction or block sale must not be completed prior to the closing and completion of the tender offer.
- If any acquisition would result in ownership of over 50 per cent of the total outstanding equity securities of a public company, the acquirer is required to make a tender offer under the rules of the SRC for all the outstanding equity securities to all remaining stockholders of the said company at a price supported by a fairness opinion provided by an independent financial adviser or equivalent third party. The acquirer in such a tender offer is required to accept all securities tendered.

Chapter 5: Foreign investment

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5.1 Foreign investment control/restriction

The Foreign Investments Act classifies industries into the following: nationalised industries (no foreign ownership is allowed), partially nationalised industries (foreign ownership is limited or subject to certain ceilings) and liberalised industries (may be 100 per cent owned by foreign investors).

Nationalised industries include the following:

- mass media;
- retail trade (where paid-up capital is less than US$2.5m);
- cooperatives;
- small-scale mining;
- utilisation of marine resources;

- ownership, operation and management of a cockpit; and manufacture, repair, stockpiling and/or distribution of biological, chemical, radiological and nuclear weapons, and anti-personnel mines; and
- manufacture of pyrotechnic devices.

Partially nationalised industries include, but are not limited to:

- private radio communications network (limited to 20 per cent foreign ownership);
- private recruitment (limited to 25 per cent foreign ownership);
- contracts for the construction and repair of locally funded public works, except: (1) infrastructure and development projects covered by Republic Act No 7718 or the Build–Operate–Transfer Law; and (2) projects that are foreign-funded or assisted and required to undergo international competitive bidding (limited to 25 per cent foreign ownership);
- contracts for the construction of defence-related structures (limited to 25 per cent foreign ownership);
- advertising (limited to 30 per cent foreign ownership);
- exploration, development and utilisation of natural resources (limited to 40 per cent foreign ownership);
- ownership of private land (limited to 40 per cent foreign ownership);
- operation and management of public utilities (limited to 40 per cent foreign ownership);
- educational institutions (other than those established by religious groups and mission boards) (limited to 40 per cent foreign ownership);
- culture, production, milling, processing and trading, except retailing, of rice and corn, and acquiring rice, corn and their by-products (limited to 40 per cent foreign ownership);
- contracts for the supply of materials, goods and commodities to state-owned and municipal corporations (limited to 40 per cent foreign ownership);
- facility operator of an infrastructure or development facility requiring a public utility franchise (limited to 40 per cent foreign ownership);
- operation of deep-sea commercial fishing vessels (limited to 40 per cent foreign ownership);
- adjustment companies (limited to 40 per cent foreign ownership);
- ownership of condominium units (limited to 40 per cent foreign ownership);
- project proponents and facility operator of a build–operate–transfer project requiring a public utilities franchise (limited to 40 per cent foreign ownership);
- all forms of gambling, except those covered by investment agreements with the Philippine Amusement and Gaming Corporation operating within special economic zones (SEZs) administered by the Philippines Economic Zone Authority (PEZA) (limited to 40 per cent foreign ownership);

- domestic market enterprises (ie, enterprises that produce goods or render services to the domestic market entirely or export less than 60 per cent of their output) with paid-in capital of less than US$200,000 (limited to 40 per cent foreign ownership); and
- domestic market enterprises that involve advanced technology or employ at least 50 employees with paid-in capital of less than US$100,000.

It should also be noted that only citizens of the Philippines or corporations owned by at least 60 per cent Filipinos are allowed to own land in the Philippines.

5.2 Foreign exchange control

The Central Bank of the Philippines (Bangko Sentral ng Pilipinas – BSP) is the central monetary authority of the Philippines. It is the entity that regulates the injection and repatriation of foreign exchange in the Philippines. The Manual of Regulations on Foreign Exchange Transactions (the 'ForEx Manual') issued by the BSP consolidates the rules governing foreign exchange transactions. In summary, foreign investors consider the following in dealing with foreign exchange transactions in the Philippines:

- Investments in foreign currency need not be registered with the BSP, as long as no foreign currency will be sourced from the Philippine banking system for the purpose of repatriating funds.
- Portfolio investments (eg, peso-denominated securities issued onshore by the national government and other public sector entities; securities of resident enterprises listed at the Exchange; peso time deposits with a local bank with a maturity of at least 90 days; and other peso-denominated debt instruments issued onshore by private resident and that do not constitute loans requiring BSP approval under the ForEx Manual) must be registered with the BSP.
- Applications for the registration of foreign currency funding for FDI must be filed with the BSP within one year from the date of inward remittance to the Philippines.

5.3 Applicable tax incentive or grant

The fiscal incentives granted to foreign investors depend on the industry and the type of vehicle that the foreign investor invests in, which can fall under incentive regimes established by the following laws:

- Executive Order No 226, as amended, or the Omnibus Investments Code, by registering with the Board of Investments (BOI), that is, by becoming a BOI-Registered Enterprise, or by establishing a regional or area headquarters (RHQ) or regional operating headquarters (ROHQ);
- Republic Act No 7916, as amended, or the SEZ Act, by registering with the PEZA and locating in a PEZA Economic Zone;
- Republic Act No 7903 by locating in the Zamboanga City SEZ; Republic Act No 7922 by locating in the Cagayan SEZ; Republic Act No 9490, as amended by Republic Act No 10083, by locating in the Aurora Pacific Economic and Freeport Zone; and Republic Act No 9728 by locating in the Freeport Area of Bataan;

- Republic Act No 7227, as amended, or the Bases Conversion and Development Act, by locating in the Subic Bay SEZ; the Clark SEZ; the John Hay SEZ; or the Poro Point Freeport Zone;
- Republic Act No 9593, or the Tourism Act, by registering with the Tourism Infrastructure and Enterprise Zone Authority and locating in a Tourism Enterprise Zone;
- Republic Act No 7844, or the Export Development Act, by registering with the Export Development Authority;
- Republic Act No 8756, or the RHQ, ROHQ and Regional Warehouses Act, by registering with the SEC upon favourable recommendation of the BOI; and
- other special laws that create SEZs or that grant incentives for certain priority industries.

Chapter 6: Restructuring and insolvency

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Republic Act No 10142, or the Financial Rehabilitation and Insolvency Act (FRIA), generally covers insolvent corporations or individuals and provides procedures for liquidation and rehabilitation. These include methods to restructure liabilities, including court-supervised or pre-negotiated rehabilitation, out-of-court informal restructuring agreements or rehabilitation plans, and suspension of payments. The FRIA also expressly adopts the UNCITRAL Model Law on Cross-Border Insolvency, which allows for the recognition of foreign insolvency proceedings, subject to section 136 (on the liquidation of securities market participants), and rules of procedure to be adopted by the Supreme Court. Note that insolvent banks, insurance companies and pre-need companies are covered by Republic Act No 7653 ('New Central Bank Act'), Presidential Decree No 1460 ('Insurance Code') and Republic Act No 9829 ('Pre-Need Code'), respectively, with the FRIA only applying in supplement.

6.1 Court-supervised rehabilitation

Under the FRIA, court-supervised rehabilitation can be voluntary or involuntary.

Voluntary court-supervised rehabilitation may be initiated by the debtor through a verified petition, with the approval of the owner in the case of a sole proprietorship; an approval by the majority vote of the partners in the case of a partnership; or an approval by the majority vote of the board of directors or trustees, with authority from the stockholders or members representing at least two-thirds of the outstanding capital stock or members, in a meeting duly called for the purpose. A group of debtors may jointly file a petition for rehabilitation in cases where one or more of its members foresee the impossibility of meeting debts as they fall due; the financial distress would be likely to adversely affect the financial condition and/or operations of the other members; and/or the participation of the other members of the group is essential under the terms and conditions of the proposed rehabilitation plan.

Involuntary court-supervised rehabilitation may be initiated by any creditor or group of creditors with an aggregate claim of at least PHP 1m or at least 25 per cent of the subscribed capital stock or partners' contribution, whichever is higher, by filing a verified petition for rehabilitation based on the following grounds: (1) there is no genuine issue of fact or law on the claims of the creditors, and the due and demandable payments were not made for at least 60 days, or the debtor has failed to meet liabilities as they fall due; or (2) a creditor, other than the petitioner(s), initiated foreclosure proceedings against the debtor that will prevent it from paying its debts as they become due or render it insolvent.

In both voluntary and involuntary rehabilitation, the petition must establish the debtor's insolvency and the viability of its rehabilitation, provide a rehabilitation plan and nominate at least three persons as rehabilitation receivers.

Should the petition be deemed sufficient in form and substance, the rehabilitation court will issue a Commencement Order, the effects of which generally retroact to the Commencement Date (which is, effectively, the date of filing of the petition). The Commencement Order has the following effects, among others:

- prohibits the debtor's suppliers from withholding the supply of goods and services in the ordinary course of business for as long as the debtor pays for them;
- authorises the payment of administrative expenses (these include expenses incurred in the ordinary course of business, such as compensation for employees, or those reasonable and necessary fees for filing the petition, conducting the rehabilitation proceeding, compensating the rehabilitation receiver and paying new obligations after the Commencement Date);
- serves as legal basis to annul the following: (1) the result of an extrajudicial process to seize property, sell encumbered property, or otherwise attempt to collect or enforce a claim against the debtor after the Commencement Date; and (2) any set-off of any debt owed to the debtor by any of the debtor's creditors after the Commencement Date;
- consolidates the resolution of all legal proceedings by and against the debtor to the rehabilitation court, provided that cases in other courts may be allowed to continue therein where the debtor initiated the suit;
- considers as waived the imposition of all taxes and fees, including penalties, interest and charges by national or local governments, from the issuance of the Commencement Order until the approval of the rehabilitation plan or dismissal of the petition; and
- incorporates a Stay Order that shall: (1) suspend all actions or proceedings, in court or otherwise, for the enforcement of claims against the debtor; (2) suspend all actions to enforce any judgment, attachment or other provisional remedies against the debtor; (3) prohibit the debtor from selling, encumbering, transferring or disposing in any manner of its properties, except in the ordinary course of business; and (4) prohibit the debtor from paying its outstanding liabilities as of the Commencement Date, except as may be provided by the FRIA.

Management and control during the rehabilitation proceedings would remain with the existing management of the debtor, unless the rehabilitation receiver is appointed to take over under section 36 of the FRIA, or the rehabilitation receiver and the rehabilitation court approve the creation of a management committee.

During rehabilitation, all disbursements, payments for sale, disposal, assignment, transfer or encumbrance of property, or any other act affecting title to or interest in property shall be subject to the recommendation/approval of the rehabilitation receiver or rehabilitation court. These dispositions include:

- sale of unencumbered property outside the ordinary course of business by reason of their perishable nature, costliness to maintain or susceptibility to devaluation;
- sale, transfer, conveyance or disposal of encumbered property with the consent of the property owners or secured creditors, when it is determined, after notice and hearing, that such a disposition is necessary for the continued operation of the debtor's business, and the debtor made arrangements to provide a substitute lien or ownership right with an equivalent level of security to a counter-party's claim or right;
- disposition of property pursuant to possessory pledges, mechanic's lien or similar claims;
- sale of assets subject to rapid obsolescence , the depreciation of which cannot be avoided and would jeopardise the security interest of a secured creditor; and
- credit arrangements entered into after the Commencement Date.

In the event that the rehabilitation court gives due course to the petition, the rehabilitation receiver shall confer with the debtor and all classes of creditors to consider their views and proposals in reviewing, revising or preparing a new rehabilitation plan.

The creditors shall be notified of the availability of the rehabilitation plan for examination. The rehabilitation receiver shall then convene the creditors as a whole, or per class, within 20 days from such a notice, to vote on the rehabilitation plan. The rehabilitation plan shall be deemed approved by *a class* of creditors if members holding 50 per cent of the total claims of such a class vote in favour of the rehabilitation plan. The rehabilitation plan shall be deemed rejected unless approved by *all classes* of creditors whose rights are adversely modified or affected by it. Note that the votes of the creditors are based on the amount of their respective claims in the registry of claims prepared by the rehabilitation receiver.

Assuming the rehabilitation plan is rejected, the rehabilitation court may still confirm it through its 'cram-down power', if: (1) it complies with the FRIA; (2) the rehabilitation receiver recommends its confirmation; (3) the shareholders, owners or partners of the debtor lose at least their controlling interest as a result of the said rehabilitation plan; and (4) it would be likely to provide the objecting class of creditors with compensation that has a net present value greater than what they would receive under liquidation.

Rehabilitation proceedings are terminated upon a motion by any stakeholder or the rehabilitation receiver through the declaration of the successful implementation of a rehabilitation plan or a failure of rehabilitation. There is failure of rehabilitation if: (1) the petition is dismissed; (2) the debtor fails to submit a rehabilitation plan; (3) there is no substantial likelihood that the debtor can be rehabilitated within a reasonable period; (4) the rehabilitation plan or its amendment is approved, but the debtor fails to perform its obligations thereunder, or the objectives, targets, goals, timelines and conditions for settlement of obligations are not met or realised; (5) there is fraud in securing the approval of the rehabilitation plan; and/or (6) other analogous circumstances.

6.2 Liquidation

Liquidation under the FRIA can either be voluntary or involuntary.

Voluntary liquidation can be initiated by a debtor through a verified petition for liquidation. At any time during the pendency of court-supervised or pre-negotiated rehabilitation proceedings, the debtor may also initiate liquidation proceedings by filing a verified motion in the same court where the said proceedings are pending to convert them into liquidation proceedings. The petition or motion must include an inventory of the debtor's assets and nominees for liquidator.

Involuntary liquidation can be initiated through a verified petition for liquidation by three or more creditors whose aggregate claim is either at least PHP 1m or at least 25 per cent of the subscribed capital stock or partner's contributions of the debtor, whichever is higher. The petition must show that: (1) there is no genuine issue of fact or law on the claims(s) of the petitioner(s) and that the due and demandable payments thereon have not been made for at least 180 days, or that the debtor has failed generally to meet its liabilities as they fall due; and (2) there is no substantial likelihood that the debtor may be rehabilitated. At any time during the pendency of or after a court-supervised or pre-negotiated rehabilitation proceedings, three or more creditors whose claim is either at least PHP 1m or at least 25 per cent of the subscribed capital or partner's contributions of the debtor, whichever is higher, may also initiate liquidation proceedings by filing a verified motion in the same court where the said proceedings are pending to convert them into liquidation proceedings.

If the court finds the petition for liquidation sufficient in form and substance, it shall issue a liquidation order, which shall:

- direct the sheriff to take possession and control of the debtor's properties, except those exempt from execution;
- direct payments of any claims and conveyance of any property due the debtor to the liquidator;
- prohibit payments by the debtor and transfer of any property;
- direct all creditors to file their claims with the liquidator within the applicable periods; and
- authorise the payment of administrative expenses as they become due.

The liquidation order shall also have the following effects:

- the juridical debtor shall be deemed dissolved and its corporate or juridical existence terminated;

- legal title to and control all of the debtor's assets, except those exempt from execution, shall be deemed vested in the liquidator or, pending his or her election or appointment, with the court;
- all contracts of the debtor shall be deemed terminated and/or breached, unless the liquidator, within 90 days from the date of his or her assumption of office, declares otherwise and the contracting party agrees;
- no separate action for the collection of an unsecured claim shall be allowed, and actions already pending will be transferred to the liquidator for him or her to accept and settle or contest. If the liquidator contests or disputes the claim, the court shall allow, hear and resolve such a contest, except when the case is already on appeal, in which case the suit may proceed to judgment, and any final and executory judgment thereon for a claim against the debtor shall be filed and allowed in court; and
- no foreclosure proceeding shall be allowed for a period of 180 days.

The liquidator shall submit to the liquidation court a liquidation plan within three months from assumption of office. The liquidation plan shall abide by the following principles, among others:

- The plan shall enumerate all assets of the debtor and schedule a liquidation thereof and payment of claims. Properties exempt from execution shall be set apart.
- The liquidator may sell unencumbered assets of the debtor in a public auction and convert them into money. However, a private sale may be allowed with approval of the court, if: (1) the goods are of a perishable nature, liable to quick deterioration in value, or disproportionately expensive to keep or maintain; or (2) it is in the best interest of the debtor and creditors.
- It shall ensure the concurrence and preference of credits under the Civil Code of the Philippines.

Chapter 7: Employment, industrial relations, and work health and safety

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7.1 Employees' rights and protection

The Philippine Constitution guarantees security of tenure, humane conditions of work and a living wage for workers. Presidential Decree No 442, as amended, or the Labor Code of the Philippines, provides that an employee may only be terminated by the employer for just and authorised causes that must comply with the procedural due process requirements mandated by law. Otherwise, the termination may be deemed illegal, which shall make the employer liable for backwages, damages and separation pay if reinstatement is no longer feasible.

The following are just causes for termination:

- serious misconduct or wilful disobedience;
- gross and habitual neglect of duties;
- fraud or wilful breach of trust;
- loss of confidence;
- commission of a crime or offence by the employee against his or her employer, the employer's immediate family or his or her duly authorised representatives; and
- other causes analogous to the foregoing.

In termination for just cause, due process involves the two-notice rule:

- a written notice of intent to dismiss specifying the ground for termination and a detailed narration of facts and circumstances that serve as a basis for the charge, and giving said employee reasonable opportunity (five calendar days from the receipt of the notice) within which to explain his or her side;
- a hearing or conference in which the employee is given an opportunity to respond to the charge, present evidence or rebut the evidence presented against him or her; and
- a notice of dismissal indicating that, upon due consideration of all the circumstances, grounds have been established to justify termination.

The following are the authorised causes for termination:

- installation of labour-saving devices;
- redundancy;
- retrenchment to prevent losses;
- closure or cessation of business; and
- a disease not curable within six months, as certified by a competent public authority, and when the continued employment of the employee is prejudicial to his or her health or to the health of his or her colleagues.

In a termination for an authorised cause, due process means a written notice of dismissal to the employee and the Department of Labor and Employment specifying the grounds at least 30 calendar days before the date of termination.

In addition, an employee terminated based on an authorised cause is entitled to separation pay, except when the termination is due to closure or cessation of business operation due to serious business losses.

For termination due to redundancy and implementation of labour saving-devices, the employee shall be paid by the employer separation pay equivalent to at least one month's pay or at least one month's pay for every year of service, whichever is higher; a fraction of at least six months service is considered as one whole year.

For termination due to retrenchment, cessation of business operation not due to serious business losses, or disease, the employee shall be paid by the employer separation pay equivalent to at least one month's pay or at least half a month's pay for every year of service, whichever is higher; a fraction of at least six months service is considered as one whole year.

