Summer 2020

IFLR

World on pause

Coronavirus ground the world to an almost complete halt.
Corporate finance dealmakers explain how they're keeping things moving

Social bonds & use of proceeds

What does a board of directors do?

LMG Analytics DCM report

Special focus: Africa market makers

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"It's much easier for independent directors to be critical of management when nobody from management is present"

David Berstein considers what a board of directors actually does on page 12

EDITORIAL

The new iflr.com

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In the last issue of IFLR, we talked about the threat coronavirus posed to Chinese economic growth at a pivotal moment following the implementation of its much-anticipated new foreign investment law. Before magazines had even made it to readers' desks, it was clear that the virus would have severe ramifications far beyond China.

With approximately half of the world under some form of lockdown for the past few months, typically hectic streets have been deserted and City watering holes boarded up. Yet corporate and finance lawyers have been busy tweaking and drafting contract after contract, holding the hands of management teams and boards as they make impossibly difficult decisions, and even executing transactions, from rescue financings to, remarkably, the odd IPO.

There's certainly something strange about the thought that for months now, practically the entire business world has been run from home offices, living room sofas and kitchen tables across the globe. We've got to know each other's pets and feature walls on endless Zoom calls, and many have managed difficult home lives – caring for others and home schooling – at the same time. It's all been very impressive.

This issue's cover story on page 8, which is a collection of stories previously published online, looks closely at some of the work that's been going on behind the scenes. You can read the full, original versions on iflr.com, where we publish new content every day.

On that note, we're excited to announce the launch of our new-look website. Our content and focus remain the same: we'll continue to bring you deal analysis, expert opinion and best practice across capital markets, corporate finance and lending, but with more in-house voices and opinions than ever before.

Head to iflr.com now to check it out – and do get in touch to let us know what you think, at elizabeth.meager@euromoneyplc.com.

Enjoy the issue,

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ONLY ONLINE

GLOBAL

Liquidity slowdown prompts derivatives rethink

A significant spike in futures trading followed by a contraction across the board has forced derivatives traders to reassess priorities – and leave documentation alone for now, which could be problematic when it comes to the transition away from Libor

AMERICAS

Broker-dealers like Reg Best Interest

Fidelity and Allianz told IFLR that they hope US states will wait and see how Regulation Best Interest goes before introducing their own separate fiduciary rules, which would overlap with the Securities and Exchange Commission's US-wide framework

ASIA

Asian issuers look to adopt EU taxonomy

Debt issuers in Asia are increasingly looking to the EU's sustainability taxonomy as a model, with many hoping that it will become a blueprint for the region. However, national divergences are likely as the market matures

EUROPE

Covid-19 highlights Schuldschein issues

The instrument has become more popular in recent years, but as the pandemic grinds the market to an almost complete halt, companies in need of urgent financing are looking elsewhere, with some switching to bridging loans and traditional bonds instead

GLOBAL

Corona effect weighs on private equity

Even the notoriously booming private equity market is suffering as a result of the pandemic, with hundreds of deals on hold and terms changing quickly. Issues surrounding valuation, relationship management and documentation are all weighing heavily on fund managers' minds

WEBINAR

The post-pandemic business world: get ready

IFLR's latest webinar, in collaboration with Baker McKenzie and Cyril Amarchand Mangaldas, considered Covid-19's impact on Indian companies, expected trends, and the outlook for 2020. Speakers also provide tips for dispute resolution and methods for effective prioritisation. Listen to the recording for free now by going to iflr.com

QUOTES OF THE MONTH

"The mere fact that an individual holds XRP does not create any relationship, rights or privilege with respect to Ripple"

Crypto Dad Chris Giancarlo and his colleague Conrad Bahlke consider the applicability of US securities laws to XRP, exclusively on iflr.com

"After decades of working in China intensively on financial accounting, there's not a single state-owned enterprise I came across that abided by international standards"

Berkeley Research Group partner and IFLR contributing editor Harry Broadman has some hard truths

"I've advised on more MAC [material adverse change] and *force majeure* clauses over the past eight weeks than in my entire career"

Akin Gump partner Gavin Weir sums up the feeling of many transactional lawyers

"No one is talking about long-term fixes at the moment - we're in pure firefighting mode"

BNP Paribas' Adrian Docherty assesses the mood of regulators and markets alike

"A lot of Chinese companies know that the outlook for them is pretty gloomy"

UBS' Samson Lo gets real on the outlook for the world's second-largest economy

ASIA PACIFIC

A virtual paradise?