Republic Act No 11058 ensures a safe and healthful workplace for all workers and requires employers to equip the workplace so that it is free from hazardous conditions that are likely to cause death, illness or physical harm to the workers, among other requirements.

The Philippine Constitution also guarantees the rights of all workers to self-organisation, collective bargaining and negotiations, and peaceful concerted activities, including the right to strike in accordance with law.

7.2 Statutory contributions and minimum wage

Employers are required to pay their employees at least the minimum wage required by law. Under the most recent wage order (Wage Order No 22), the minimum gross basis wage for employees in the National Capital Region (Metro Manila) is PHP 37 per day.

The following laws require mandatory employer contributions to a state fund from which employees may claim applicable benefits:

- Republic Act No 8282, or the Social Security Law;
- Republic Act No 7875, as amended, or the National Health Insurance Act; and
- Republic Act No 9679, or the Pag-Ibig Fund.

7.3 Work permits

Foreign nationals who intend to engage in gainful employment in the Philippines must obtain an Alien Employment Permit from the Department of Labor and Employment, and a work visa or 9(g) visa from the Philippine Bureau of Immigration.

During the pendency of an application for a 9(g) visa, a Provisional Work Permit valid for three months may be applied to allow the foreign national to commence employment.

For short-term assignments of up to six months, a foreign national may obtain a Special Working Permit from the Philippine Bureau of Immigration.

Chapter 8: Tax law

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8.1 Taxes applicable to individuals

An individual taxpayer is subject to the following income taxes:

8.1.1 Graduated income tax rates

Tax schedule effective 1 January 2018 until 31 December 2022:

Under PHP 250,000	0%
Over PHP 250,000 but under PHP 400,000	20% of the excess over PHP 250,000
Over PHP 400,000 but under PHP 800,000	PHP 30,000 + 25% of the excess over PHP 400,000
Over PHP 800,000 but under PHP 2,000,000	PHP 130,000 + 30% of the excess over PHP 800,000
Over PHP 2,000,000 but under PHP 8,000,000	PHP 490,000 + 32% of the excess over PHP 2,000,000
Over PHP 8,000,000	PHP 2,410,000 + 35% of the excess over PHP 8,000,000

Tax schedule effective 1 January 2023 onwards:

Under PHP 250,000	0%
Over P250,000 but under PHP 400,000	15% of the excess over PHP 250,000
Over PHP 400,000 but under PHP 800,000	PHP 22,500 + 20% of the excess over PHP 400,000
Over PHP 800,000 but under PHP 2,000,000	PHP 102,500 + 25% of the excess over PHP 800,000
Over PHP 2,000,000 but under PHP 8,000,000	PHP 402,500 + 30% of the excess over PHP 2,000,000
Over PHP 8,000,000	PHP 2,202,500 + 35% of the excess over PHP 8,000,000

The compensation of an employee is subject to creditable WHT using the graduated income tax rates. The employer shall act as the withholding agent for the compensation who must deduct the WHT prior to payment of the compensation, as well as remit the taxes withheld to the BIR.

8.1.2 Self-employed individuals

Self-employed individuals and/or professionals have the option to avail of an eight per cent tax on gross sales or gross receipts and other non-operating income in excess of PHP 250,000 in lieu of the graduated income tax rates and the percentage tax.

8.1.3 Individuals earning income from both compensation income and from self-employment

Taxpayers earning both compensation income and income from business or practice of profession shall be subject to the following taxes:

- all income from compensation: graduated income tax rates; and
- all income from business or practice of profession:
  - if total gross sales and/or gross receipts and other non-operating income do not exceed the VAT threshold: the graduated rates prescribed on taxable income or eight per cent income tax based on gross sales or gross receipts and other non-operating income in lieu of the graduated income tax rates and the percentage tax; and
  - if total gross sales and/or gross receipts and other non-operating income exceeds the VAT threshold: the graduated income tax rates.

8.2 Taxes applicable to businesses

The taxes applicable to businesses depend on the type of business entity.

8.2.1 Domestic corporation

A domestic corporation shall be taxable on income derived from sources within and outside the Philippines. Among the principal taxes imposed on a domestic corporation are:

- corporate income tax at a rate of 30 per cent of its net taxable income;
- the minimum corporate income tax of two per cent of the gross income as in the case of a branch office;
- tax on certain passive income;
- VAT at a rate of 12 per cent of its gross receipts from its sales of goods and/or services in the course of trade or business, and 12 per cent of the value of the goods from its importation of goods; and
- local taxes, fees and charges imposed by the appropriate local government unit (ie, province, municipality, city or *barangay*), subject to guidelines and limitations provided by Congress, which normally include business, community and real property taxes.

8.2.2 Branch office

A branch office is considered a resident foreign corporation and shall be taxable only on income derived from sources within the Philippines. It shall be liable for the following taxes:

- corporate income tax at a rate of 30 per cent of its net taxable income;
- a minimum corporate income tax of two per cent of the gross income as of the end of the taxable year beginning on the fourth taxable year immediately following the year in which the

corporation commenced its business operations, when the minimum income tax is greater than the tax computed in accordance with the specified formula;

- tax on branch profit remittances at a rate of 15 per cent upon any profit remitted by an ROHQ to its parent company based on the total profits applied or earmarked for remittance without any deduction for the tax component thereof (except those activities registered with the PEZA);
- tax on certain passive income;
- VAT at a rate of 12 per cent of its gross receipts from its sales of goods and/or services in the course of trade or business, and 12 per cent of the value of the goods from its importation of goods; and
- local taxes, fees and charges imposed by the appropriate local government unit (ie, province, municipality, city or *barangay*), subject to guidelines and limitations provided by Congress, which normally include business, community and real property taxes.

8.2.3 Representative office

A representative office is not subject to income tax and is exempt from filing a corporate income tax return. However, a representative office is required to deduct, withhold and remit to the BIR income taxes due on the salaries of its employees. Likewise, a representative office is required to secure its Taxpayer's Identification Number from the BIR.

8.2.4 Regional or area headquarters

A RHQ is not subject to income tax. Further, it is exempt from VAT and all kinds of local taxes, fees or charges imposed by a local government unit, except real property tax on land improvement and equipment. However, it is required to submit an annual information return of a tax-exempt corporation. A RHQ also enjoys tax and duty-free importation of equipment and materials for training and conferences needed and used solely for its functions as a RHQ and not locally available subject to the prior approval of the BOI.

8.2.5 Regional operating headquarters

A ROHQ is taxable only on income derived from sources within the Philippines and subject to the following taxes:

- corporate income tax at a rate of ten per cent of its net taxable income;
- tax on branch profits remittance at a rate of 15 per cent upon any profit remitted by a ROHQ to its parent company based on the total profits applied or earmarked for remittance without any deduction for the tax component thereof (except those activities registered with the PEZA);
- tax on certain passive income; and
- VAT at a rate of 12 per cent of its gross receipts from sales of goods and/or services in the course of trade or business, and 12 per cent of the value of the goods from its importation of goods, except the importation of equipment and materials for training and conferences needed for ROHQ functions.

A ROHQ is exempt from all kinds of local taxes, fees or charges imposed by a local government unit, except real property tax on land improvement and equipment. A ROHQ also enjoys tax and duty-free importation of equipment and materials for training and conferences needed and used solely for its functions as a ROHQ and not locally available subject to the prior approval of the BOI.

8.3 Other taxes

8.3.1 Final withholding tax

Final withholding tax (FWT) is a tax on passive income, and constitutes a full and final payment of the income tax due. The payee is not required to file an income tax return for the particular income subject to FWT, as the liability for the payment of tax rests primarily on the payor as the withholding agent. The following are types of income subject to FWT:

- interest;
- royalties;
- rent;
- dividends; and
- capital gains on the sale of real property.

Generally, the FWT rates for interest and royalties are as follows:

- 20 per cent if the income recipient is a domestic/resident foreign corporation, citizen, resident foreign national or non-resident foreign national engaged in business in the Philippines;
- 25 per cent for a non-resident foreign national not engaged in business in the Philippines; and
- 30 per cent for a non-resident foreign corporation, subject to preferential rates under applicable tax treaties.

Rentals from sources within the Philippines paid to a non-resident foreign corporation are subject to 30 per cent FWT.

Dividends received by one domestic corporation from another are not subject to tax, while those received by a non-resident foreign corporation are subject to 30 per cent FWT, subject to preferential rates under applicable tax treaties.

8.3.2 Capital Gains Tax

CGT is a tax imposed on the gains presumed to have been realised by the seller from the sale, exchange or other disposition of capital assets located in the Philippines. The sale of real property is generally subject to six per cent CGT. The sale of shares not listed in the stock exchange is subject to 15 per cent CGT if the seller is an individual or domestic corporation. If the seller is a non-resident foreign corporation, the sale of shares not traded in the stock exchange are subject to CGT of five per cent on the net capital gains not exceeding PHP 100,000 plus ten per cent on any amount in excess of PHP 100,000.

8.3.3 Documentary stamp tax

Documentary stamp tax (DST) is an excise tax levied on documents, instruments, loan agreements and papers evidencing the acceptance, assignment, sale or transfer of an obligation, right or property incident. The amount of tax is either fixed or based on the par or face value of the document or instrument. The tax is paid by the person making, signing, issuing, accepting or transferring the documents. However, whenever one party to the taxable document enjoys exemption from the tax, the other party who is not exempt is directly liable for the tax. The DST is payable on or before the fifth day of the month following the month when the document was executed.

8.3.4 VAT

VAT is a tax on consumption levied on the sale, barter, exchange or lease of goods or properties and services in the Philippines and on the importation of goods into the Philippines. The current VAT rate is 12 per cent on the purchase price or consideration. It is an indirect tax, which may be shifted or passed on to the buyer, transferee or lessee of goods, properties or services. Any person or entity who, in the course of trade or business, sells, barters, exchanges or leases goods or properties and renders services subject to VAT, if the aggregate amount of annual gross sales or receipts exceeds PHP 3m, shall be required to file and pay VAT.

8.3.5 Donor's tax

Donor's tax is a tax upon the transfer by any person, resident or non-resident of property as a gift. The tax for each calendar year shall be six per cent computed on the basis of the total gifts in excess of PHP 250,000 excluding the gift made during the calendar year. In the case of transfers of property for less than an adequate and full consideration, the amount by which the fair market value of the property exceeds the value of the consideration shall be deemed a gift subject to donor's tax, except if the transfer was made in the ordinary course of business (a transaction that is bona fide, at arm's length[2] and free from any donative intent).

Chapter 9: Intellectual property

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9.1 Patents

The Philippine legal system provides protection for inventions, utility models and industrial designs. The basis for protection is primarily statutory law, particularly Republic Act No 8293 or the Intellectual Property Code of the Philippines, as amended, and its implementing rules and regulations. In addition, Republic Act No 9502 or the Universally Accessible Cheaper and Quality Medicines Act, and Republic Act No 9150 or An Act Providing for the Protection of Layout-Designs

2 The arm's length principle is an internationally recognised standard for transfer pricing between associated enterprises. The arm's length principle requires the transaction with a related party to be made under conditions and circumstances comparable to a transaction with an independent party.

(‘Topographies’) of Integrated Circuits, which amended some provisions of the Intellectual Property Code, may also be referred to. Rights under applicable statutes are further developed by case law.

The Philippines is also a contracting party to the PCT, which provides additional rights to member states, such as the possibility of seeking patent protection for an invention or utility model (if the contracting state provides utility model protection) simultaneously in the contracting states by filing one initial application and subsequently entering into national phase entry applications for selected countries.

The procedure and requirements for the grant of a patent for an invention differs from that of a utility model. As in most jurisdictions, invention patents must comply with the requirements of novelty, inventiveness and industrial applicability. On the other hand, the requirement of inventiveness is dispensed with for utility models. In terms of the patent grant procedure, the examination of an application for an invention patent is more stringent than that for a utility model.

Upon filing a patent application for an invention, the application will undergo a formal examination wherein the required documents are checked. The results of this examination are issued by the Intellectual Property Office of the Philippines (IPOPHL) approximately three months from the filing date of the application. Once the formal examination has cleared, a National Phase Entry Application Report (NPEAR) is issued by the IPOPHL, indicating that all the required documents have been filed and the application is complete. Otherwise, the IPOPHL will issue an NPEAR indicating the documents that have yet to be submitted or matters that need to be clarified by the applicant.

After passing the formal examination, a patent examiner for substantive examination will be assigned to the application. It takes approximately three years from the filing date of a patent application for its substantive examination to be completed. However, due to enhancements in manpower currently under way in the IPOPHL, this period is expected to be significantly reduced.

During a substantive examination, the Patent Examiner checks for possible issues in the application, mainly regarding the clarity of the submitted disclosures and novelty and/or inventiveness of the claims covering the invention. Thereafter, office actions may be issued by the Patent Examiner and the applicant must file its responses within a period of two months. Upon the filing of a request with good and sufficient cause, and payment of the corresponding fees within the initial period to file the response, the deadline to respond may be extended for a maximum of two extensions, provided that the aggregate period inclusive of the initial period allowed to file the response shall not exceed six months from the mailing date of the official action. A substantive examination takes approximately two years and depends on the complexity of the issues in question, as well as the speed by which the applicant responds to the objections.

If the Patent Examiner decides that the application may be published, the IPOPHIL issues a Notice of Allowance and the application is published. A Notice of Issuance of Letters of Patent Certificate will then be issued once the Letters Patent are ready.

Similar to patents, once an application for a utility model or industrial design is filed, it undergoes a formal examination whereby the required documents are checked for completeness. A report is then issued to the applicant or its agent indicating that all required documents have been filed and the application is complete. Otherwise, the IPOPHL will issue a report indicating the documents still to be submitted or matters that need to be clarified by the applicant.

If no further issues are found in the formal examination, the application is published. After 30 days from publication, the allowance of the application for registration ensues and the Certificate of Registration is issued. This registration of a utility model or industrial design is published in the IPOPHL Gazette.

In terms of the timeframe for patent applications to be granted protection, invention patents are usually granted approximately five years from the filing date, depending on the complexity of the application, the number of claims, the speed with which the applicant responds to each office action of the IPOPHL and whether or not voluntary amendments are filed by the applicant. For utility models and industrial designs, registration may be obtained within approximately nine months from the filing date.

Invention patents have a validity of 20 years from the filing date. However, for PCT applications, the term of protection is reckoned from the international filing date. For utility models, the term of protection is seven years from the filing of the application. The term of protection for invention patents and utility models is not subject to renewal.

Part of the maintenance requirements of an invention patent is the payment of annual fees, starting four years from the date the application is published. There is no such requirement for utility models and industrial designs.

9.2 Trademarks

The primary legislation governing trademarks in the Philippines is the Intellectual Property Code. In addition to domestic legislation, the Philippines is a party to the following international trademark agreements:

- the Agreement on Trade-Related Aspects of Intellectual Property Rights (the ‘TRIPS Agreement’);
- the Paris Convention for the Protection of Industrial Property; and
- the Madrid Protocol.

The Intellectual Property Code defines a ‘trademark’ as any visible sign capable of distinguishing the goods (trademark) or services (service mark) of an enterprise, including a stamped or marked container of goods. From the definition of a trademark in the Philippines, it seems apparent that this jurisdiction does not accord protection marks not perceptible to the human eye.

A trademark is unregistrable in the Philippines if it falls under any of the absolute or relative grounds for refusal under section 123 of the Intellectual Property Code. Absolute grounds include immoral, generic, descriptive, non-distinctive or customary marks, while relative grounds cover confusing similarity with previously registered or earlier filed marks and with marks that are well known internationally and/or in the Philippines.

Marks that are wholly descriptive, consist of the shape of a good or comprise of a colour may be registered if they become distinctive in connection with the applicant’s goods and/or services as a result of extensive commercial use in the Philippines for at least five years before the claim of distinctiveness is made.

In order to apply for the registration of a trademark, a completed application form should be submitted to the IPOPHL, accompanied by a reproduction of the mark applied for. The reproduction of the mark may be in printed or electronic form, which should be in .jpg file format. A POA is needed for an application to proceed to substantive examination, but its submission is not required for an application to be issued with a filing number and filing date. The submission of a scanned POA is sufficient. The POA does not need to be attested, notarised, legalised, authenticated or apostilled. Trademark applications may be submitted in printed form or through electronic filing using the eTMfile system of the IPOPHL.

Upon the completion of the formal requirements for a trademark application, the application undergoes substantive examination, where the examiner determines the registrability of the trademark based on section 123 of the Intellectual Property Code. If there are no objections from the IPOPHL regarding the registrability of the applied-for trademark, a Notice of Allowance is issued requiring the applicant to pay the publication for opposition fee. The applicant may simultaneously pay the issuance of certificate and a second publication fee alongside the publication for opposition fee to expedite the registration. Once the publication fee is paid, the trademark will then be published in the IPOPHL e-Gazette for third-party oppositions. If no opposition to the registration of the mark is filed within 30 days from its publication, the mark shall be deemed registered on the day following the expiration of the 30-day period. A trademark registration is valid for ten years from the date of registration.

Unlike in other countries, use of a trademark is not a prerequisite for its registration in the Philippines, but use is required to maintain the application or registration of a mark, whether for national applications or international registrations via the Madrid Protocol. Trademark use is supported through the submission of a Declaration of Actual Use (DAU) within:

- three years from the filing date, international registration date or date of subsequent designation;
- one year following the fifth anniversary of the date of registration or date of grant of protection;
- one year from the date of renewal; or
- one year from the fifth anniversary of each renewal.

The DAU should be accompanied by any of the acceptable proofs of use listed in Rule 210 of the Philippine Trademark Regulations, 2017.

Failure to file the DAU and proofs of use within any of the specified periods will mean the automatic refusal of an application or the cancellation of a registration. Unjustified non-use of a registered mark for an uninterrupted period of three years may also be the basis of a cancellation action.

In lieu of the DAU, an applicant or registrant may file a declaration of non-use (DNU) if non-use of the mark is based on any of the following circumstances outside the owner's control, except for a lack of funds:

- where the registrant or applicant is prohibited from using the mark in commerce because of a requirement imposed by another government agency before placing the goods in the market or rendering services;
- where a restraining order or injunction was issued by the Bureau of Legal Affairs, the courts or quasi-judicial bodies prohibiting the use of the mark; or
- where the mark is the subject of an opposition or cancellation case.

Generally, the DNU may be submitted only in lieu of the third-year DAU. However, if the use of a mark has been interrupted or discontinued pending litigation, a DNU may be submitted instead of the relevant DAU.