Covid-19 has created unprecedented mayhem, with travel restrictions and lockdowns in place across the globe. But it has also forced the business world to rethink the travelling that would have otherwise continued. While there has long been an expectation in the business world of face-to-face meetings, they may not be so necessary anymore.

In China, platforms such as Zoom, WeChat Work and DingTalk have been gaining popularity as people working from home turn to virtual networking and communication tools. Webinars, podcasts and video streaming have, for the time being at least, replaced conferences. Stock markets and even some courts around Asia have also gone virtual.

In March, InnoCare Pharma completed the first ever virtual IPO in Hong Kong SAR, raising $289 million. Its retail tranche was 300 times oversubscribed, with many investors turning their attention to pharmaceutical stocks amid the pandemic. Investor presentations were fully digital.

In fact, Asian capital markets have embraced digital to such an extent that the Shanghai Stock Exchange took first place in the global IPO league table in the first quarter of 2020, with 33 companies raising a total of $7.31 billion.

For professionals who are frequent flyers but do so at the expense of losing valuable time with family, and of course considering the environment, the move to virtual provides a way of doing lots of things much more efficiently than before Covid-19. It's also an excellent way to keep costs down. But it may not be for everyone. For instance, many senior executives at smaller, lesser known companies taking the IPO route would likely want to meet face-to-face with potential investors for roadshows to build trust.

With physical courts also closed for months on end, virtual courts were launched in various cities across China, including Hangzhou, Beijing and Guangzhou. Beijing courts required parties to make use of online case handling systems, and some cases were heard by judges online. In India, the High Courts of Bombay and Karnataka, as well as the Supreme Court, used video conferencing.

Virtual hearings can ensure that the most urgent cases are handled amid Covid-19 and in the long run, can help increase efficiency of courts. However, they are not perfect. For instance, they can be impractical when judges need to cross-examine witnesses: it's much easier to extract the truth from someone when they are physically in court than when the person responds with well-prepared answers behind a computer. Access to justice may also be an issue if hearings are off limits to the public.

The path to digitisation has also sped up significantly for banks. Some brick-and-mortar bank branches in Hong Kong SAR, for instance, had to close between February and April. Banks have been shifting to online meetings and phone calls with clients rather than meeting them face to face. For virtual banks, digital onboarding has become even more popular as customers are prompted to embrace digital solutions and have no choice but to cut down on the physical paperwork many traditional banks still rely on.

While the pandemic is far from over, it's already clear that things will not be going back to exactly how they were before. A fundamental mindset shift has taken place throughout much of the professional services sector.

AMERICAS

The rich get richer, the poor get poorer

It's been one hell of a year. Take a day off and who knows what you might miss. The Covid-19 crisis and the civil rights movement that followed have been incredibly eye-opening. For much of March and April, our time at IFLR was taken up writing about suspensions, delays, setbacks, concerns: article after article about planned regulatory changes that have been pushed back as a result of the health crisis. It's entirely possible the industry was looking for excuses. Things have levelled out as market participants have worked out how to cope with crying toddlers and lacklustre internet speeds; our coverage is slowly returning to normal.

There have been some positives. Despite being struck by a wholly unexpected blow, the financial sector has remained resilient and handled the pandemic surprisingly well. While M&A may be on hold, inboxes are filled daily of news of record numbers in the capital markets, and the banking sector appears to have learned from its 2008 mistakes. Dodd-Frank is working.