9.3 Copyright

The Intellectual Property Code also provides for copyright protection over original intellectual creations in the literary and artistic domain. Copyright over such work exists from the moment of its creation, without need for registration.

Apart from the Intellectual Property Code, the following international treaties/conventions in relation to the protection of copyright and other related rights also apply to copyrighted subject matter in the Philippines:

- the Berne Convention for the Protection of Literary and Artistic Works;
- the Rome Convention for the Protection of Performers, Producers of Phonograms and Broadcasting Organizations;
- the TRIPS Agreement;
- the WIPO Performances and Phonograms Treaty, 2002; and
- the WIPO Copyright Treaty;

Copyrightable works may be registered and deposited with the Copyright Division of the National Library of the Philippines, the Supreme Court Library (only with respect to works in the field of law), and the Bureau of Copyright and Other Related Rights, as deputised by the National Library. Since registration is not a prerequisite for copyright protection, the purpose of the registration and deposit is only to complete the records of the National Library and the Supreme Court Library. Deposited works are considered to be public records and are open to public inspection, subject to safeguards that may be issued by the National Library.

In the Philippines ideas, procedures, systems, methods or operations, concepts, principles, discoveries or mere data as such are not subject to copyright protection, even if they are expressed, explained, illustrated or embodied in a work. News of the day and other miscellaneous facts having the character of press information, as well as any official text of a legislative, administrative or legal nature, and the legal translations thereof, are also not protected under copyright.

It is important to note that only a natural person may be considered as an author or the original creator of a copyrightable work. While a corporation cannot be considered as an author of a work, copyright over a work may be transferred to the juridical entity by assignment.

With respect to works created in the course of employment, copyright belongs to the employee if the work is not part of his or her regular duties, even if the author uses the time, facilities and materials of the employer. On the other hand, if the work is the result of the performance of the author's regularly assigned duties, the employer owns the copyright, unless there is an express or implied agreement to the contrary.

If the work is commissioned outside of an employer–employee relationship (ie, consultancy or freelance), the copyright is owned by the author although the work itself is owned by the person who commissioned and paid for it, unless there is a written stipulation to the contrary.

The copyright owner's rights under section 177 (Economic Rights) of the Intellectual Property Code are transmissible. To be valid, the assignment or licensing of a copyright must be in writing and should appear in a public instrument in order to be effective against third parties. The rights under section 193 (Moral Rights) of the Intellectual Property Code are not transmissible. However, these rights may be waived by a written instrument subject to statutory limitations.

9.4 Designs

The protection of industrial designs in the Philippines falls under the regime of patents. However, the only substantive requirement for the grant of an industrial design patent is novelty. Industrial designs may also be copyrighted if they satisfy the original and artistic requirements for copyright protection.

The process for a grant of an industrial design is the same as that for a utility model (see 9.2 above).

Industrial designs have a term of protection of five years from the filing date of the application and may be renewed for no more than two consecutive five-year terms.

Chapter 10: Financing

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10.1 Modes of entry for foreign banks

Under Republic Act No 10641, the Monetary Board may authorise foreign banks to operate in the Philippine banking system through any of the following modes of entry:

- by acquiring, purchasing or owning up to 100 per cent of the voting stock of an existing bank;
- by investing in up to 100 per cent of the voting stock of a new banking subsidiary incorporated under the laws of the Philippines; or
- by establishing branches with full banking authority.

10.2 Qualification and minimum capital requirement for foreign banks

A foreign bank that intends to operate in the Philippines must be:

- widely owned and publicly listed in the country of origin, unless the foreign bank applicant is owned and controlled by the government of its country of origin; and
- established, reputable and financially sound.

If a foreign bank is owned and controlled by a holding company, the aforementioned requirement may apply to the holding company.

Moreover, the BSP will also consider the following factors in selecting the foreign banks allowed to enter the Philippine banking system:

- geographic representation and complementation;
- strategic trade and investment relationships between the Philippines and the home country of the foreign bank;
- relationship between the applicant bank and the Philippines;
- demonstrated capacity, global reputation for financial innovations and stability in the competitive environment of the applicant bank;
- reciprocity rights enjoyed by Philippine banks in the applicant's country; and
- willingness fully to share banking technology.

The subsidiary or branch of a foreign bank is also required to comply with the minimum capital requirements applicable to a domestic bank in the same category.

10.3 Qualifications of subscribers/directors/officers of banks

All the incorporators, subscribers, directors and officers of the bank, present or proposed, must have the following qualifications:

- be persons of integrity and of good credit standing in the business community;
- have adequate financial strength to pay the proposed subscription in the bank;
- not have been convicted of any crime involving moral turpitude, and unless otherwise allowed under provisions of law, not be officers or employees of government agencies, instrumentalities, departments or offices charged with the supervision or granting of loans to banks;
- not be an appointive or elective public official, full or part-time, and at the same time serving as an officer of a bank, except when such service is incidental to the financial assistance provided by the government or a government-owned or controlled corporation to the bank, or except in cases allowed under existing laws;
- hold the qualifications provided in the Manual of Regulations for Banks; and
- hold none of the disqualifications prescribed under the Manual of Regulations for Banks.

10.4 Registration of direct foreign equity investment in a domestic corporation

Inward foreign investment must be registered with the BSP within one year from the date of inward remittance (if in cash) or from the date of the actual transfer of assets to the Philippines (if in kind) if the foreign investor intends to source the foreign exchange requirement needed to service the repatriation of capital and remittance of cash dividends/profits/earnings accruing on foreign investment from the Philippine banking system (ie, authorised agent banks or their affiliate/subsidiary foreign exchange corporations).

Without the required BSP registration, the foreign investor may source foreign exchange from internally generated revenue or from outside the Philippine banking system, such as foreign exchange dealers, money changers and remittance agents.

The registration of inward investment shall be supported by: (1) proof of funding; and (2) proof of an actual investment made by the non-resident investor.

After complying with the requirements to register the inward remittance, a Bangko Sentral Registration Document is issued in the name of the domestic corporation.

10.5 Registration of foreign loans

Foreign loans must be registered with the BSP if the company intends to source foreign currency from the Philippine banking system in connection with the repayment of the principal amount or the interest of the foreign loan.

Without the required BSP registration, the borrower may still source foreign exchange from internally generated revenue or from outside the Philippine banking system, such as foreign exchange dealers, money changers and remittance agents.

In order to register a private-sector foreign loan, the borrower must:

- submit a notice to the BSP supported with a copy of the signed covering agreement(s), within one month from the date of signing (the 'Notice');
- send a notification to the BSP for: (1) any changes in the loan's financial terms and conditions; or (2) cancellation (whether partial or in full) of the loan/commitment/agreement, within 15 banking days from the availability of information/signing of the amended or supplemental agreement/effectivity date, as the case may be, for monitoring purposes;
- apply for loan registration with the BSP within one month from drawdown date (for short-term loans) and within six months from utilisation of proceeds (for medium and long-term loans) (the 'Application for Loan Registration'); and
- a foreign borrowings plan for medium and long-term loans.

In the event that the signing date and drawdown occur simultaneously, the Notice and the Application for Loan Registration may be filed simultaneously.

After complying with the requirements to register the loan, a Bangko Sentral Registration Document is issued in the name of the domestic corporation.

Chapter 11: Privacy laws and data protection

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The Data Privacy Act, 2012 is the primary law governing the protection and processing of personal data in the Philippines. Personal data refers to all types of personal information. Personal information refers to any information, whether recorded in a material form or not, from which the identity of an individual is apparent or can be reasonably and directly ascertained by the entity holding the information, or when put together with other information, would directly and certainly identify an individual. Personal data is classified as *sensitive* personal information when it refers to personal information: (1) about an individual's race, ethnic origin, marital status, age, colour, or religious, philosophical or political affiliations; (2) about an individual's health, education, genetic or sexual life, or to any proceeding for any offence committed or alleged to have been committed by such an individual, the disposal of such proceedings or the sentence of any court in such proceedings; (3) issued by government agencies peculiar to an individual, which includes, but is not limited to, social security numbers, previous or current health records, licences or their denial, suspension or revocation, and tax returns; or (4) specifically established by an executive order or an act of Congress to be kept classified. Processing, meanwhile, refers to any operation or any set of operations performed upon personal data including, but not limited to, the collection, recording, organisation, storage, updating or modification, retrieval, consultation, use, consolidation, blocking, erasure or destruction of such data.

11.1 Registration of data processing systems

Personal information controllers (PICs) and personal information processors (PIPs) with fewer than 250 employees are not required to register their data processing systems, unless the processing carried out is likely to pose a risk to the rights and freedoms of data subjects, is not occasional or includes sensitive personal information of at least 1,000 individuals. Processing of personal data will not be considered occasional if processing constitutes a core activity of the PIC or PIP. Processing operations that pose a risk to data subjects are those involving information that would be likely to affect national security, public safety, public order or public health; information required by applicable laws or rules to be confidential; vulnerable data subjects (eg, minors, the mentally ill, asylum seekers and elderly patients); automated decision-making; or profiling.

The National Privacy Commission (NPC) has identified the processing of personal data by the following sectors or institutions as either likely to pose a risk to the rights and freedoms of data subjects or not occasional:

- telecommunications networks, internet service providers and other entities or organisations providing similar services;
- business process outsourcing companies;

- universities, colleges and other institutions of higher learning, alongside all other schools and training institutions;
- hospitals, including primary care facilities, multi-specialty clinics, custodial care facilities, diagnostic or therapeutic facilities, specialised outpatient facilities and other organisations processing genetic data;
- providers of insurance undertakings, including life and non-life companies, pre-need companies and insurance brokers;
- bank and non-bank financial institutions;
- businesses involved mainly in direct marketing and networking, and companies providing reward cards and loyalty programmes;
- pharmaceutical companies engaged in R&D;
- PIPs processing personal data for a PIC included in the preceding items and data processing systems involving automated decision-making; and
- government branches, bodies or entities, including the national government, agencies, bureaus or offices, constitutional commissions, local government units, and government-owned and controlled corporations.

Automated decision-making refers to wholly or partially automated decision-making processes that significantly affect the data subject. This includes profiling based on socio-economic situation, political or religious beliefs, behavioural or marketing activities, electronic communication data and financial data.

PIC and PIP registration with the NPC is completed in two phases. Phase I involves the appointment of the PIC or PIP's data protection officer and the notification of the NPC of such an appointment. Under Phase II, the data protection officer shall provide all relevant information regarding its data processing systems through the NPC online registration system, such as:

- purpose and mandate of the entity;
- all existing policies relating to data governance, data privacy and information security;
- data processing certifications attained by the PIC or PIP, including personnel;
- description of the data processing systems, including the name of the system; purposes or purposes of processing; whether processing is done as PIC, PIP or both; whether the system is outsourced or subcontracted; categories of data subjects and their personal data or categories thereof; recipients or categories of recipients to whom the personal data might be disclosed; and whether personal data is transferred outside the Philippines; and
- notification regarding any automated decision-making operation.

11.2 Notification of a personal data breach

The Data Protection Act defines a personal data breach as a breach of security leading to the accidental or unlawful destruction, loss, alteration, unauthorised disclosure of or access to personal data transmitted, stored or otherwise processed. A personal data breach may be in the nature of: (1) an availability breach resulting from the loss or accidental or unlawful destruction of personal data; (2) an integrity breach resulting from the alteration of personal data; and/or (3) a confidentiality breach resulting from the unauthorised disclosure of or access to personal data.

Notification to the NPC shall be required upon knowledge of or when there is reasonable belief by the PIC that a personal data breach requiring notification has occurred, under the following conditions:

- the personal data involves sensitive personal information or any other information that may be used to enable identity fraud; for this purpose, 'other information' shall include, but not be limited to: data about the financial or economic situation of the data subject; usernames, passwords and other login data; biometric data; copies of identification documents, licences or unique identifiers like a PhilHealth number, Social Security System number, Government Service Insurance System number or Tax Identification Number; or other similar information, that may be made the basis of decisions concerning the data subject, including the grant of rights or benefits;
- there is reason to believe that the information may have been acquired by an unauthorised person; and
- the PIC or the NPC believes that the unauthorised acquisition is likely to give rise to a real risk of serious harm to any affected data subject.

The PIC must notify the NPC, in instances when this is required, within 72 hours upon knowledge of or the reasonable belief by the PIC that a personal data breach has occurred. Notification may only be delayed to the extent necessary to determine the scope of the breach, to prevent further disclosure or to restore reasonable integrity to the information and communications system. The PIC need not be absolutely certain of the scope of the breach prior to notification. Its inability immediately to secure or restore integrity to the information and communications system shall not be a ground for any delay in notification if such a delay would be prejudicial to the rights of the data subjects. Delay in notification shall not be excused if it is used to perpetuate fraud or to conceal the personal data breach.

Failure to notify shall be presumed if the NPC does not receive notification from the PIC within five days from the knowledge of or upon a reasonable belief that a personal data breach occurred. There shall be no delay in the notification if the breach involves at least 100 data subjects, or the disclosure of sensitive personal information will harm or adversely affect the data subject. In both instances, the NPC shall be notified within the 72-hour period based on available information. A full report of the personal data breach must be submitted within five days, unless the PIC is granted additional time by the NPC to comply.

Chapter 12: Competition law

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The Philippine Competition Act generally prohibits three practices: (1) anti-competitive agreements; (2) abuse of a dominant position; and (3) anti-competitive mergers.

12.1 Prohibited activities

12.1.1 Anti-competitive agreements

Prohibited anti-competitive agreements can be classified into the following:

- hardcore cartel agreements, price-fixing agreements and bid manipulation agreements between or among competitors, which are per se prohibited;
- agreements among competitors that have the object or effect of substantially preventing, restricting or lessening competition by: (1) setting, limiting or controlling production, markets, technical development or investment; or (2) dividing or sharing the market, whether by volume of sales or purchases, territory, type of goods or services, buyers or sellers or any other means; and
- other agreements that have the object or effect of substantially preventing, restricting or lessening competition.

12.1.2 Abuse of a dominant position

An entity is considered dominant if it enjoys a position of economic strength that allows it to control the relevant market independently from its competitors, customers, suppliers or consumers. The Philippine Competition Commission (the 'Commission') can also consider other factors in evaluating whether an entity is dominant, and there is a rebuttable presumption of market dominance if the market share of an entity in the relevant market is at least 50 per cent or such other threshold that may be set by the Commission.

When an entity is deemed to be dominant, its performance of certain acts will be considered an abuse of such a dominant position and could subject the entity to penalties. Examples of an abuse of a dominant position include:

- predatory pricing;
- imposing barriers to entry or barriers to growth;
- imposing tying or bundling obligations in transactions;
- discriminating on pricing and terms and conditions;
- imposing unfair prices; and
- limitation of markets, production or technical development.

12.2 Consequences of a breach

The entry into prohibited anti-competitive agreements and the commission of abuses of dominant position have severe consequences.

12.2.1 Remedies

The Commission may issue injunctions, require divestment and require disgorgement of excess profits.

12.2.2 Administrative fines

The Commission may impose administrative fines of up to PHP 100m for the first offence, and between PHP 100m and PHP 250m for the second offence on entities found to have entered into prohibited anti-competitive agreements or committed abuses of a dominant position.

12.2.3 Criminal penalties

Fines of between PHP 50m and PHP 250m may be imposed by the courts on entities that enter into those defined anti-competitive agreements between competitors that are either prohibited per se or that have the object of substantially preventing, restricting or lessening competition by setting, limiting or controlling production, markets, technical development or investment, or by dividing or sharing the market. Directors and management personnel of such entities who knowingly and wilfully participated in the criminal offences may be sentenced to imprisonment for two to seven years.

Treble damages may be imposed by the Commission or courts, as the case may be, where the violation involves the trade or movement of basic necessities and prime commodities.

12.3 Pre-merger and pre-acquisition notification

The Philippine Competition Act imposes mandatory notification requirements on covered transactions. Parties to a transaction will be prohibited from closing until the transaction is cleared by the Commission or the lapse of 30 days from the date that substantive review (or Phase 1 review) of the transaction commenced, if no action is taken by the Commission. Within the 30-day period, the Commission can request additional information on the transaction, and such a request will have the effect of triggering a Phase 2 review and extending the review period by 60 days, but in no case will the review period exceed 90 days from commencement of the Phase 1 review unless the statutory periods are waived by the parties.

If the Commission determines that the M&A agreement will have an anti-competitive effect, it may outrightly prohibit the implementation of the agreement; prohibit the implementation of the agreement unless modifications are made to its terms; or prohibit the implementation of the agreement unless the relevant parties enter into other agreements.

Non-compliance with the notification requirement will result in the imposition of a fine of between one and five per cent of the value of the transaction, in addition to the agreement being deemed void.

Chapter 13: Dispute resolution

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13.1 Structure of the courts

The Philippine judiciary consists of a hierarchy of courts, with the Supreme Court at the top tier, exercising administrative supervision over all courts and court personnel.

The Supreme Court has both original and appellate jurisdiction. It exercises original jurisdiction over cases affecting ambassadors, other public ministers and consuls, and over petitions for *certiorari*, prohibition, *mandamus*, *quo warranto* and *habeas corpus*. It also has original jurisdiction over writs of *amparo*, *habeas data a*nd the environmental writ of *kalikasan*. It exercises appellate jurisdiction to review, revise, reverse, modify or affirm final judgments and orders of the lower courts in:

- all cases in which the constitutionality or validity of any treaty, international or executive agreement, law, presidential decree, proclamation, order, instruction, ordinance or regulation is in question;
- all cases involving the legality of any tax, impost, assessment or toll, or any penalty imposed in relation thereto;
- all cases in which the jurisdiction of any lower court is in issue;
- all criminal cases in which the penalty imposed is *reclusiónperpetua* or higher; and
- all cases in which only an error or question of law is involved.

In the next tier below the Supreme Court are three collegiate courts: the Court of Appeal, the Court of Tax Appeals and the Sandiganbayan.

The Court of Appeals is the primary appellate court of the Philippines, sitting in three stations: the City of Manila, Cebu and Cagayan de Oro. It is assigned to review cases elevated to it from the Regional Trial Courts (RTCs), as well as quasi-judicial agencies, such as the Civil Service Commission, SEC, National Labor Relations Commission and Land Registration Authority. The Court of Appeals also reviews cases where the sentence is *reclusión perpetua* or life imprisonment, as well as decisions of the Office of the Ombudsman in administrative disciplinary cases.