So why, with the end in sight, are banks gearing up to undo all their hard work, by not being more prudent? The largest banks in the US, the systemically important financial institutions (SIFIs), are under immense pressure as the economy strains. Things may well get worse over the next few months. Covid-19 numbers aren't going down and public spending is a long way off where it was in 2019. There are still more than 13 million unemployed in the US alone. Travel is a distant memory. So why are the US SIFIs still paying dividends to shareholders and to executives, and why are they even contemplating the resumption of share buybacks? Things might appear broadly stable at the banks, but that could change very quickly. If any bank later needs a bailout and the only way to finance that is from the public coffers in some form of Robin-Hood-in-reverse rescue, it would not go down well. A whole is only as great as the sum of its parts. Banks need customers.

Banking regulators should be taking steps to encourage banks to hold on to capital, to keep a strong and stable buffer that can be deployed to absorb losses if things get worse. Consumers and corporates are going to continue to need bank lending; if it dries up much more there could be dire consequences.

Regulators such as the OCC, the FDIC, and most importantly the Fed, should in the short term at least prevent buybacks and shareholder dividends, executive bonuses, and any other payout designed to lower capital buffers. Current measures seem to be more aligned to encouraging this behaviour.

These regulators should be more cautious this time around. Things might be better than they were during 2008, but not by much – and even still, it's hardly a high bar. Taxpayers should not bail out bank shareholders. They've got enough problems as it is.

EUROPE, MIDDLE EAST AND AFRICA

Springing into action

Within just a few weeks of reports that the virus had spread to the continent, almost the whole of Europe was swept into lockdown. Borders were closed, trips cancelled and thousands of people began to work from home full-time, while others were laid off or placed on furlough: a blow to the real economy barely anyone had anticipated.

Many in finance predicted a market correction was likely by 2021, but nobody quite expected what could be the worst recession for centuries. It's clear that many of the businesses that closed their doors in March will never reopen – a number of UK retailers have already folded – but European policymakers have been working hard to ensure that as few as possible exit entirely.

Early on in the lockdown, the UK government announced the Coronavirus Business Interruption Loan Scheme (CBILS). CBILS has offered financial support to smaller businesses (SMEs) across the UK that are losing revenue as a result of the pandemic, along with various other schemes. These fast-track schemes resemble moves made in other European countries such as Germany, Denmark, Italy, Spain and France – which have all made varying commitments to support local businesses and employees. As President Emmanuel Macron said during his lockdown announcement, "no business, whatever its size, will face the risk of bankruptcy".

The UK government published new statistics at the end of May showing that British businesses have to date benefitted from over £27 billion in loans and guarantees to support cashflow during the crisis. Boris Johnson's government has also introduced a new insolvency and governance bill, enabling organisations undergoing a restructuring and rescue process to continue trading, as well as the temporary suspension of wrongful trading until the end of June. So far companies seem to like it. However, for many, the 2020 landscape remains grim. We have yet to see the full extent of the damage done by the pandemic – and many have raised entirely legitimate concerns about the impact on Brexit negotiations. Concerns are that the UK is back in no-deal territory. Meanwhile, foreign direct investment (FDI) will become more challenging in many jurisdictions, making it harder for companies to scale internationally. The European Commission has already advised member states on how to protect what are now cheap assets from foreign takeovers – something echoed by both the EU's trade and competition commissioners.

Many European leaders have been faced with their very first real-life stress test – and not all of them have passed.

OFF THE

RECORD

"Most MEPs' idea of securitisation is Margot Robbie in a bathtub"

A European ABS market participant doesn't have much faith in politicians' understanding of complex financial instruments

"I can't wait to go back to the office. We're in the kind of business where you need those personal connections - and I'm so tired of back-to-back Zoom meetings"

A New York-based private equity manager has had it with lockdown

"Not all investment banks are the same; not all advisors are the same. My strong belief is that dishonest people do not last long in the industry, because it's fundamentally based on relationships. The good drives out the bad"

A London-based investment banker defends his industry against accusations of short-termism

"It was for a very limited purpose: to create breathing room so the country would not be confronted with a significant increase in interest while it negotiates with the official sector this summer"

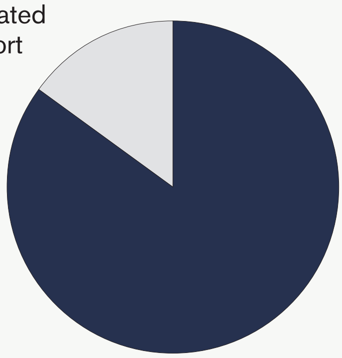
A person close to the deal explains the rationale behind Ecuador's $19 billion consent solicitation in May