The Court of Tax Appeals is a special collegiate court with exclusive jurisdiction to review appeal decisions in cases involving disputed assessments, refunds of internal revenue taxes, fees or other charges, penalties in relation thereto or other matters arising under the National Internal Revenue Code. It also exercises original jurisdiction over all criminal offences arising from violations of the Tax or Tariff Codes and other laws administered by the Bureau of Internal Revenue or the Bureau of Customs.

The Sandiganbayan is an anti-graft court with jurisdiction to try public officers with a salary grade of 27 and above charged with criminal cases involving the violation of the country's laws on graft and corruption and corresponding civil cases for the recovery of civil liability arising from the offence. Likewise, the Sandiganbayan is vested with appellate jurisdiction over final judgments, resolutions or orders of the RTCs in the exercise of their original or appellate jurisdiction over crimes and civil cases falling within the original exclusive jurisdiction of the Sandiganbayan, but which were committed by public officers below a salary grade of 27.

The next tier consists of the RTCs, which have both original and appellate jurisdiction. In exercising the former jurisdiction, RTCs act as trial courts, receiving evidence in the first instance from the parties to a case falling within its jurisdiction. In exercising the latter jurisdiction, the RTCs act as a court of appeal over the decisions of the first-level courts.

Finally, the lowest tier consists of the Metropolitan Trial Courts, which are established in Metropolitan Manila; the Municipal Trial Courts in Cities, in every city that does not form part of Metropolitan Manila; the Municipal Trial Courts, established in municipalities; and Municipal Circuit Trial Courts, created in each circuit comprising such cities and/or municipalities as grouped by law.

13.2 Arbitration

Arbitration is expressly sanctioned by law as an alternative mode of dispute resolution. Congress enacted Republic Act No 9285, also known as the ADR Act, 2004, which provided the much-needed legislation to institutionalise arbitration in the Philippines. The ADR Act addressed most of the inadequacies of its predecessor, Republic Act No 876. The ADR Act governs both domestic and international commercial arbitration, and has adopted the 1985 UNCITRAL Model Law as a complement to the earlier accession of the Philippines to the New York Convention on 19 June 1958, which the Philippines ratified on 6 July 1967.

The Supreme Court issued Administrative Matter No 076-11-08-SC, on 1 September 2009, also known as the Special Rules of Court on ADR, which provided for the procedural guidelines for both domestic and international arbitration, as well as the enforcement of arbitral awards in the Philippines.

13.3 Other forms of dispute resolution

In addition to arbitration, the other modes of dispute resolution provided for under the ADR Act are mediation, early neutral evaluation, mini-trial, mediation arbitration or any combination thereof.

Mediation is defined as a voluntary process in which a mediator, selected by the disputing parties, facilitates communication and negotiation, and assists the parties in reaching a voluntary agreement regarding a dispute.

'Early neutral evaluation' means an ADR process wherein parties and their lawyers are brought together early in the pre-trial phase to present summaries of their cases and to receive a non-binding assessment by an experienced neutral person, with expertise in the subject matter or substance of the dispute.

'Mini-trial' means a structured dispute resolution method in which the merits of a case are argued before a panel comprising senior decision-makers, with or without the presence of a neutral third person, before which the parties seek a negotiated settlement.

'Mediation-arbitration' is a two-step dispute resolution process involving mediation followed by arbitration.

Chapter 14: Other

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14.1 Regulation of payment systems

A payment system provides a channel for the transfer of funds among banks and other institutions to discharge obligations arising from economic and financial transactions to reduce the cost of exchanging goods and services. Republic Act No 11127, otherwise known as the National Payment Systems Act, grants the BSP authority over the maintenance of a safe, efficient and reliable payment system. The law requires the registration of payment system operators with the BSP and for said operators to incorporate as stock corporations. By way of exception, those operated by the BSP shall not be required to do so. Payment systems operators must first secure a certificate of authority to register from the Monetary Board before seeking registration to do business in the Philippines from the SEC. Acting as an operator without the requisite authority from the BSP may open a participant of a designated payment system, its directors and officers to fines not exceeding PHP 1m for each transactional violation or PHP 100,000 per day for each continuing violation. Should any profit be gained or any loss avoided by reason thereof, an additional fine of no less than the amount of profit gained or loss avoided, but not more than three times the profit gained or loss avoided, may be imposed.

14.2 Ease of doing business

Republic Act No 11032, otherwise known as the Ease of Doing Business Act, mandates all government offices and agencies including local government units and other government corporations, agencies and instrumentalities to reengineer their systems and procedures to reduce bureaucratic red tape and processing time.

The processing of applications for government-issued documents must be acted upon within the prescribed processing time stated in the Citizen's Charters to be enacted by government offices, which should be no longer than: (1) three days for simple transactions; (2) seven days for complex transactions; and (3) 20 days for highly technical transactions. During the processing period, government officers or employees should have no contact with the applicant unless necessary. The Ease of Doing Business Act limits the signatories of any document to a maximum of three signatures representing officers directly supervising the office or agency and requires an explanation in writing for any denial of application or request for access by the citizens. To ensure the efficiency and reliability of the system, all heads of offices or agencies are responsible for the implementation of the law.

14.3 Regulations on exports and imports

The Bureau of Customs administers the provisions of Republic Act No 10863 or the Customs Modernisation and Tariff Act (CMTA) and exercises supervision and control on all Philippine import and export activities. All goods imported into the Philippines are subject to duty and tax upon importation, except those that the CMTA expressly excludes. Under the CMTA, importation begins when the carrying vessel or aircraft enters Philippine territory with the intent to unload therein.

All imported goods are subject to a lodgement of goods declaration. The two types of goods declaration are: (1) informal entry, which covers goods of a commercial nature with free on board or free carrier value of less than PHP 50,000 and personal and household effects or goods, not in commercial quantity; and (2) formal entry, which covers goods of a commercial nature with free on board or free carrier value of not less than PHP 50,000. Within 15 days from the date of discharge of the last package from the vessel or aircraft, a goods declaration must be lodged. This period within which to file a declaration may be extended for another 15 days, filed prior to the expiration of the original period, only on valid grounds. Failure to lodge the goods declaration constitutes an implied abandonment of goods.

Goods classified by the Department of Trade and Industry (DTI) requiring mandatory product certification must secure an Import Commodity Clearance prior to sale of the goods imported.

For exportation, after securing the necessary registrations with the DTI, SEC or Cooperative Development Authority, an exporter should utilise the Client Profile Registration System of the Bureau of Customs. Registration should be made with the DTI if accredited under the Export Development Act or a coffee exporter; with the BOI if registered therewith; or with the PEZA if located in an area governed by the PEZA.

Depending on the products to be exported, additional permission by way of an Export Clearance is required from various government agencies concerned, such as:

- Bureau of Animal Industry for animals and animal products;
- Food and Drug Administration for food, drugs, cosmetics, toys and device products;
- National Food Authority for rice;
- National Museum for artwork more than 100 years old; and
- Sugar Regulatory Administration for sugar and molasses.

Meanwhile, businesses operating within SEZs or Freeport Zones are exempt from paying taxes and tariffs on imported raw materials and manufacturing equipment in the main SEZs, such as the Clark SEZ, Subic SEZ and John Hay SEZ.

14.4 Money laundering compliance

The Anti-Money Laundering Act, 2001 (AMLA), as amended, requires covered persons to comply with reportorial requirements imposed by the Anti-Money Laundering Council, specifically with regard to covered and suspicious transactions that may signal acts of money laundering. ‘Covered persons’ broadly include natural and juridical persons supervised and regulated by the BSP, Insurance Commission and SEC. Also covered are Designated Non-Financial Business and Professions, which include jewellery dealers in precious metals and stones, in addition to company service providers and persons engaged in the management of client money and finances, including lawyers, accountants and other professionals.

‘Covered transactions’ refer to: (1) those transactions in cash or other equivalent monetary instrument involving a total amount in excess of PHP 500,000 within one banking day; (2) a transaction with or involving jewellery dealers, dealers in precious metals and dealers in precious stones in cash or other equivalent monetary instrument exceeding PHP 1m; and (3) a casino cash transaction exceeding PHP 5m or its equivalent in other currency. ‘Suspicious transactions’, meanwhile, are transactions with covered institutions, regardless of the amounts involved, where any of the following suspicious circumstances exist:

- there is no underlying legal or trade obligation, purpose or economic justification;
- the client is not properly identified;
- the amount involved is not commensurate with the business or financial capacity of the client;
- taking into account all known circumstances, it may be perceived that the client’s transaction is structured in order to avoid being the subject of reporting requirements under the AMLA;
- any circumstance relating to the transaction that is observed to deviate from the profile of the client and/or the client’s past transactions with the covered institution;
- the transaction is in any way related to an unlawful activity or offence under the AMLA that is about to be, is being or has been committed; or
- any transaction that is similar or analogous to any of the foregoing.

Notwithstanding the provisions of Republic Act No 1405, or the Bank Secrecy Law, and other regulations, the Anti Money Laundering Council is granted the power to inquire into or examine any particular deposit or investment, including related accounts, with any banking institution or non-bank financial institution upon the order of any competent court based on an *ex parte* application in cases of violations of the AMLA. An inquiry occurs when it has been established that there is probable cause that the subject funds are related to an unlawful activity or a money laundering offence.

Vietnam

Chapter 1: Business and corporate structures

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In Vietnam, there are four forms of enterprises: limited liability company (LLC), joint stock company (JSC), partnership company (PC) and private enterprise (PE). Of these four forms, the LLC and JSC are the most preferred and common forms of enterprise for foreign investors due to their significant advantages compared with the PC and the PE.

Below is a brief comparison of the basic characteristics of each enterprise:

Criteria	LLC	JSC	PC	PE
Ownership	Quantity: 1–50 Qualification: a member can be either an individual or an organisation	Quantity: ≥ 3 Qualification: a shareholder can be either an individual or an organisation	Quantity: ≥ 2 general partners; and ≥ 0 limited partners Qualification: a general partner must be an individual; a limited member can be either an individual or an organisation	Quantity: 0 Qualification: the sole owner must be an individual
Liability of owners	Members of an LLC generally bear liability for the debts and obligations of the LLC only to the extent of their contributed capital	Shareholders of a JSC generally bear liability for the debts and obligations of the JSC only to the extent of their contributed capital	General partners bear liability for the debts and obligations of the PC to the extent of all their assets Limited partners bear liability for the debts and obligations of the PC to the extent of their contributed capital	Sole owners bear liability for the debts and obligations of the PE to the extent of all their assets
Securities issuance	LLCs cannot issue shares LLCs may issue only straight corporate bonds to raise capital	JSCs may issue all kind of shares and corporate bonds to raise capital	PCs cannot issue securities of any kind	PEs cannot issue securities of any kind

1.1 Incorporation process

Upon completion of investment procedures specifically designated to investment projects by foreign investors, that is, obtaining an in-principle approval and an investment registration certificate (IRC), a foreign investor must complete an enterprise registration certificate (ERC) application in order to set up his/her business. The content of the ERC includes material corporate information, such as corporate name, tax code, charter capital, registered address, legal representative(s), information on general partners in the case of a PC and information on the owner or members in the case of an LLC. Upon issuance, information contained in the ERC is published on the National Portal of Business Registration (NPBR).

1.2 Ongoing reporting and disclosure obligations

Vietnamese law sets forth various obligations on the disclosure and reporting of information related to Vietnamese enterprises and their investors.

For instance, enterprises must have the content of their ERC and other corporate information made available on the NPBR. Vietnamese enterprises also have an obligation to report to licensing authorities any changes to the ownership of foreign shareholders, board of management (BOM) members, controllers and directors/general directors.

Moreover, in the case of a JSC with an operational website, information on the charter; resumes of all the JSC's BOM members, controllers, directors and general directors; the JSC's annual financial statements approved by its General Meeting of Shareholders (GMSs), as well as operation outcome assessment reports of the JSC's BOM and control committees must be publicised on the JSC's website.

In addition, public JSCs are subject to more onerous disclosure obligations, including, but not limited to, the disclosure of any information that might affect their securities' prices, information on stock offerings and capital utilisation reports.

1.3 Management structures

In practice, PEs are not a common enterprise form used for foreign investment in Vietnam, therefore this section concentrates on the three other forms: LLCs, JSCs and PCs.

1.3.1 LLC (multi-member LLC and single-member LLC)

Multi-member LLC

The management structure of a multi-member LLC comprises the Members' Council (MC), the Director/General Director and the Control Committee.

MC

The MC is composed of all members of the multi-member LLC and is the highest decision-making body of the multi-member LLC.

Meetings of the MC can be held periodically as prescribed in the charter of the multi-member LLC, but not less than once per year. Extraordinary meetings of the MC can be held upon the request of the Chair of the MC, or one or more members of the MC representing no less than ten per cent of the charter capital of the multi-member LLC.

The quorum for an MC meeting of a multi-member LLC is constituted when no less than 65 per cent of the charter capital of the multi-member LLC is represented at the meeting.

Resolutions of the MC in a physical meeting are passed by the affirmative votes of no less than 65 per cent of the total capital contribution of the members in attendance. The affirmative votes of no less than 75 per cent of the total capital contribution of the attending members are required for resolutions approving: (1) disposals of assets worth 50 per cent or more of the total asset value of the multi-member LLC stated in its latest financial statements; (2) any amendments and/or supplements to its charter; and (3) restructuring and/or dissolution of the multi-member LLC.

Where the resolutions are passed in writing in the form of opinion polls, the resolutions are passed upon the affirmative votes of MC members representing no less than 65 per cent of the charter capital of the multi-member LLC.

Director/General Director

A Director/General Director is the person in charge of managing day-to-day business affairs of the multi-member LLC and bears responsibility before the MC for the exercise and the performance of his/her rights and duties. The Chair of the MC can also hold the position of a Director/General Director.

Control Committee

The management structure of any multi-member LLC with 11 members or more must include a Control Committee. In cases of multi-member LLCs with fewer than 11 members, a Control Committee may be established if requested by the multi-member LLCs.

The rights, obligations, appointment criteria, conditions and working regulations of the Control Committee (including the head of the Control Committee) are set out in the charter of the multi-member LLC.

Single-member LLC

The management structure of a single-member LLC comprises the MC or President, the Director/General Director and the Controller. Generally, the management structure of a single-member LLC is of similar features to that of a multi-member LLC, except for those stated below.

MC

The MC is not part of the management structure of a Single Member LLC owned by an individual.

Unlike the MC in a multi-member LLC, the MC in a single-member LLC is composed of three to seven authorised representatives appointed by the owner of the single-member LLC.

The quorum for a meeting of a single-member LLC is constituted when no less than two-thirds of MC members are present.

Resolutions of the MC in a physical meeting are passed by the affirmative votes of a simple majority of MC members in attendance. The affirmative votes of three-quarters of MC members in attendance are required for resolutions approving: (1) assignment of all or part of the charter capital of the single-member LLC; (2) any amendments and supplements to the charter; and (3) restructuring of the single-member LLC.

President

Unlike a multi-member LLC, the owner of a single-member LLC may opt to appoint only one authorised representative as the President in lieu of an MC. In the case of a single-member LLC owned by an individual, the owner holds the position of President.

Controller

In the case of a single-member LLC owned by an organisation, the owner decides and appoints one or Controllers. However, a single-member LLC owned by an individual is not required to have a Controller.

1.3.2 JSC

The management structure of a JSC comprises the GMS, BOM, Control Committee and Director/General Director.

GMS

The GMS is the highest decision-making body of a JSC and is composed of all shareholders owning shares in the JSC with voting rights.

The GMS is convened periodically once per annum. Extraordinary Meetings of Shareholders can be convened where: (1) the BOM deems it necessary; (2) the minimum number of members of the BOM and/or Control Committee are not satisfied; (3) upon the request of the Control Committee or a shareholder/a group of shareholders holding ten per cent or more of the total ordinary shares for a consecutive period of six months; and (4) other circumstances prescribed in the charter of the JSC.

The quorum for the GMS is constituted when no less than 51 per cent of the total number of voting interests in the JSC are in attendance.

Resolutions of the GMS are passed by the affirmative votes of no less than 51 per cent of the voting interests in attendance. The affirmative votes of no less than 65 per cent of the voting interests in attendance are required for resolutions approving: (1) amendments to the classes of shares and number of each class of shares; (2) changes to the scope of business or management structure; (3) investment projects or disposals of assets worth 35 per cent or more of the total asset value of the JSC stated in its latest financial statements; (4) restructuring and dissolution of the JSC; and (5) other matters so prescribed in the charter of the JSC.

Where the voting is conducted in the form of opinion polls, resolutions shall be passed upon agreeing votes of shareholders representing no less than 51 per cent of the total number of votes in the JSC.

BOM

The BOM is the managing body of a JSC and has the power to exercise rights and perform the obligations of the JSC on behalf of the JSC, save for those rights and powers reserved for the GMS. The BOM is composed of three to 11 members elected by the GMS by means of cumulative voting.

Meetings of the BOM can be convened periodically or extraordinarily, but no less than once per quarter, by the Chair of the BOM.

The quorum for meetings of the BOM is constituted when no less than three quarters of the BOM members are present.

Resolutions of the BOM are passed by the affirmative votes of a simple majority of members in attendance. The Chair of the BOM shall have the casting vote in the case of even votes.

Control Committee

The Control Committee is the body responsible for, among other things, supervising the BOM and the Director/General Director in their management and administration of the JSC. The Control Committee is composed of three to five members elected by the GMS.

The management structure of the JSC can be organised without a Control Committee, so long as at least 20 per cent of the BOM members are independent members and an internal Auditing Committee is organised subordinate to the BOM.

Director/General Director

The Director/General Director is the person in charge of managing the day-to-day business affairs of the JSC, and is subject to the supervision of and bears responsibility before the BOM for the exercise and the performance of his/her rights and duties. The Director/General Director is elected among the BOM members or hired by the BOM.

1.3.3 PC

The management structure of a PC is outlined below:

Partners' Council

The Partners' Council is the highest decision-making body of the PC and is composed of all general partners of the PC. Any general partner may convene meetings of the Partners' Council to discuss and decide business matters of the PC. The Law on Enterprises, 2014 sets forth no quorum for meetings of the Partners' Council.

Resolutions of the Partners' Council shall be passed by the affirmative votes of no less than two-thirds of the general partners. The affirmative votes of least three-quarters of the general partners is required for resolutions approving: (1) business plan development; (2) amendments or supplements to the charter; (3) acceptance of new partners, or withdrawal or removal of existing partners; (4) investment projects, lending or other forms of capitalisation and borrowing to the value of 50 per cent or more of the PC's charter capital; (5) acquisition and disposal of assets to the value of the PC's charter capital or higher; (6) approval of annual financial statements, total profits, profit distributions and shares of profits to each partner; and (7) dissolution of the PC.

Director/General Director

The Chair of the Partners' Council holds the position of Director/General Director unless otherwise provided for in the charter of the PC.

1.4 Liability of directors, officers and shareholders

Like many other jurisdictions, under Vietnamese law directors and those holding other managerial posts (eg, Chair of the MC, Controllers and BOM members) generally bear a duty of care and fiduciary duty towards and a duty to act in the best interest of the enterprise and the members/shareholders of the enterprise.

Members/shareholders of enterprises have the right to bring civil lawsuits against directors and other managerial personnel to seek indemnification in any case of violation or omission of any delegated rights and obligations.

Chapter 2: Takeovers (friendly M&A)

Samuel Son Tung Vu, Bae, Kim & Lee, Hanoi

2.1 Overview of a tender offer

In Vietnam a friendly takeover can be conducted by the submission of a tender offer, by either entities or individuals, for a part of or all the voting shares of a public company with the intention to obtain the controlling right of such a listed company.

2.2 Transactions of which a tender offer is required

According to the Law on Securities, 2006, as amended in 2010, a tender offer should be submitted by a party in one of the scenarios:

1) it intends to purchase voting shares leading to the ownership of 25 per cent or more of the number of currently circulating shares in any one public company;

2) it and its related persons holding 25 per cent or more of the voting shares in any one public company wish to purchase a further ten per cent or more of the currently circulating voting shares in the public company;

   – this requirement is supplemented by Circular 194/2009/TT-BTC, which requires a tender offer to be submitted in instances where purchase of shares results 'in ownership of 51 per cent, 65 per cent or 75 per cent' of a public company; or

3) it and its related persons holding 25 per cent or more of the voting shares wish to purchase a further interest of between five and ten per cent of the voting shares in the public company within one year from the date of completion of the acquisition of a previous tender offer tranche.

Furthermore, after conducting a public offer, an acquirer holding 80 per cent or more of the number of shares of a public company must continue to purchase the remaining number of shares within 30 days on the same conditions on price and method of payments offered in the public offer.

The Law on Securities was made in 2006, and has been amended and supplemented during the implementation process. Many provisions of the Law on Securities are not amended and supplemented directly into the law, but are amended, supplemented and clarified through the provisions of guiding decrees and circulars. In order to provide a clear and consistent legal ground for the securities sector, on 26 November 2019 the National Assembly of Vietnam adopted the Law on Securities, 2019, which will replace the current Law on Securities and take effect from 1 January 2021. The Law on Securities, 2019 essentially maintains the spirit of the current Law on Securities, brings critical contents currently prescribed in guiding decrees and circulars directly into the provisions of law, and at the same time, clarifies some of the content. In particular, the Law on Securities, 2019 supplements the applicability of the scenario set out in scenario (1) above from just the acquirer to the acquirer and its related persons. For the scenario set out in scenario (2), instead of specifying the number of shares to be offered for purchase being '10% or more of the voting shares in in the public company' and the thresholds of '51%, 65% or 75%', the Law on Securities, 2019 supplements and specifies ownership thresholds that require a tender offer to be 'leading to direct or indirect ownership of or in excess of 35%, 45%, 55%, 65% or 75% of the number of voting shares of the public company'. The Law on Securities, 2019 also removes scenario (3) above and replaces it with the requirement for an acquirer holding 80 per cent or more of the number of shares of a listed company to continue purchasing the remaining number of shares held by the other shareholders.

2.3 Procedure for conducting a tender offer

The process for conducting a tender offer includes the following steps:

- the offeror sends the tender offer dossier to the State Securities Commission (SSC) for approval and, at the same time, sends the tender offer to the target company;
- the target company makes a public announcement on receiving the tender offer dossier within three days from its receipt of the tender documents;
- the board of directors of the target company sends its opinion regarding the tender offer to the SSC and the shareholders of the target company within ten days from receipt of the tender documents;
- the SSC sends its reply to the tender offer dossier to the offeror (either an approval or request for further information) within 15 days from receipt of the tender documents;
- the offeror makes three consecutive public announcements regarding the tender offer on one electronic newspaper or written newspaper and on the relevant stock exchange within seven days from receipt of the SSC's approval;
- the term of a tender offer must be no fewer than 30 days and no longer than 60 days from the date of the tender offer application submitted to the SSC; and
- the offeror reports the results of the tender offer to the SSC within five days of completion, and at the same time, makes a media announcement regarding the results of the tender offer.

The tender offer may only be implemented after the SSC has provided its opinion and after the public announcement about the tender offer. In addition, the acquirer must appoint a securities company to act as an agent for conducting the procedures implementing the tender offer. Furthermore, a foreign investor cannot submit any tender offer that would result in a breach of any foreign ownership limitation applicable to the target company prescribed by Vietnamese law.

2.4 Cases where the tender offer requirement can be waived

Under the Law on Securities, the purchase of shares of a public company newly issued under an issuance plan passed by the public company's GMS will not require a tender offer even if the envisaged share acquisition results in the ownership of 25 per cent or more of the voting shares in the company. A tender offer is also not required in relation to a share transfer of a shareholder in a public company to another organisation or individual, resulting in changing ownership in excess of 25 per cent, where such transfer has been approved by the GMS of the public company.

The new Law on Securities, 2019 maintains the stance that the acquisition of shares with voting rights will not be subject to a tender offer if such a waiver is approved by the GMS.

Chapter 3: Foreign investment

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In general, the Law on Investment No 67/2014/QH13, passed by the National Assembly of Vietnam on 26 November 2014 as amended and supplemented with the latest amendment by Laws No 90/2015/QH13, No 03/2016/QH14, No 04/2017/QH14, No 28/2018/QH14 and No 42/2019/QH14 regulates almost all business investment activities of both foreign and local investors in Vietnam. The Law on Investment sets out prohibited business investments, conditional business investments, and the relevant procedures for making investments and so on. In addition to the Law on Investment, the business investment activities of foreign investors in Vietnam are regulated by: various Vietnamese laws and international treaties to which Vietnam is a signatory. In particular, with the exception of provisions regulating business investment prescribed in the Law on Securities, the Law on Credit Institutions, the Law on Insurance Business and the Law on Petroleum, in the event there is any discrepancy between provisions of the Law on Investment and the provisions of any other Vietnamese laws relating to prohibited business investments, conditional business investments, and procedures for making investments, the provisions of the Law on Investment shall prevail (pursuant to Article 4.2 of Law on Investment). If an international treaty to which Vietnam is a signatory contains provisions that differ from or conflict with the provisions of the Law on Investment or other provisions of Vietnamese law, then the provisions of the relevant international treaty shall prevail (pursuant to Article 4.3 of the Law on Investment and Article 6.1 of the Law on International Treaty).

3.1 Forms of investment

Foreign investors are able to invest in Vietnam through the following forms of investment as prescribed by the Law on Investment: (1) establishment of an economic organisation;

(2) investment in the form of capital contribution, or purchase of shares or portion of capital in an existing Vietnamese economic organisation; (3) investment in the form of business cooperation contract (BCC); or (4) investment in the form of public–private partnership (PPP).

For the establishment of an economic organisation, foreign investors must prepare an investment project and register it in Vietnam to obtain an IRC (Article 22.1 of the Law on Investment). After obtaining the IRC, foreign investors must register the establishment of an economic organisation and receive the ERC for such economic organisation.

In order to make a capital contribution or purchase shares or a portion of capital in an existing Vietnamese economic organisation, foreign investors must obtain a notification on satisfaction of investment conditions from the provincial department of planning and investment (the 'DPI') if either: (1) the contribution or purchase results in 51 per cent or more of charter capital of the Vietnamese economic organisation being held by foreign investors; or (2) the Vietnamese economic organisation operates in a business sector with conditions to foreign investment (Article 26.1 of the Law on Investment). In theory, other than these two scenarios, foreign investors investing in Vietnam in this form are not required to go through the above procedure with the provincial DPI. However, in practice, many provincial DPIs request all foreign investors investing in their provinces in this form to perform such procedures.

In order to make investments into Vietnam through a BCC, foreign investors must obtain an IRC, but the parties to the BCC are not required to establish a new economic organisation to implement the investment project (Article 28.2 of the Law on Investment).

To make an investment in Vietnam in the form of a PPP, foreign investors must sign the PPP contract with the authorised state agency in accordance with the Vietnamese regulations governing PPPs (the primary legislation governing the PPP is Decree No 63/2018/ND-CP ('Decree 63'), dated 4 May 2018 on investment in the form of a PPP). Foreign investors are not required to obtain an IRC when investing in the form of a PPP.

In the cases where foreign investors are required to go through the aforementioned procedure to obtain an IRC (in relation to the establishment of an economic organisation or investment through a BCC), if the sector, scope and impact of foreign investors' investment projects require an in-principle approval from the National Assembly, the Prime Minister or provincial People's Committee, then the in-principle approval for such investment project must be obtained before the issuance of the IRC (Article 37.1 of the Law on Investment).

3.2 Restriction on foreign investment

The Law on Investment specifies six sectors in which foreign investment is prohibited: (1) trading of narcotics; (2) trading of hazardous chemicals and minerals; (3) trading of endangered flora and fauna; (4) business dealing with prostitution; (5) human trafficking, trading of human tissue and body parts; and (6) human cloning (Article 6, Appendices 1 and 2 of the Law on Investment).

Furthermore, the Law on Investment also lists 243 conditional investment sectors applicable to both foreign investors and local investors in Vietnam (Article 7 and Appendix 4 of the Law on Investment), such as financial and professional services; certain types of education; trading and exploration for energy and minerals; operation of ports, railroads and airports; and trading in medical services. In general, if operating in one of the conditional investment sectors, the economic organisation in Vietnam may be required to obtain specific licences (Article 9 of Decree 118/2015/ND-CP). The specific conditions applicable to these conditional investment sectors are detailed in specialised laws regulating the particular sector or in international treaties to which Vietnam is a signatory.

Apart from the conditional business applicable to all investors, foreign investors are also required to satisfy further investment conditions when investing in certain sectors that have conditions regarding foreign investment set out in laws, ordinances, decrees and international treaties on investment (Article 2.6 of Decree 118/2015/ND-CP). Examples of such conditions include: (1) limitation on foreign ownership; (2) form of investment; (3) conditions on the scope of investment activities; (4) conditions on qualification of Vietnamese partners; and (5) other conditions prescribed in laws, ordinances, decrees and international treaties on investment (Article 10.1 of Decree 118/2015/ND-CP).

3.3 Foreign exchange control relating to the foreign investment

The main legislation regulating foreign exchange in Vietnam is the Ordinance on Foreign Exchange Control, 2005 as amended in 2013 (the 'FX Ordinance'). The Vietnamese government and State Bank of Vietnam have issued numerous guiding decrees and circulars to supplement the FX Ordinance.

Vietnamese laws (and, in particular, the FX Ordinance) generally regulate foreign exchange issues relating the foreign investment (eg, capital injection into Vietnam or remittance of profits abroad) via a system of investment capital accounts. Because the FX Ordinance is drafted based on the Law on Investment, 2005, which classifies investment as direct investment and indirect investment, the FX Ordinance and its guiding supplements are not completely compatible with the Law on Investment, 2014, which does not make a distinction between direct and indirect investment. Pursuant to the FX Ordinance and its guiding supplements, foreign exchange issues relating to foreign investment are settled via either: (1) a direct investment capital account (which is mainly regulated by Circular 06/2019/TT-NHNN); or (2) an indirect investment capital account (which is mainly regulated by Circular 05/2014/TT-NHNN). In other words, depending on the investment forms identified under the FX Ordinance and its guiding legal documents, foreign investors are allowed to inject capital into Vietnam or repatriate profits via direct or indirect investment capital accounts.

3.4 Investment incentives available to foreign investors

Under Vietnamese law, investment incentives are given to investment projects of both foreign investors and local investors when such investment projects are performed in certain geographic areas and business sectors (Article 15.2 of the Law on Investment). In addition, investment incentives are given to enterprises or organisations in the high-tech and scientific/technology sector, investment projects where the investment capital is VND 6tn or more (of which at least VND 6tn will be disbursed within a period of three years or less from the date investment approval), and for investment projects located in rural areas and employing 500 employees or more.

According to Article 15.1 of the Law on Investment, investment incentives offered under Vietnamese laws are:

- application of a lower rate of corporate income tax (CIT) for a definite period or for the whole duration of implementation of the investment project, or exemption from or reduction of CIT;
- exemption from import duty in respect of goods imported to form fixed assets, raw materials, supplies and components for implementation of an investment project; and
- exemption from and reduction of land rent, land use fees and land use tax.

The current standard CIT rate is 20 per cent (Article 1.6 of Law No 32/2013/QH13). There are also preferential tax rates set at ten per cent, 15 per cent or 17 per cent and applied for a period of either 15 years or ten years (Article 1.7 of Law No 32/2013/QH13 and Article 1.7 of Law No 71/2014/QH13). It is also possible to receive CIT exemption for a period of either two or four years, and 50 per cent CIT reductions for a period of either four or nine years (Article 1.8 of Law No 32/2013/QH13). For example, except for projects relating to the production of goods subject to special consumption tax and exploitation of mineral resources, manufacturing projects are eligible for a ten per cent tax rate for 15 years, a four-year tax exemption and a nine-year 50 per cent tax reduction, if one of the following conditions are met (Articles 1.7–8 of Law No 32/2013/QH13):

- investment capital of at least VND 6tn to be disbursed within three years from the issuance date of the IRC, and total annual revenue of at least VND 10tn three years after the year the enterprise begins earning revenue; and
- investment capital of at least VND 6tn to be disbursed within three years from the issuance date of the IRC and employing more than 3,000 employees.

No tax incentives are applicable to income arising from the transfer of capital; transfer of real estate; transfer of investment projects; income from business activities outside Vietnam; or income from precious mineral resources, oil and gas exploration and exploitation and so on (Article 1.12 of Law No 32/2013/QH13).

Chapter 4: Restructuring and insolvency

Samuel Son Tung Vu, Bae, Kim & Lee, Hanoi

4.1 Petition for bankruptcy

The primary of legislation governing the insolvency of companies incorporated in Vietnam is the Law on Bankruptcy of Vietnam No 51/2014/QH13, dated 19 June 2014. The Bankruptcy Law applies to enterprises, cooperatives and units of cooperatives. The scope of the Bankruptcy Law does not extend to natural persons.

Pursuant to the Bankruptcy Law, an enterprise is deemed insolvent when it fails to meet its financial obligations and pay its debts within three months following the date that such debts become due. An enterprise is bankrupt only when it is declared so by the People's Court.

Upon the insolvency of the enterprise, the following persons have the right to file a bankruptcy petition to the court:

- unsecured creditors or partially secured creditors;
- labourers or trade union representatives; and
- shareholders of the insolvent enterprise.

On the other hand, the owner of a sole proprietary, the chairman of the board of directors of a JSC, the chairman of the MC of an LLC, a partner of a partnership and the legal representative of the insolvent enterprise are obliged to file a bankruptcy petition upon an enterprise becoming insolvent. Failure to comply with this obligation will bring the above persons subject to liability under the Bankruptcy Law and also give rise to the obligation to pay compensation if there is any damage caused due to such non-compliance.

4.2 Asset protection

With the intention to preserve assets in the event of insolvency, the following transactions conducted by the insolvent enterprises during a six-month period prior to the decision on the commencement of bankruptcy proceedings will be deemed invalid and declared so by the People's Court:

- asset transfer or assignment not at the market price;
- conversion of unsecured debt(s) into debt(s) secured or partly secured by the assets of the enterprise;
- payments or setoffs that benefit a creditor in respect of a debt that has not yet become due or with a sum that is larger than a debt that has become due;
- donation of movable or immovable assets to another person; and
- other transactions for the purpose of dispersing assets of the debtor.

Furthermore, transactions between insolvent entities and their related persons within 18 months before the People's Court issues the Commencement Decision will also be deemed invalid.

4.3 Steps of the bankruptcy procedure

In general, the bankruptcy procedure may last over a year. A summary of the bankruptcy procedure is as follows:

1. The petitioner files the application with the court to commence bankruptcy proceedings.
2. The petitioner and the insolvent enterprise negotiate on withdrawal of the petition.
3. The court accepts the bankruptcy petition after the payment of required court fees by the petitioner and notifies such acceptance to various relevant entities, including the petitioner,

the insolvent enterprise, the relevant procuration authority and other authorities dealing with cases relating to the insolvent enterprise. Upon acceptance of the bankruptcy petition, all ongoing judicial proceedings and enforcement against the insolvent enterprise's assets must be suspended.

4. The court decides on the commencement of bankruptcy proceedings and circulates its decision to the petitioner; the insolvent enterprise; (other) creditors; the relevant procuration authority, judicial enforcement authority, tax authority and local licensing authority; and makes a public announcement on the national enterprise registration information portal, the court's official website and two consecutive volumes of a local newspaper.
5. The judge in charge appoints an asset administrator or an asset management liquidation firm.
6. The insolvent enterprise conducts an inventory and evaluation of its assets.
7. The judge in charge calls for the creditors' meeting, which decides whether to suspend the bankruptcy proceeding, conduct a restoration plan or declare bankruptcy.
8. The insolvent enterprise conducts the restoration plan if it is resolved by the creditors' meeting or the court declares bankruptcy, if the restoration is not resolved or is unsuccessful, such a declaration shall be circulated to relevant entities.
9. The judicial enforcement authority conducts the liquidation procedure under the supervision of the asset administrator or asset management liquidation firm.

Upon the decision on the commencement of bankruptcy proceedings (Step 4) and the appointment of an asset management liquidation firm (Step 5), all operations of the insolvent enterprise are put under supervision of the judge in charge and the asset administrator or the asset management liquidation firm.

Chapter 5: Employment, industrial relations, and work health and safety

Kim Thanh Tran, Bae, Kim & Lee, Ho Chi Minh City

5.1 Employees rights and statutory protection method

The main law regulating the employment relationship is the prevailing Labor Code, 2012, which will be replaced by Labor Code, 2019 from 1 January 2021. The employment relationship is also further governed by the Law on Social Insurance, Law on Labor Hygiene and Security, and other governmental regulations, decrees and circulars.