The antisocial social bond club

For the summer edition of IFLR magazine we asked readers whether social bonds allocated for Covid-19 should be used to finance the redevelopment of basic infrastructure, essential services, socioeconomic advancement, etc., in developing countries, or if this a misuse of proceeds

By John Crabb

Should Covid-19 allocated social bonds be used to finance the redevelopment of basic infrastructure, essential services, socioeconomic advancement, etc., or is this a misuse of proceeds?



A good rule of thumb when it comes to new asset classes is that typically, when Bank of America gets involved in something, it's time to start paying attention. So when in May, the firm became the first US bank to issue a $1 billion corporate social bond entirely dedicated to fighting the impact of the Covid-19 pandemic, it was big news for this nascent ESG [environmental, social & governance] product.

According to the International Capital Market Association (ICMA), social bond issuance for 2020 totaled $11.6 billion as of May 15, which is significantly higher than the $6.2 billion issued over the same period of 2019. The total for 2019 was just $16.7 billion. Bank of America says that proceeds from the offering are to be allocated to healthcare industry lending in the firm's global commercial bank; specifically not-for-profit hospitals, skilled nursing facilities, and manufacturers of healthcare equipment and supplies.

"The world is in a fight against Covid-19 and we are committed to doing our part by supporting the companies and professionals on the front lines," says Bank of America vice chairman Anne Finucane. "The proceeds from this offering will help deliver critical resources for the companies involved in the testing, diagnosis, treatment and prevention of this insidious virus, while providing investors an opportunity to join us in this all-important effort."

However, Bank of America's deal aside, some are concerned that with the large number of social bonds issued over the past few months by companies across the globe, the potential for greenwashing and fund misuse is high.

METHODOLOGY

IFLR publishes its quarterly poll question on iflr.com and Linkedin group page iflr.com/LinkedIn. Throughout the quarter, IFLR's editorial team gathers the responses and interviews selected respondents.

With that in mind, for this Covid-19 themed issue of IFLR, we polled readers on how far social bonds directly targeted at supporting those most in need as a result of the pandemic could go, and whether proceeds could or should be used for other projects.

Overwhelmingly, respondents (85%) suggested that proceeds from Covid-19 allocated social bonds can be used for redevelopment not specifically related to fighting the virus. The consensus suggests that the most important caveat is that the use of proceeds, if not directly financing the development of vaccines or similar, complies with ICMA's social bonds principles.

"It all comes down to what the issuer says in its documentation," says Nicholas Pfaff, head of sustainable finance at ICMA. "It is good practice in a social or green bond for an issuer to indicate a range of potential project categories – because a few years down the line it may be a very different world." According to Pfaff, if the new use of proceeds is a clearly recognised social project category then there should be no problem – but there is of course the risk that, in extreme cases, the money is used elsewhere altogether.

Denise Odaro, head of investor relations at the International Finance Corporation (IFC), goes as far as to say that it is not plausible to even think of the question as 'what to do with excess funds'. When a company issues a social bond and the proceeds are expected to go towards Covid-19 related projects, and there's a surplus,

Everyday life may never be the same again

that surplus has to go to other social projects by definition.

"It is not a credible social bond unless the use of proceeds is exclusively for social projects which should or could include Covid-19 related products. Thus, if 70% of the funding an entity has raised goes to Covid-19 projects, the 30% balance has to go to other social projects," she says. "The projects are what should lead to the financing. If you are an issuer and you identify $10 million worth of projects and then issue a bond, you do not issue that bond ahead of any strategy or plan at all."

"The main benefit of the label is the transparency disclosure, but some issuers feel there's no time for all that so they just jump straight in"

Rules or guidelines?

Another important aspect of this concept is which principles the issuer abides to. IFLR has covered in great detail the taxonomy of ESG, which varies region by region. It is important to remember that social bond principles are simply guidelines. Because of this, many issuers opt against using concise social bond principles. "Some decide not to go down the official social bond route, but instead publish a framework that adheres to the best practice of social bonds, without the label," says Herve Duteil, chief sustainability officer at BNP Paribas Americas. "Then you have those typically FSA-approved, typically multilateral development banks that issue in a different format, with different strings attached."

In general, organisations like the World Bank already have very clear social mandates so do not need to follow this route. "It's already in their organisational mandate to have an impact on society for this type of work. So even though the perfectly fleshed social bond format is not there, they are able to issue social bonds because they were quickly responding to an emergency situation," adds Duteil.

Urgency is one reason why some pandemic response bonds are not being appropriately labelled as social or even Covid-19 bonds. This is potentially damaging to the bond itself, and will almost certainly lead to confusion. "The main benefit of the label is the transparency disclosure, but some issuers feel there is no time for all that so they just jump straight in," says Justine Leigh-Bell, director of market development at the Climate Bonds Initiative.

For example, some of the Covid-19 related issuances being issued by Chinese companies are directed towards healthcare or rescuing jobs, or ensuring that the country can sustain its economy going forward. "But we have seen some bonds that are tied to renewable energy assets as China develops new infrastructure as a response to the crisis," she adds. "Who knows to what extent a lot of their pandemic-related debt is going to be pushed in that direction? We're still trying to get our heads around what's being financed," she added.

World on pause

Coronavirus ground the world to an almost complete halt. Dealmakers explain how corporate finance is adapting

By John Crabb, Jimmie Franklin Karry Lai and Lizzie Meager

With flights grounded, offices shuttered and more than half of the world's population under some form of government-enforced quarantine, the unenlightened might imagine that financial services dealmaking has also ceased. While it's true that volumes in many areas – M&A, for instance – have taken a freefall over the past quarter, businesses are still in need of cash. Many of them more so than ever before. And unlike in previous crises (except perhaps the last), when the vast majority of companies could turn to their bank for a quick line of credit, companies across the world are increasingly tapping the public capital markets instead.

As this issue's cover story – which is a roundup of content previously published on the new-look iflr.com – finds, some financing tools have boomed. While the vast majority of IPOs are on hold, PIPEs [private investments in public equities] have enabled private equity firms sitting on reams of dry powder to, quite literally, share the wealth with struggling listed companies. While M&A plummeted to its lowest level since 2009, on-the-fly share placements have given many businesses access to the lifeline they need to make it to the other side. Meanwhile, governments across the world have essentially suspended capitalism, injecting billions into local economies and companies via emergency loans, employee furlough schemes and, in some cases, full-scale bailouts.

As for the long-term effects of this incredibly strange period, unfortunately only time will tell. Global economics aside, the irony of entire countries locking down right at the start of AGM season – at a time when management teams need the support and guidance of their shareholders more than ever – is not lost.

So, while in many respects, the world has been on hold, there's been plenty to keep the IFLR team busy. Here are a few highlights.

Chevron was one of many companies to suspend share buybacks to protect dividends as a result of the pandemic

Buybacks get a bad rap

In the early days of the pandemic there was a major drop in the number of US corporates taking part in share buyback programmes. This prompted a discussion on whether the practice should be more heavily regulated.

As the crisis led to tens of millions of layoffs, cancelled dividends and trillions of stimulus dollars, the financial sector was once again under public scrutiny – with share buyback programmes at the centre.

In early April, Chevron, the largest oil producer in the US, told IFLR that it was adjusting to significant shifts in supply and demand. "We have announced changes to reduce our capital spending by about 20%, or $4 billion," said Sean Comey, Chevron's senior advisor of external affairs.

"Our financial priorities are unchanged. The dividend is our number one priority," he added. Chevron has not cut its dividend since 1934 – in the depths of the Great Depression – so has a long track record of being a safe bet. "We came into this environment with the strongest balance sheet and lowest breakeven in the industry, and we're taking strong actions to preserve cash today, not just with the capital spending reductions, but with the termination of our share repurchase programme and the continuation of efforts...to further reduce costs, and improve margins and efficiency in our underlying business," continued Comey.