An employee shall have the following rights, among others:

- to participate in vocational training, and to improve occupational skills and suffer no discrimination; furthermore, employers are prohibited from discriminating on the basis of gender, race, skin colour, social strata, marital status, belief, religion, HIV infection, disabilities and for the reason of establishing or joining trade unions and participating in trade union activities;
- to receive a wage commensurate with his/her occupational knowledge and skills on the basis of an agreement reached with the employer; skilled labourers can receive a salary at least seven per cent higher than the minimum wage;
- to receive protection and be able to work in conditions that ensure labour safety and labour hygiene; employers are required to provide appropriate tools, equipment and a safety plan for employees to prevent labour accidents and occupational diseases;
- to work normal working hours and be paid additional wages for overtime work, where eight hours per day and 48 hours per week is considered normal working hours; for overtime work, employees can receive additional pay, but the maximum overtime hours shall not exceed four hours per day, 30 hours per month (from 1 January 2021, the maximum overtime hour will be increased to 40 hours per month) and 200 hours per year; and a gross maximum annual overtime of 300 hours is permitted in some special scenarios;
- to take at least 12 days of paid annual leave and to enjoy collective welfare benefits;
- to take leave on the ten public holidays, including: (1) Calendar New Year Holiday: one day; (2) Lunar New Year Holidays: five days; (3) Victory Day: one day; (4) International Labour Day: one day; (5) National Day: one day; and (6) Commemorative Celebration of Vietnam's Forefather – Hùng King: one day; under the Labour Code 2019, an additional one day will be added to the National Day holiday; and if employees are required to work on public holidays, they will be paid 300 per cent of their normal salary;
- to form and join and participate in activities of trade unions, occupational associations and other organisations in accordance with Vietnamese law; employers are prohibited from obstructing or causing difficulties to employees in the establishment, joining and operation of trade unions;
- to request and participate in dialogue with employers, implement democratic regulations and be consulted at the workplace to protect his/her rights and legitimate interests;
- unilaterally to terminate the labour contract in accordance with Vietnamese law, although employees are required to provide prior notice to employers; and
- to go on strike in certain circumstances provided by Vietnamese law; an employees' collective is permitted to carry out the strike in order to achieve its demands in the process of a labour dispute settlement.

Recognising that an employer holds a stronger position than its employees, in order to protect the legitimate rights and benefits of employees, Vietnamese law provides certain statutory protection for employees. Firstly, the laws provide the legal basis to protect the job of the employee, according to which any termination by employers must be based on statutory grounds, and are subject to strict formal requirements and procedures. Employers are also required to provide severance payment to employees with more than 12 months' service and who choose to terminate their labour contracts as allowed by law. Secondly, Vietnamese law ensures suitable labour conditions for the employee by providing for minimum wages applicable for various regions, working hours, annual leave and equipment for employees for dangerous and/or hazardous work. Such labour conditions must be explicitly set out in the labour contract, internal regulations, collective labour agreements and other documents required under law. Moreover, Vietnamese law prescribes some specialised regulations applicable to female employees (eg, six-month maternity leave), juvenile labour or elder labour, and disabled labour. Last but not least, Vietnamese law grants labour unions 'the role of representing and protecting the rights and legitimate interests of trade union members and employees' and, in certain disciplinary processes, the participation of the trade union is mandatory to ensure the legitimacy of the disciplinary decision of the employer.

5.2 Statutory contributions and minimum wage

By law, both the employee and employer are required to make payments towards mandatory insurance (including social insurance, healthcare insurance and unemployment insurance) at the following rates:

Contribution subject	**Percentage for mandatory insurance (based on the monthly salary of the employee)**			
	Social insurance	**Healthcare insurance**	**Unemployment insurance**	**Total**
Contribution of the employer (per cent)	17.5	3	1	21.5
Contribution of the employee (per cent)	8	1.5	1	10.5
Total (per cent)	**25.5**	**4.5**	**2**	**32**

Social insurance contributions apply to foreign employees working in Vietnam who satisfy the following requirements: (1) they obtain work permits, practising certificates and practising licences issued in Vietnam; (2) they enter into indefinite-term or definite-term labour contracts valid for at least one year with employers in Vietnam; (3) they have not reached the age of 60 for males and 55 for females; and (4) they are not intra-company transferees, including employees who have been managers, chief executive officers, experts or technicians of a foreign enterprise for at least 12 months, and have been transferred to work in the commercial presence of such an enterprise within the territory of Vietnam.

Minimum wages differ depending on the location of employment. In comparison with 2019, the minimum wage of employees has increased by an average of approximately five per cent due to the proposals and opinions from the General Trade Union and National Salary Council, as follows:

Region	**Minimum wage in 2019 (under Decree 157/2018/ND-CP) (VND)**	**Minimum wage in 2020 (under Decree 90/2019/ND-CP) (VND)**
Region I	4,180,000	4,420,000
Region II	3,710,000	3,920,000
Region III	3,250,000	3,430,000
Region IV	2,920,000	3,070,000

The above regional minimum wages are only applicable for unskilled employees, whereas the minimum wage applied for skilled/educated employees is higher by at least seven per cent.

5.3 Work permits and residence card

At least 15 working days before the day on which a foreign employee begins work, the employer must submit an application for a work permit to the provincial Department of Labour, Invalids and Social Affairs ('DOLISA'). The maximum term of a work permit is currently two years. Upon expiry of the two-year term, it is possible for an employer to renew the work permit for a foreign employee for another two-year term.

For certain foreigners working in Vietnam who would not normally receive exemption from the requirements for a work permit, at least seven working days before beginning work, the employer may request the DOLISA to certify that such foreign employees are eligible for exemption from work permits. A foreign worker who receives a work permit exemption can be: (1) a capital contributing member or owner of an LLC; (2) a member of the BOM of a shareholding company; (3) the head of a representative office or of a project of an international organisation or non-governmental organisation in Vietnam; (4) entering Vietnam for a period of less than three months in order to offer services; (5) a foreign lawyer issued with a certificate to practise law in Vietnam in accordance with the Law on Lawyers; (6) an employee who is internally reassigned in a company that engages in one of the 11 service industries for which Vietnam's World Trade Organization (WTO) commitments on services apply.

A foreign employee who holds a valid work permit or is legally exempt from obtaining a work permit will receive a temporary residence card issued by the police authorities, which is valid throughout the term of his/her work permit or work permit exemption notice. A foreign employee who has received a temporary residence card can enter and exit Vietnam without a visa throughout the term of his/her temporary residence card.

Chapter 6: Tax law

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6.1 Overview of taxation

Knowledge of tax regulations is a must for enterprises doing business in Vietnam. Vietnam only has national taxes centrally managed by the Ministry of Finance (MOF), which is also responsible for releasing implementation guidance for tax laws and regulations. The General Department of Taxes (the 'GDT') and the General Department of Customs administer almost all the taxes that companies need to be aware of when doing business in Vietnam. Tax agencies and customs offices are established at the provincial and district levels.

Enterprises operating in Vietnam are required to pay: (1) VAT; (2) CIT; (3) personal income tax (PIT); (4) foreign contractor; (5) special sale tax import/export tax; and (6) certain other specific taxes.

On 26 November 2019 the National Assembly of Vietnam adopted the Law on Securities, 2019, which will replace the current Law on Securities and take effect from 1 January 2021. The promulgation of the Law on Securities, 2019 focused on reviewing tax risk management, promotion of electronic transactions and administrative procedure, and enhancement of international cooperation on tax management. The Law on Securities, 2019 has the following new provisions:

- tax authorities will be granted more competence to collect tax;
- taxpayers and tax authorities will be required to conduct electronic transactions for tax purposes if they fully satisfy certain requirements;
- providing guidance on electronic invoicing;
- enhancing the cooperation between Vietnamese tax authorities and their overseas counterparts in various areas;
- changing various regulations on tax filing and payment procedures;
- reaffirming general principles of the existing transfer pricing regulations, such as the arm's length principle or the principle that adjustment of prices shall not reduce taxable profits; and
- providing more guidance in relation to tax audit, admin penalties and late payment interest.

6.2 Taxes imposed on enterprises

6.2.1 VAT

VAT is levied on supplies of goods and services made in Vietnam by a taxable person, including the import of goods and services into the country during the course of business. VAT payers include organisations and businesspersons that purchase services from foreign organisations (or individuals) that do not have a permanent establishment in Vietnam and are not registered for VAT in Vietnam.

There are two VAT calculation methods: tax deduction and direct calculation. Under the former, the VAT payable is determined by deducting the input VAT from the output VAT charged. Under the latter, VAT is applied on the added value of the goods or services. Taxpayers must file VAT returns on a monthly basis by the 20th of the following month, or on a quarterly basis by the 30th day of the subsequent quarter.

There are three categories of VAT rates:

- zero per cent, which mainly applies to exported goods and services;
- five per cent, which mainly applies to essential goods; and
- ten per cent, which is the standard VAT rate applicable to most types of goods and services.

There are, however, areas where VAT is exempt, the most important being:

- certain agricultural products and transfer of land use rights;
- financial derivatives and credit services;

- medical services;
- teaching and training;
- transfer of technology and software services; equipment, machinery and spare parts; and specialised means of transport;
- necessary materials used for the prospecting, exploration and development of oil and gas fields that cannot be produced in Vietnam; and
- goods and services imported under official development assistance (ODA) programmes.

6.2.2 Corporate income tax (CIT)

Foreign enterprises doing business under the Law on Investment, 2014, the Law on Petroleum and the Law on Credit Institutions, 2010 are subject to taxation imposed under CIT laws. The standard rate is 20 per cent.

CIT-taxable income is the difference between an enterprise's total revenue, whether domestic or foreign-sourced, and its deductible expenses, plus other assessable income. CIT taxpayers are required to prepare an annual CIT return, which must include a section setting out the adjustments between accounting profits and taxable income. CIT taxpayers may carry forward their tax losses for five years. The carrying-back of losses is not permitted. There is no provision for any form of consolidated filing or group loss relief.

Expenses are tax deductible if they relate to the generation of income and are properly supported by suitable documentation, such as a contract, invoice or bank transfer voucher.

The following is a non-exhaustive list of non-deductible expenses under current laws:

- depreciation of fixed assets that are not in accordance with the prevailing regulations;
- employee remuneration expenses that are not stated in a labour contract or collective labour agreement; and
- provisions for stock devaluation, bad debts, financial investment losses, product warranties or construction work that are not in accordance with prevailing regulations.

There are three preferential tax rates available: (1) ten per cent, either for 15 years or the lifetime of the project; (2) 17 per cent for the lifetime of the project; and (3) 17 per cent for ten years. Preferential tax rates start from the commencement of operating activities. When the preferential rate expires, the CIT rate reverts to the standard rate of 20 per cent.

6.2.3 Foreign contractor tax (FCT) – withholding tax

FCT applies to certain payments to foreign parties, such as interest, royalties, service fees, leases, insurance, transport, transfers of securities and goods supplied within Vietnam or associated with services rendered in Vietnam. FCT comprises a CIT and VAT element at varying rates and can also include PIT for payments to foreign individuals.

There are three methods for tax payment: direct method, deduction method and hybrid method. Under the direct method, the foreign contractor does not have to register for VAT purposes, nor file CIT and VAT returns. Instead, CIT and VAT will be withheld by the Vietnamese customer at prescribed rates from the payments made to the foreign contractor, whereas the deduction method requires the foreign contractor to register for VAT and file CIT and VAT returns in the same way as a local entity. The foreign contractor needs to issue VAT invoices and charge VAT similar to a local company. CIT is paid at 20 per cent on net profits.

Foreign contractors can apply the deduction method if they meet the following requirements:

- they have a permanent establishment or are tax resident in Vietnam;
- the duration of the project in Vietnam is more than 182 days; and
- they adopt the full Vietnam Accounting System, complete a tax registration and are granted a tax code. The Vietnamese customer is required to notify the tax office that the foreign contractor will pay tax under the deduction method within 20 working days of the date of signing the contract.

If the foreign contractor carries out several projects in Vietnam and qualifies for the application of the deduction method for one project, the contractor is then required by law to apply the deduction method to all its other projects as well.

Under the hybrid method, the foreign contractor registers for VAT and accordingly pays VAT based on the deduction method (ie, output VAT less input VAT), but with CIT being paid under the direct method rates on gross turnover. Foreign contractors wishing to adopt the hybrid method must:

- have a permanent establishment in Vietnam;
- operate in Vietnam under a contract with a term of more than 182 days; and
- maintain accounting records in accordance with the accounting regulations and guidance set out by the MOF.

6.2.4 Double taxation avoidance agreements (DTTA)

Vietnam has entered into Double Taxation Avoidance Agreements with over 75 countries and regions in the world, which helps to reduce an enterprise's tax liability in Vietnam. For example, capital gains are normally subject to 25 per cent CIT, but for residents of some contracting countries, capital gains are only taxed in the resident's home country and exempt from CIT in Vietnam. Accordingly, if these capital gains are not taxed in the home country, the taxpayer will be exempt from any CIT against capital gains in Vietnam.

6.2.5 Special Excise Duty (Special Sales Tax or SST)

SST applies to the production or import of certain goods, the domestic sales by the importers of these goods and the provision of certain services. The Law on SST classifies SST objects into the following two groups:

- commodities, which include cigarettes, liquor, beer, automobiles that have less than 24 seats, motorcycles, aeroplanes, boats, petrol, air-conditioners up to 90,000 British thermal units, playing cards and votive papers; and
- services, which include discotheques, massage, karaoke bars, casinos, gambling, lotteries, golf clubs and entertainment with betting.

SST rates depend on the object and currently range between five and 150 per cent. Taxpayers must file SST returns on a monthly basis by the 20th of the following month.

6.2.6 Import and export duties

Import duty at various rates is imposed on goods imported into Vietnam. Import duty exemptions are provided for projects classified as encouraged sectors and goods imported in certain circumstances.

There are three import duty rates in Vietnam:

- ordinary rates;
- preferential rates; and
- special preferential rates, which apply to imported goods from countries that have free trade agreements (FTA) with Vietnam. Vietnam has signed many FTAs with nations and areas, such as the Association of Southeast Asian Nations (ASEAN), Australia and New Zealand, Japan, South Korea and the EU-Vietnam FTA.

Vietnam also has an anti-dumping tax, anti-subsidy tax and self-defence tax.

Export duties are levied on a few items comprising natural resources, such as sand, chalk, marble, granite, ore, crude oil, forest products and scrap metal.

The General Department of Customs and its agencies are central to imported/exported goods and services issues in Vietnam, particularly in determining the value of goods and services for tax calculations.

6.2.7 Personal Income Tax (PIT)

A personal income taxpayer is any resident individual with taxable income arising either within or outside the territory of Vietnam, or any non-resident individual with taxable income arising within the territory of Vietnam.

Residents are those residing in Vietnam for 183 days or more in a calendar year, or for 12 consecutive months from the first date of arrival; or those having a permanent residence in Vietnam.

Tax residents are subject to Vietnamese PIT on their worldwide taxable income, wherever it is paid or received. Employment income is taxed on a graduated tax rates basis, while non-employment income is taxed at a variety of different rates.

Individuals who do not meet the definition of a tax resident are considered to be taxed non- residents. Taxed non-residents are subject to PIT at a flat tax rate of 20 per cent on the income received as a result of working in Vietnam in the given tax year. Non-employment income is taxed at various other rates subject to any applicable DTAA.

For residents with regular income, depending on their monthly income, the rate shall be five per cent to 35 per cent. For residents with irregular income, the capital gains tax (CGT) as PIT is due and payable when the transaction is completed, with the following range: 0.1 per cent for a security transfer; five per cent for interest/dividends, income from copyright and franchising/royalties; ten per cent for income from winning prizes and inheritance/gifts; and 20 per cent for capital transfer.

In addition, there is a list of taxable income and non-taxable income. This list is complex and changes depending on the policy of the government. Therefore, advice from a qualified tax consultant should be sought.

6.3 Tax compliance, audits and penalties

To reform the tax administration, as well as to modernise tax administration systems and procedures, taxpayers are now required to self-assess their taxes, and there is a shift towards declaring and paying taxes online.

There are detailed regulations setting out penalties for various tax offences. For discrepancies identified by the tax authorities upon audit/inspection, a 20 per cent penalty is imposed on the amount of tax that is under-declared. Late payment of tax is subject to interest of 0.03 per cent of the tax liability for each day that the tax is late instead of 0.05 per cent previously.

Chapter 7: Intellectual property

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7.1 Patents

Vietnam distinguishes between invention patents and utility solution patents.

An invention patent is a technical solution in the form of a product or process intended to solve a problem by the application of natural laws. An invention shall be eligible for protection in the form of the grant of an invention patent when it satisfies the following conditions: it is novel, it is of an inventive nature and it is susceptible to industrial application. Rules for utility solution patents are similar to those for invention patents, but the item is not required to demonstrate an inventive nature.

The following objects are ineligible for protection as inventions: (1) scientific discoveries or theories and mathematical methods; (2) schemes, plans, rules and methods for performing mental acts, training domestic animals, playing games and doing business; (3) computer programs; (4) presentations of information and solutions of aesthetic characteristics; (5) plant varieties and animal breeds; (6) processes of plant or animal production that are principally of a biological nature, other than microbiological processes; and (7) human and animal disease prevention methods, diagnostic and treatment methods.

Invention patents are protected for a maximum of 20 years, while utility solution patents are valid for ten years.

7.2 Trademarks

A trademark is any sign in the form of letters, words, drawings or images, including holograms, or a combination thereof, represented in one or more colours, used to distinguish goods or services of different organisations or individuals. Vietnam laws provide another nearly similar definition of 'trade name', which can be interpreted as the designation of an organisation or individual used in business activities in order to distinguish the business entity bearing such a trade name from other business entities in the same business sector and area.

However, the following signs are ineligible for protection as marks: indistinctive (eg, simple shapes and geometric figures, numerals, letters or scripts of uncommon languages or signs indicating time, place and method of production, category, quantity, quality, properties, ingredients, use, value or other characteristics descriptive of goods or services); identical with or confusingly similar to national flags or national emblems; causing misunderstanding or confusion or deceiving consumers as to the origin, properties, use, quality, value or other characteristics of goods or services.

Trademarks are generally protected by registration. Unregistered trademarks may still be protected in Vietnam if such trademarks are deemed to be 'well-known' based on the number of customers, territories for sales, sales turnover and so on.

A trademark is valid for ten years; after which it may be renewed indefinitely for additional ten-year periods.

7.3 Copyright

Copyright means rights of an organisation or individual to works (any creation in the literary, artistic or scientific sector) that such an organisation or individual created or owns, whereas copyright-related rights mean rights of an organisation or individual to performances, audio and visual fixation, and broadcasts and satellite signals carrying coded programs.