According to Standard & Poor's, the outlook for buybacks in 2020 is unsurprisingly grim: "Dividends are under pressure, and buybacks appear to be gasping for air," said Howard Silverblatt, senior index analyst for S&P Dow Jones Indices. Pre-Covid-19 estimates predicted 2020 buybacks would come close to or exceed the $806 billion record set in 2018. American Airlines alone has spent about $12.4 billion on stock repurchases since 2014, making up a significant portion of its free cash flows.

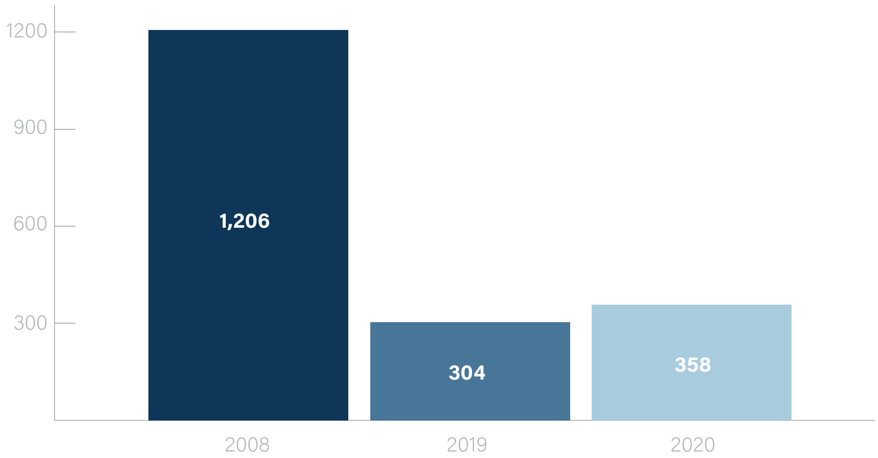
One source, the director of equity derivatives at a major US bank, told IFLR that these major programmes are a product of low rates that eventually led to an abusive situation. "When there is little clarity in the regulatory environment, many companies have simply continued to conduct stock buybacks," he said. "There is a certain degree of abuse going on, but the question is how you go about regulating that. Capital structure should be at the purview of management."

> *"Dividends are under pressure, and buybacks appear to be gasping for air"*

When businesses conduct buybacks, the liquidity that could help them cope when sales and profits decline in an economic downturn is no longer available. If companies never required bailouts, there would be no problem. Running a business so that shareholders get wiped out if there is a crisis is a concern – but a risk a company can choose to take. Yet despite the negative press surrounding the practice, and the restrictions on many of those undertaking programmes, S&P predicts the numbers will bounce back eventually.

This is a highly political issue with complex market dynamics. Under a Democratic

PIPE transactions by US companies (Source: Mayer Brown)



administration, whether that be the president in the White House or both houses of Congress, there would likely be calls for change.

"Even if the government didn't do something, a lot of companies are more concerned with liquidity and cash at this point," said Silverblatt. "It will be interesting to see when Apple reports. Filings usually have a breakdown to see how many and what kinds of comments a company receives. Coronavirus is going to be mentioned in every press release."

M&A documentation's pandemic makeover

Just one of the many ways Covid-19 has overturned the dealmaking landscape – aside from temporarily grinding it to an almost complete halt – is its influence on due diligence.

"For deals that are still progressing, buyers and sellers are now factoring Covid-19 into the legal process as well as the valuation," Herbert Smith Freehills partner Gavin Davies told IFLR in mid-May. New due diligence questions – surrounding business continuity, employee protections, data protection and the use of government programmes – have slowed down the few deals that are still progressing. Parties must also factor in the risk of legislation changing – which has been seen across the world – and its potential impact on the company. This is a marked difference from the pre-coronavirus world.

Lawyers say that while some deals have continued – the most conservative estimates put it at less than ten percent – healthy company M&A has almost entirely ceased. This has prompted nervous dealmakers to revisit and rephrase boilerplate terms, with *force majeure* and material adverse change (MAC) clauses becoming particularly popular. SpringOwl Asset Management CEO Jason Ader said that while these are technically nothing new, specific pandemic-related language is appearing in documentation.

Another item in the long list of deal roadblocks is valuation. Many believe that sellers will need to adjust their expectations on price – and that it will take time for prices to stabilise – so unblocking the current pipeline may not be as efficient as some hope.

Add to that any number of delays in regulatory approvals and third-party consents, and the outlook for deals closed in 2020 starts to look a little grim. If parties can't agree on a new price, there are of course other tools available, such as earnouts. A power shift in favour of the buyer can be pretty safely expected.

"This is not a good time for shareholder activism"

PIPEs have their day

By the end of April 2020, 358 US-based companies had raised $20.7 billion via PIPEs [private investment in public equities], up from $10.8 billion in the same period last year. Lawyers expect this number to climb further throughout the year. "As March progressed, companies started saying 'ok – what do I do? How do I raise capital?'," said Angus Whelchel, global head of private capital markets at Barclays.

A PIPE is usually comprised of ordinary shares, preferred shares, convertible debt, warrants, or a mixture of these, generally offered at a discount to the prevailing share price of the company. Absolving the company of the requirement for shareholder approval or a prospectus, they can be completed in days.

During periods of heightened volatility, PIPEs tend to be highly structured and backed by private equity and venture capital funds, along with other financial sponsors. The stake can be significant and may, in some circumstances, constitute a change in control. "Counsel should consider whether the transaction would indeed result in a change of control and, if so, whether it would trigger any change of control provisions in credit facilities, outstanding debt securities, or other material agreements," said Mayer Brown partner Anna Pinedo.

The number and type of investors bidding for structured PIPEs during the Covid-19 era has changed since the 2008 financial crisis. Today, private equity funds are larger and new fund formation over the past several years in hybrid, structured equity and special opportunities strategies has led to a highly competitive market. Peter Sorrentino, head of private placements advisory at Evercore, has been involved in many recent high-profile PIPE transactions, including US Foods, Outfront Media, Expedia and SunOptima. "We've certainly seen a spike recently," he told IFLR in May. "The difference is that in 2008, roughly two-thirds of issuance was by financial services companies," he said. That's obviously different this time around, with travel, real estate and outdoor companies some of the most heavily affected. "Issuers will continue to turn to the private markets when unable to access public market syndications of common stock or convertible debt offerings," added Sorrentino.

Europe's AGM rules rewritten

With entire countries in lockdown throughout AGM season, many companies have been conducting meetings and voting virtually – but some are concerned that this approach risks diluting shareholder voices. "Access to remote voting and participation during the AGM differs between companies. In the best-case scenario, even if intervention during the meeting is allowed, it's not the same as posing a question in person. There is less visibility and a risk that the company filters the questions or does not answer properly," Juan Prieto, managing director of Spanish proxy advisor Corporance, told IFLR in late April. "This is not a good time for shareholder activism – but it does prompt an important discussion on regulating virtual meetings to improve the participation of shareholders remotely."

In-person meetings allow those present to assess tension between shareholders and the board. "Shareholders can push the limits when challenging boards, and on occasion make lengthy speeches instead of asking succinct questions," said White & Case partner Patrick Sarch. "When shareholders are not present, forms of challenge can be made in writing and read out by the company secretary to the chair, which changes the nature of the interaction." Essentially, the mood of the room is an important factor. Business is conducted by human beings, after all. "Meetings will be much more choreographed affairs, which could hand companies more control and dilute shareholders' ability to hold them to account," said Sarch.

While some are proceeding virtually, many companies have opted to postpone their meeting – but it's not hard to imagine this having an adverse effect on performance, with leadership teams dragging their feet and avoiding shareholder discussions. "It is odd that, in the 21st century, these meetings are still required to be held in person," added Sarch. He of course has a point – so with technology improving constantly, are AGMs destined to become a relic? The answer is maybe. As Sarch pointed out, the fact many companies have been scrambling to find a virtual solution is evidence of the attitude towards them in the shareholder community up to this point. Voting services and retail shareholders are particularly sceptical. One thing is certain: a move to virtual would take the theatrics out of many of these meetings.