Copyright in works shall comprise moral rights (eg, to give titles to their works, to publish their works, to authorise other persons to publish their works or to forbid other persons from modifying, editing or distorting their works in whatever form) and economic rights (eg, to display their works to the public, to reproduce their works, or to communicate their works to the public by wireless or landline means, and electronic information networks or other technical means).

Copyright shall arise at the moment a work is created and fixed in a certain material form, irrespective of its content, quality, form, mode and language, and irrespective of whether or not such work has been published or registered. Furthermore, the copyright-related rights shall arise at the moment a performance, audio and visual fixation, broadcast or satellite signal carrying coded programs is fixed or displayed without causing loss or damage to copyright.

To be protected as copyrights in Vietnam, works that are created in another country and exist in a definite form, or that are first published or disseminated in another country, must be published in Vietnam within 30 days from the first publication. Provided, however, that if such a foreign country is a member of the international treaties to which Vietnam is also a signatory (eg, the Bern Convention for the Protection of Literary and Artistic Works or any other bilateral convention regarding national treatment), Vietnam extends its national treatment in copyright protection to such a member country.

7.4 Design

Design (literally referred to as 'industrial design' under Vietnamese law) is defined as the outward appearance of a product embodied in three-dimensional configurations, lines, colours or a combination of such elements. Similar to a patent, a design shall be protected if it satisfies the following conditions: (1) it is novel; (2) it is of an inventive nature; and (3) it is susceptible to industrial application. There are three types of designs deemed as ineligible for protection: (1) outward appearance of a product that is necessary due to the technical features of the product; (2) outward appearance of civil or industrial construction works; or (3) shape of a product that is invisible during the use of the product.

An industrial design patent shall be valid from the grant date until the end of five years after the filing date and may be renewed for two consecutive terms, each of five years.

7.5 Other remarks

To enjoy most types of intellectual property rights in Vietnam, the intellectual property should be registered. The application for registration may be lodged in Vietnam or overseas if so allowed under the law of Vietnam and the treaty regarding intellectual property to which Vietnam is a party. Vietnam laws apply the 'first to file' principle, under which if two or more applications for registration are filed by different parties, a protection title may only be granted to the valid application with the earliest priority or filing date among applications that satisfy all conditions for the grant of a protection title.

Any organisation or individual who commits an act of infringement of the intellectual property right of another organisation or individual may be dealt with by the application of civil, administrative or criminal remedies.

Preliminary injunctions and compensation for damages are available through the civil courts. Administrative remedies can include caution or monetary fines and additional penalties (eg, confiscation of intellectual property counterfeit goods, raw materials, and materials and facilities used mainly for the production or trading of such intellectual property counterfeit goods; or the suspension of business activities for a fixed period in the sector in which the infringement was committed). In certain cases, criminal proceedings may be launched against persons who violate trademarks, geographical indications, copyrights and other related rights.

Chapter 8: Financing

Samuel Son Tung Vu, Bae, Kim & Lee, Hanoi

8.1 Types of banks

A foreign bank is permitted to provide banking operations and other related business operations in Vietnam through one or more of the following forms after it has obtained an establishment and operation licence (the 'Licence') issued from the State Bank of Vietnam (the 'SBV'):

1. a wholly foreign-owned bank;
2. a joint venture bank (between a foreign bank and a Vietnamese bank); and/or
3. a branch of a foreign bank in Vietnam.

Under Vietnamese law, banks operating in form (1) and/or (2) are independent legal entities, while entities operating in form (3) do not have legal entity status. In addition, a foreign bank may also set up a representative office in Vietnam for the purpose of acting as a liaison office (without providing any banking services in Vietnam). A representative office is also not an independent legal entity and may not conduct revenue-generating activities.

The scope of operation of a wholly foreign bank, joint venture bank and branch of a foreign bank will be specified in the Licence issued by the SBV, which may include some or all of the below activities as stipulated under Article 98 of Laws on Credit Institutions, 2010 (as amended in 2017):

- taking demand deposits, time deposits, saving deposits or other deposit types;
- issuing deposit certificates, promissory notes, treasury bills and bonds to raise capital within and outside Vietnamese territory;
- extending credits in forms as approved by the SBV;
- opening current accounts for clients;
- providing payment instruments; and
- providing payment services as approved by the SBV.

8.2 Licensing requirement for banks

The specific licensing conditions may vary depending on whether the bank is a wholly foreign-owned bank, joint venture bank or branch of a foreign bank. Generally, an application for a Licence may be granted upon satisfaction of the following conditions:

- having funded capital at least equal to the minimum legal capital as required by laws; for instance, VND 3,000bn for wholly foreign-owned and joint venture banks, and $15m for a branch of a foreign bank;

- the foreign bank/foreign credit institution (CI) must be a legal entity currently operating lawfully and must have sufficient financial capacity to participate in capital contribution. In the case of a branch of a foreign bank, the total asset value of the foreign parent bank must be at least $20bn in the preceding year. In the case of a wholly foreign-owned bank or joint venture bank, the requirement on total asset value is at least $10bn in the preceding year;
- managers, executives and members of the board of controllers must satisfy all the criteria and conditions in accordance with Vietnamese law;
- having a charter with provisions in accordance with Vietnamese law;
- having a proposal for establishment and a feasible business plan that do not adversely affect the safety and stability of the Vietnamese CIs system and do not create a monopoly or restrict competition, or create unfair competition within the Vietnamese CI system;
- the foreign bank/foreign CI is permitted to conduct banking operations in accordance with the law of the country where its head office is located;
- the proposed operations for which the Licence is applied to conduct in Vietnam must be the operations that the foreign bank/foreign CI is permitted to conduct in the country where its head office is located;
- the foreign bank/foreign CI must have a healthy operation and satisfy all conditions on total assets, financial status and prudential ratios in accordance with the SBV's regulations;
- the competent authority of the foreign country has agreed in writing with the SBV on the inspection and supervision of the banking operation, and on the exchange of information about the supervision of banking safety, and has given a written commitment on the unified supervision of the operation of the foreign bank/foreign CI in accordance with international practice; and
- the foreign bank must give a written commitment that it accepts liability for all obligations and commitment of its branch in Vietnam; ensures that the actual value of the funded capital of its branch will be maintained at no less than the minimum capital as required by law; and that it will comply with Vietnamese banking regulations on safety requirements. On the other hand, the foreign CI must give a written supporting commitment on the finance, technology, administration and operation of the joint venture bank or the wholly foreign-owned bank, and ensure that those entities shall maintain funded capital at least equal to the minimum legal capital and comply with provisions on the prudential ratios as required by laws.

The procedure for issuing a Licence for a wholly foreign-owned bank, joint venture bank or branch of a foreign bank in Vietnam is as follows:

- The applicant submits to the SBV the applications dossier as required by Vietnamese laws. Within 60 days from the receipt of the complete application documents, the SBV will issue a letter of acknowledgment of such receipt.

- Within 90 days from the letter of acknowledgment, the SBV will issue an in-principle approval for the establishment of the applicant. In the case that the SBV refuses to issue an in-principle approval, the SBV will explain the reasons for such a refusal in writing.
- Within 60 days from the receipt of the in-principle approval from the SBV, the applicant will submit to the SBV additional documents as required by Vietnamese laws. Failure to supplement the additional documents as required by Vietnamese laws within the aforesaid period shall result in the in-principle approval no longer being in effect.
- Within two days from the receipt of the complete additional documents, the SBV will issue a letter of acknowledgment of such receipt.
- Within 30 days from the receipt of the complete additional documents, the SBV will issue the Licence. In the case that the SBV refuses to issue the Licence, the SBV will explain the reasons for the refusal in writing.

With respect to the issuance of a Licence for representative offices, within 60 days from the receipt of a complete application dossier, the SBV must either issue the Licence or explain the grounds for its refusal of such an application.

Chapter 9: Privacy laws and data protection

Anh Dung Tran, Bae, Kim & Lee, Hanoi

Despite rights to privacy and confidentiality of information being stated as one of the fundamental rights under the 2013 Constitution, there is no single unified legislative document regulating this matter in Vietnam.

9.1 Regulations on privacy and data protection

Although the National Assembly has repeatedly proposed to issue a single law on privacy and data protection, in practice there has been no movement to introduce such a law. For the time being, several regulations on privacy and data protection are found across various legislative documents, such as the Civil Code, 2015, Law on Telecommunication, 2009, Law on Post, 2010, Consumers' Rights Protection Law, 2010, Cyber-Information Safety Law, 2015, Cybersecurity Law, 2018, Criminal Code, 2015, Law on Children, 2016, Law on Medicine, 2016, Law on Statistics, 2015, Law on Press, 2016 and Law on Citizen Identification, 2014. However, these regulations merely provide general regulations, and most of them are overlapping in content. Due to the current situation, the application of privacy and data protection regulations is rather difficult in Vietnam.

Because privacy and data protection are regulated in different pieces of legislation and without cross reference, it is difficult to achieve a consistent understanding of privacy and data protection. Nevertheless, privacy and data protection are recognised principles in Vietnam. In practice, unless otherwise permitted by Vietnamese law, no collection, processing or usage of personal data can be conducted without consent being sought from the data subjects by target entities. Data subjects also have the right to request that any target entities furnish them with their personal data so that the data subjects are able to check, correct, remove and prevent the disclosure or transmission of their personal data to other parties.

9.2 Remedies against violations related to privacy and data protection

Infringements of privacy and data protection will result in the imposition of administrative sanctions or even criminal penalties depending on the severity of the violations. An individual may also pursue civil procedures to protect his/her privacy and personal information, such as requesting the relevant authority or the court recognise his/her right or terminate the infringement, or requesting compensation for any damages or loss.

The three different remedies mentioned above are provided for under law, but in practice, such remedies are ineffective. This is due to a lack of detailed implementing regulations. Moreover, the sanctions and penalties are not strong enough to prevent the violation of the relevant regulations. Ultimately, the unclear and troublesome nature of such remedies discourage entities from pursuing them.

Chapter 10: Competition law

Anh Tuan Nguyen, LNT & Partners, Ho Chi Minh City

The recently passed Competition Law, 2018 No 23/2018/QH14 introduces significant changes to the competition landscape in Vietnam, most notably the shift to an effects-based regulatory approach that focuses on the significant competition-restraining impact of a conduct rather than the form in which it is carried out. The Law also applies to offshore transactions that have an impact on domestic market competition. Decree 35/2020/ND-CP, which guides a number of provisions of the Competition Law, and provides for, among other matters, detailed merger filing thresholds and pertinent factors for substantive assessment, took effect on 15 May 2020.

This chapter outlines three key areas regulated by the Competition Law: (1) abuse of monopolisation and dominance; (2) cartels; and (3) merger control.

10.1 Abuse of monopolisation and dominance

Under the Competition Law, an undertaking is deemed to be in a dominant market position if it possesses: (1) a market share of at least 30 per cent in the relevant market, or (2) significant market power. Significant market power is determined based on, inter alia, financial capacity, market barriers and market share ratio, among undertakings in the relevant market. A group of two, three, four or five undertakings is deemed to have a collective dominant market position if the group has a combined market share of at least 50 per cent, 65 per cent, 75 per cent or 85 per cent in the relevant market, respectively.

An undertaking is monopolistic if it has no competitors in the same relevant market.

An undertaking or (where applicable), a group of undertakings, having monopolistic or dominant market power, is not in and of itself unlawful. Legal concerns are only raised if such an undertaking or group of undertakings abuses the monopolisation or dominance that it enjoys. As such, the Competition Law prohibits the following abusive conduct:

Prohibited conduct	Dominance	Monopolisation
Predatory pricing	✓	
Resale price maintenance (RPM) practice	✓	✓
Restraining production or distribution of goods or services, limiting the market, or impeding technical or technological development	✓	✓
Applying different commercial conditions to the same transaction	✓	✓
Imposing unrelated conditions	✓	✓
Hindering the participation in, or expansion of, the market by other undertakings	✓	✓
Imposing disadvantageous conditions on customers		✓
Unilaterally changing or terminating signed contracts without justification		✓
Conducting acts prohibited by other laws		✓

Of note, not all of the aforementioned conduct is prohibited per se. Except for those for which the prohibition is exclusive to monopolistic undertakings, abusive conduct is only illegal if it is actually or potentially harms competitors or causes loss to customers.

10.2 Cartels/restrictive agreements

Article 3.3 of the Competition Law defines a 'restrictive agreement' as an agreement in any form that has an actual or potential competition-restraining effect.

Under the Competition Law, cartels are no longer prohibited solely on the basis of the undertakings' combined market share as outlined under the former regime. The law instead adopts a new approach, according to which a given cartel is assessed on the basis of its restrictive impact on the domestic market. Accordingly, certain types of restrictive agreements, such as price fixing or market allocation between undertakings having a combined market share lower than 30 per cent in the relevant market than were permitted under the former competition law, are now prohibited.

Furthermore, certain cartels are now criminally prosecutable. Prohibited and criminalised cartels include the following:

Cartels	Illegal per se[1]		Conditionally prohibited[2]		Criminally prosecutable	
	Horizontal	Vertical	Horizontal	Vertical	Horizontal[3]	Vertical
Bid rigging[4]	✓	✓			✓	✓
Removal of non-members from the market	✓	✓			✓	✓
Restriction of non-members' market access or business development	✓	✓			✓	✓
Price-fixing	✓			✓	✓	
Allocation of market and/or customer	✓			✓	✓	
Quota fixing	✓			✓	✓	
R&D restriction			✓	✓	✓	
Agreements on the refusal to deal			✓	✓		
Agreements to limit the upstream/downstream market			✓	✓		
Agreements to impose businesses conditions not directly related to the subject matter of the contract			✓	✓	✓	
Other restrictive agreements			✓	✓		

The Competition Law provides for a leniency programme, under which co-conspirators participating in a cartel may turn themselves in and assist with the competition authority's investigation in exchange for either full immunity from, or a reduction of, fines for breach of competition law that the authority would have otherwise imposed on them. This is the first time a leniency programme has been formally introduced in Vietnam. Nevertheless, it is designed to create a so-called 'race to court' effect with conditions and levels of immunity similar to those of the conventional leniency programme recommended by the Organisation for Economic Co-operation and Development (OECD).

10.3 Merger control

Under the Competition Law, a contemplated economic concentration that crosses any of the filing thresholds must be notified to the competition authority prior to its completion. An economic concentration encompasses a merger, consolidation, acquisition, joint venture or other type of concentration provided by law.

1 Illegal cartels are considered hard-core cartels, in that their mere existence is in and of itself detrimental to market competition, and thus strictly prohibited.

2 Conditionall prohibited cartels are only prohibited if they actually or potentially restrict competition significantly.

3 Except for bid rigging and agreements on the removal of non-members from the market or restriction of non-members' market access or business development, horizontal cartels are only considered criminally prosecutable if the co-conspirators' combined market share is at least 30 per cent.

4 For bid rigging, only individuals are criminally prosecuted.

The Competition Law no longer relies on market share as the sole jurisdictional threshold, but adds a new set of criteria to its filing test, namely total assets, total turnover and transaction value. This means there will be no merger prohibited per se as under the former competition law regime. Two sets of thresholds are set out in Decree No 35/2020/ND-CP, one applicable to transactions in virtually all sectors, the other reserved for transactions involving CIs, insurers and/or securities companies.

10.3.1 General thresholds

A contemplated concentration, except for one involving any of the above listed undertakings, must be notified to the competition authority if any of the following thresholds is met:

Criteria	Threshold
Total sales or purchase turnover or total assets on the Vietnamese market of either undertaking to the transaction or group of affiliated undertakings	VND 3tn
Transaction value of the merger[5]	VND 1tn
Combined market share of the parties to the transaction in the fiscal year prior to the year of merger filing	20 per cent

10.3.2 Specific thresholds

A contemplated transaction involving CIs, insurers and/or securities companies must submit a notification if it crosses any of the following thresholds:

<table>
<tr><th>Threshold</th><th>CIs</th><th>Insurers</th><th>Securities companies</th></tr>
<tr><td>Total assets of either transaction undertaking or the respective group of related undertakings</td><td>20 per cent of total assets of all CIs on the Vietnamese market</td><td colspan="2">VND 15tn</td></tr>
<tr><td>Total sales/purchase turnover of either transaction undertaking or the respective group of related undertakings</td><td>20 per cent of total revenue of all CIs on the Vietnamese market</td><td>VND 10tn</td><td>VND 3tn</td></tr>
<tr><td>Transaction value</td><td>20 per cent of total charter capital of all CIs on the Vietnamese market</td><td colspan="2">VND 3tn</td></tr>
<tr><td>Combined market share</td><td colspan="3">20 per cent</td></tr>
</table>

Of note, the total assets/turnover and combined market share values refer to those as of the fiscal year prior to the year of the anticipated transaction. The transaction value thresholds in both cases do not apply to offshore deals.

The substantive assessment of a notified transaction comprises two phases. At the preliminary appraisal stage, the authority will assess the parties' combined market share and/or post-merger Herfindahl–Hirschman Index (HHI) to decide whether the contemplated transaction falls within any of the safe harbours and should consequently be cleared. It is noteworthy that if the authority does not issue a decision within the statutory timeframe, the transaction will be automatically cleared.

If the transaction fails the preliminary appraisal, the review moves to the second phase, where the authority employs a substantial lessening of the competition test to decide whether to issue an approval and on what conditions (if any). Accordingly, a concentration, even a foreign-to-foreign one, which causes or is capable of causing significant anti-competitive impact on the Vietnamese market, is prohibited.

5 This threshold does not apply to offshore transactions.

Chapter 11: Dispute resolution

Net Le, LNT & Partners, Hanoi

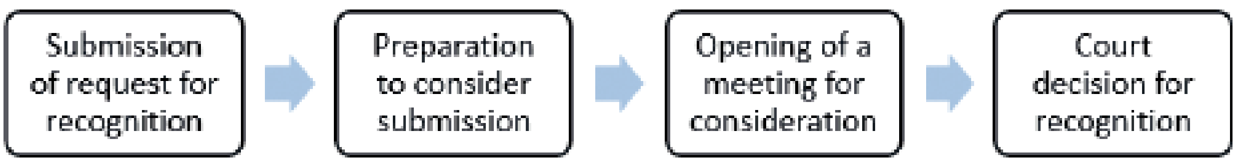
There are three potential means of dispute resolution under the Vietnamese legal system: mediation, arbitration and litigation.

11.1 Mediation

Due to certain drawbacks in the Vietnamese court system, it is essential that the parties to any dispute attempt to reach an amicable settlement outside of the court system. Vietnamese law acknowledges this by requiring the parties to certain disputes (including civil, labour and family disputes) at least to attempt mediation before commencing litigation. Decree No 22/2017/NDCP on commercial mediation was established on 24 February 2017, making commercial mediation an independent and effective form of dispute resolution, as well as making the result of mediation legally binding on the involved parties.

If the parties reach a settlement during mediation, that arrangement is enforceable as a normal contractual agreement. One or both parties to the mediation settlement agreement can apply to the court for the recognition of their settlement agreement. After being recognised, the mediated settlement agreement is enforceable as a full and final court judgment in compliance with the law of Vietnam on civil enforcement, which means it shall take effect immediately upon issue and can neither be appealed nor protested against through appellate procedures.

The process for recognising the successful result of mediation is as follows:



11.2 Arbitration

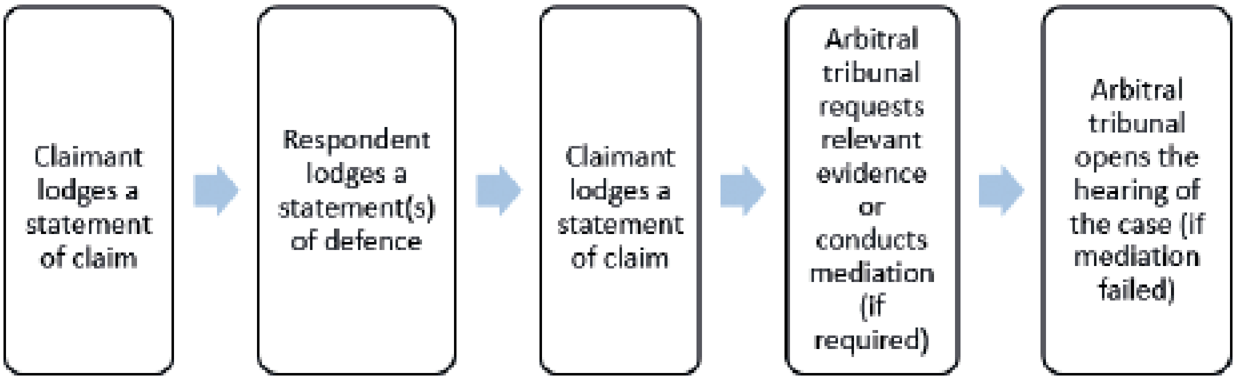
11.2.1 Legal framework of arbitration

The Law on Commercial Arbitration No 54/2010/QH12 (the 'LCA') is the main legal instrument governing Vietnamese law on arbitration. According to the LCA, arbitration in Vietnam covers:

- disputes arising from commercial activities;
- disputes between the disputants, with at least one carrying out commercial activities;
- disputes between goods or services provider and consumer by consent of the consumer; and
- other disputes to be settled by arbitration as provided by law.

Disputes between the involved parties can be settled by an arbitral tribunal organised by an arbitration centre, such as the Financial and Commercial Centre for Arbitration (the 'FCCA') or the Vietnam International Arbitration Centre (VIAC), in accordance with its procedural rules ('Institutional Arbitration'), or through ad hoc arbitration set up by the parties involved in accordance with the procedures as agreed by the parties ('Ad hoc Arbitration'). Unless otherwise agreed, if the parties cannot agree on the number of arbitrators, the tribunal will be composed of three arbitrators.

Commercial disputes shall be settled by arbitration through the following basic procedural steps:



Decisions from Vietnam's arbitration centres are final and binding on the parties, and may be enforced by the Enforcement Department in the same manner as an enforceable court decision.

11.2.2 Foreign arbitration

Under the Civil Procedure Code (CPC), foreign arbitral awards are arbitral awards rendered outside Vietnam or those rendered by non-Vietnamese arbitrators within Vietnam. As the law currently stands, Vietnamese courts will only consider an application for recognition and enforcement of a foreign arbitral award if the award has been made in or by arbitrators of a member state of the New York Convention or to the extent that the country in question grants reciprocal treatment to Vietnam. Vietnam ratified the New York Convention in 1995. There have been many instances where Vietnamese courts have enforced foreign arbitral awards.

An award recognised by a Vietnamese court will have the same legal effect as a judgment given by a Vietnamese court and can be enforced in Vietnam.

On the other hand, a Vietnamese court may reject an application for recognition and enforcement of a foreign arbitral award if the respondent can provide evidence. Interestingly, the procedures prescribed by law in relation to the recognition and enforcement of foreign arbitral awards appear to grant only the respondent (the party who is subject to enforcement of the arbitral award) the right to participate in the court hearing. The applicant (the party seeking recognition and enforcement of the arbitral award) does not appear to enjoy a similar right.

Although the law states that the courts should ratify awards that meet the aforementioned requirements without assessing their merits, the Vietnamese courts have historically gone beyond this legal rule. However, since Vietnam's accession to the WTO in 2007, the Vietnamese government has made considerable efforts to strengthen the enforcement regime by introducing new legislation and detailed guideline regulations. The current Law on Enforcement of Civil Judgment, which was amended and supplemented in 2014, has helped to improve the recognition and enforcement of foreign arbitral awards in Vietnam.

11.3 Litigation

11.3.1 Foreign court

Vietnamese law generally allows foreign investors to refer their disputes to courts in a foreign jurisdiction if parties have a choice of law clause, unless statutorily exempt under the Civil code 2015. These include:

- cases where the consequences of referring such a foreign court are inconsistent with the fundamental principles of Vietnamese law;
- the disputes over immovable property located in Vietnam, particularly disputes over the ownership rights, other rights with respect to such immovable property, and lease or use of such immovable property as security property; and
- the applicable law in a labour contract or a consumer contract adversely affects the minimum interests of employees or consumers as prescribed by Vietnamese law.

There are two points that investors should take note of when choosing to litigate in foreign courts under the Vietnamese system. Firstly, Vietnamese courts might not uphold choice of law contract provisions. Therefore, an investor should either include a clause referring disputes to arbitration or be prepared to enforce their rights in Vietnamese courts under Vietnamese law. Secondly, a judgment issued by a foreign court is only enforceable in Vietnam if Vietnam has signed a bilateral treaty with the country in question. The CPC does offer some hope in this regard, as it provides that Vietnamese courts will recognise and enforce foreign court judgments on a reciprocal basis.

11.3.2 Domestic court

Under the Law on Organisation of the People's Courts and the CPC, there are four main People's Courts in Vietnam, excluding military tribunals, other tribunals provided by law and special tribunals set up by the National Assembly under special circumstances, namely the Supreme People's Court, Superior People's Court, Provincial People's Court and District People's Court. Excluding the District People's Court, these courts have separate specialised courts, namely the criminal court, civil court, economic court, labour court and administrative court.

The court process in Vietnam can be lengthy. Parties begin proceedings at the first instance, where parties are required to disclose evidence and attend mediation meetings. If the parties still maintain their claims afterwards, then a council of adjudicators consisting of one judge and two jurors (usually) will commence the hearing. Afterwards, the council will render a judgment. If a party disagrees with such holding, an appeal must be heard in the court that held the trial at first instance within 15 days.

Parties may also petition for a second review on grounds of legal error or newly discovered evidence, subject to a decision by the Chief Judge or the Chief Procurator of a competent court or procuracy. The grant of a review can also be accompanied by an order for stay of enforcement. The review will take place in closed courtrooms and can be lengthy.

Vietnam is a civil law jurisdiction, so judges in Vietnam base their decisions mostly upon the applicable law and principles of interpretation. However, under the new CPC, from 6 April 2016 the Council of Supreme Court has officially issued nine precedents for lower-level courts to consider and apply. As of the end of 2017, there have been 16 precedents enacted by the Council of the Supreme Court.

In an attempt to streamline what was a very complex system of enforcement, the Law on Judgment Enforcement, 2008, amended and supplanted in 2014, was introduced to replace the Ordinance on Judgment Enforcement, 2004. The new system provides for two steps:

- Firstly, the court will serve judgment to litigants and the judgment enforcement authority (JEA), and the successful claimant may request the enforcement of the judgment. The person who is responsible for satisfying the judgment has the right to lodge an application to the JEA for enforcement within the time limit of five years from the effective date of the judgment.
- Secondly, the JEA will issue a decision to enforce the judgment and serve it on the obligatory party within three days from issue. Subsequently, the obligatory party will have 15 days voluntarily satisfy the judgment. If the obligatory party fails to do so, the JEA will enforce the judgment in accordance with the law.

Foreign investors should be aware of the statute of limitations and the time-consuming nature of court proceedings. In general, the new CPC does not provide a statute of limitations for initiating court proceedings as stipulated in the Civil Proceedings Code 2004. The statute of limitations is subject to specific laws. Although Vietnamese law sets strict time limits for courts to dispose of cases (eg, two to four months for first instance proceedings), each party involved in a dispute must bear in mind that court procedures are time-consuming and sometimes unpredictable. In practice, some disputes have been heard and reviewed in various court proceedings over a period of several years.

Chapter 12: Infrastructure

Thai Binh Tran, LNT & Partners, Ho Chi Minh City

Net Le, LNT & Partners, Hanoi

12.1 Overview of infrastructure in Vietnam

As the backbone of urbanisation and key to smooth economic operation, infrastructure is one of the most important sectors in Vietnam. A blooming infrastructure sector needs legislative coherence and consistency, yet in Vietnam the sector is subject to a plethora of regulations, from construction and planning to land and environment.

In an attempt to tackle this issue, the National Assembly passed a new Planning Law on 24 November 2017 and a Law amending 37 laws related to planning on 20 November 2018, both of which came into force on 1 January 2019. These legislative measures are long-awaited and designed to enhance consistency in the infrastructure regulatory regime. One point to note in particular is that the new Planning Law has abolished the planning permission requirement, thereby removing the gray area in the application for a construction permit under the previous legislation.

One of the recent areas of great interest in Vietnam is PPPs. The first legislative measure concerning PPPs surfaced in 1992, when for the first time the amended Foreign Investment Law defined build–operate–transfer contracts (BOTs). In recent years, given the intense demand for new and improved infrastructure fuelled by rapid industrialisation and urbanisation, the development strategy of Vietnam is to prioritise investment in the form of PPPs. As a result of these developments, the government is now in the process of developing an improved legal framework for PPP projects, the most recent being Decree 63.

12.2 Construction projects characteristics

12.2.1 General construction projects

Foreign investors wishing to conduct construction business in Vietnam are allowed to do so by setting up a foreign-invested company incorporated under Vietnamese laws. Alternatively, they can directly partake in a construction project as a foreign bidder then either enter into a joint-venture agreement with a Vietnamese party or use local contractors to carry out the project. If there is no local contractor capable of performing the entire construction process as required, the project may be conducted solely by foreign contractors, provided that they satisfy all local requirements.

Subject to capacity, experience and education, individuals and organisations, including foreign-invested companies, in the construction sector must obtain a capacity licence in order to do business in Vietnam. The construction works performed by the individual or organisation shall be based on the licence granted. As of 15 September 2018, a foreign bidder may lose its construction licence if it fails to resolve an infringement of administrative regulations after a second notice from the authority, or if it has incurred a penalty in relation to construction works covered by the second operation licence.

The procedure of a construction project is the same as that of a real estate project. The investors must prepare and obtain approvals for the pre-feasibility study report, feasibility study report and construction economic-technical report for the construction project prior to the process in relation to the land use right and construction.

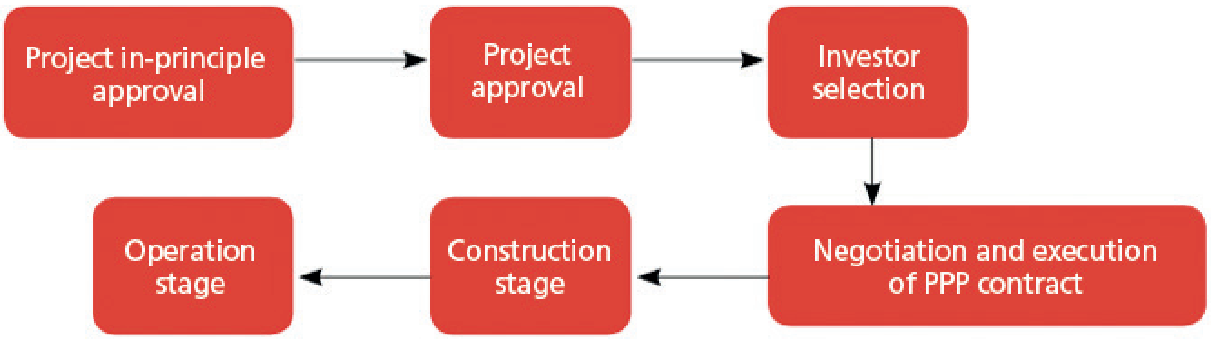
12.2.2 Public–private partnership (PPP) projects

A PPP refers to a contractual cooperation between the state (public sector) and investors (private sector) (the ‘PPP Contract’) jointly to build, innovate, operate and manage infrastructure and public services projects.

A PPP Contract can be a BOT, build–transfer–operate contract (BTO), build–transfer contract (BT), build–own–operate contract (BOO), build–lease–transfer contract (BLT) and operate–manage contract (O&M), or a combination of any of the above.

Depending on the scale, a project may be classified into grade A, B or C, and a certain ministry or provincial level People's Committee shall be authorised to execute the project contracts within the scope of its functions, duties and powers and to perform the rights and obligations and comply with the commitments under the project contract. For example, a development project with investment capital of more than VND 2,300bn (equivalent to $100m) is regarded as a Grade A project subject to the approval of the Prime Minister.

The procedures required for a PPP are outlined in the below flow chart:



Project in-principle approval

The authority shall consider and approve the PPP project in principle based on the project's preliminary proposal, which is known as the 'pre-feasibility study report', and is prepared by either the public investment authority or the investor to present results of the preliminary research into and assessment of the necessity, feasibility and efficiency of the project. After granting an approval at this stage, the authority shall publicise general information on the PPP project in question for bidding purposes.

Project approval

The authority shall consider and officially approve the PPP project based on a 'feasibility study report' prepared by either the public investment authority or the investor. If the investor is to prepare the feasibility study report, it shall sign an agreement with the authority, which usually requires it to waive any claim for the costs of preparing the feasibility study report should the report be subsequently rejected by the authority. However, investors who prepare a feasibility study report often enjoy advantages at a later stage when the authority conducts the public tender to select the investor of the PPP project.

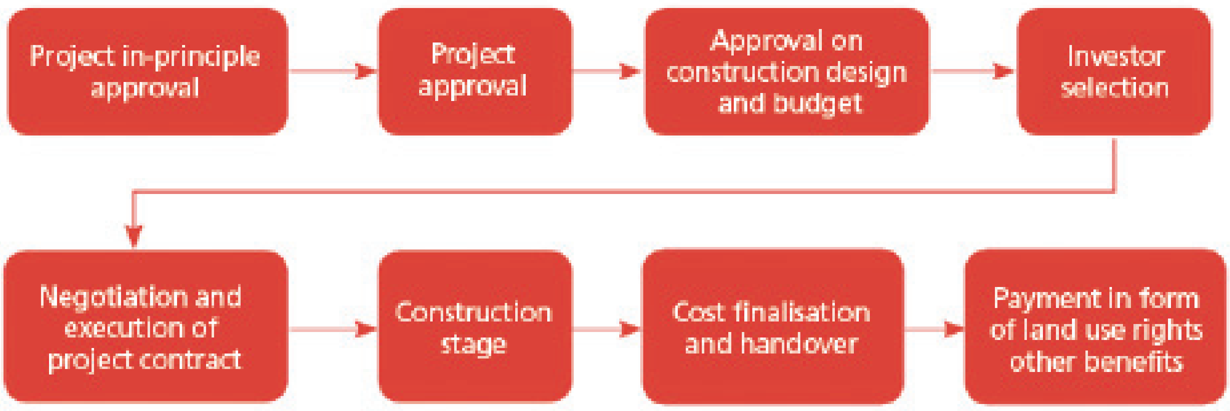
Selection of investor

The authority shall select the investor for the PPP project either by: (1) holding a public tender; or (2) directly appointing an investor. Option (2) shall only apply in cases where (i) there is only one registered bidder; or (ii) only one investor is able to perform the project due to matters concerning intellectual property, commercial secrets, technologies or capital arrangements; or (iii) the investor proposing the PPP project is able to implement it at the highest efficiency under the Prime Minister's approval.

Negotiation and execution of PPP contract

The investors and the authority will negotiate and execute the PPP contract, which will last for two rounds: (1) preliminary negotiation; and (2) official negotiation and execution of PPP contract.

For BT projects in which the authority grants land to the investor, the procedures are as follows:



12.3 Requirements for a construction project

In general, a PPP project must fall within one of the statutory sectors. It should be economically and financially feasible to the investor and affordable to the state in respect of finance, the environment and other matters required by laws.

12.3.1 Investment capital

The investor shall be responsible for contributing the equity and mobilising other capital (ie, obtaining loan from banks/other third partners) to implement the PPP project. For example, for projects with investment capital of up to VND 1,500bn (US$64m), the investor's contributed capital shall account for at least 20 per cent of the project's total investment capital.

12.3.2 Assignment of project

Decree 63 sets out more stringent requirements for private investors that wish to assign rights and obligations under the project contracts to lender(s) or other investors. In particular, the investor is now restricted from assigning part or all rights and obligations in a PPP contract prior to completion of construction works or commencement of the project's operation. To receive the assignment, the proposed assignee must satisfy the financial and managerial capability and other requirements to implement the PPP project.

12.3.3 Lender's step-in right

The lender may assume or designate another qualified investor to assume any or all the rights, interests and obligations of the investor under the PPP contract if the investor fails to perform its obligation under the PPP contract or the loan agreement. In doing so, the lender must request a tripartite agreement between the investor, lender and authority concerning the lender's step-in right.

12.3.4 Construction permit

As a fundamental part of any real estate development project or any other infrastructure investment project, a construction permit must be obtained before the commencement of construction and must suit the project's timeline and plan. As mentioned above, obtaining a construction permit is one of the last steps in registering a real estate project. It is granted subject to the land use right recognised by a legitimate certificate and the suitability of the construction project to the local plan at province and district levels.

Depending on the type and characteristics of the project, the construction permit may or may not have to be obtained from the Ministry of Construction or the People's Committee at the respective level (in practice, from the respective Department of Constructions, who is authorised by the People's Committee) prior to the construction process. Normally, infrastructure projects that have been approved by the President of the People's Committee at the provincial level or higher competent authorities shall not require a construction permit. Specifically, any seven-story residential housing project that has a 1/500 master plan approval and an area of less than 500m^2 shall be exempt from the construction permit requirement.

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