MAC clauses were thrust into the spotlight in 2017 when Verizon successfully negotiated a lower purchase price for Yahoo following a data breach

MAC clauses to the rescue? Don't count on it

It's no secret that coronavirus and the corresponding lockdown measures have had a significant impact on the volume of completed transactions across the world. But for those that were mid-deal in mid-March, here are three letters that will be very familiar: MAC. Since the start of the pandemic, buyers have been flirting with MAC, or material adverse change, clauses in agreements entered into prior to the outbreak – with sellers concerned by the prospect. As with most things in life, if it sounds too good to be true, it probably is. That's certainly the case for MACs.

Speaking to IFLR in late March, Nandakumar Ponniya, principal at Baker McKenzie Wong & Leow, said that where the event does fall within the scope of the MAC clause, parties will inevitably have differing views on whether the clause can and should be invoked, the level impact of the supervening event on performance of the obligations under the contract, and/or the steps parties should have taken to mitigate the risk. Ellis added that whether a MAC clause can be invoked really depends on the specific wording of the clause and the governing law of the relevant agreement. In general, an event would have to have a significant and long-term adverse impact on the business in question. "In the case of the Covid-19 outbreak, it might be possible to show a sufficiently significant adverse impact, but it would be much more difficult in most cases to prove that that impact will be long-lasting," said Ellis.

Courts and arbitral tribunals are generally reluctant to find that a MAC clause has been triggered, as the event must be covered expressly in the clause and to have had an impact over an extended period of time. "If there were an earthquake and the sole production facilities of a manufacturing company were completely swallowed up by the earth, a court would likely find that a MAC clause has been triggered," she said. "But short of that, the party resisting the invocation of the MAC clause can always argue that in the long term the company will bounce back, even if it requires significant restructuring." In the US, MAC clauses are quite standard in the purchase or merger agreement when a fund is acquiring a company. They're less common on private UK deals. Purchase agreements contain MAC clauses in about 25% of UK deals. "The situation in Asia is somewhere between the US and the UK," added Ellis. "MAC clauses are more commonly accepted by corporate sellers in Asia, but financial sponsor sellers often push back on them."

In general, a MAC is a high hurdle. One of the most high-profile instances of their use was in 2017 when Verizon negotiated a lower purchase price for Yahoo due to the latter suffering a data breach. In one of the few cases where a buyer was able to walk away from a deal, in 2018, a Delaware judge allowed German healthcare company Fresenius to invoke a MAC clause on Akorn, the generic drug maker it aimed to acquire, after it ran into unexpected market competition for some of its mainstay products and its performance "dropped off a cliff".

Buyers should negotiate specific financial thresholds and the general material adverse effect language: for instance, a MAC can be triggered if the target's revenue decreased by a certain percentage or for a certain period of time. "If there are no specific benchmarks then it will be hard to successfully invoke a MAC clause," said Ellis. "Likewise, if the seller is a fund, it should strongly resist any specific financial thresholds."

CORPORATE

CORPORATE GOVERNANCE QUARTERLY

What does a board of directors do?

Goodwin Procter counsel David Bernstein considers the differences between the expectations of regulators and courts and the reality

Section 141(a) of the Delaware General Corporation Law begins: 'The business and affairs of every corporation shall be managed by or under the direction of the Board of Directors.' Corporate statutes in almost every other state of the US have similar language. This makes it sound as though the board plays the principal role in managing a corporation.

But anybody who has ever served on a corporate board of directors, or been involved in the management of a corporation, knows that is not the case. A corporation is run by its management, not by its directors. The principal things directors do is (a) review and discuss strategic decisions and plans proposed by the management, (b) try to make sure the management is not doing anything foolish or improper, and (c) when the corporation encounters major problems, seek (or make sure the management seeks) somebody who can fix them. As is discussed below, increasingly, boards or board committees are being assigned specific tasks that go beyond their principal role, but none of them involves actively managing the corporation.

Nor would it be practical for directors to manage a corporation. In the first place, a director who is not a member of management usually has a full time job, or is a director of multiple corporations, and is not able to devote more than two or three days a quarter (or, if the board meets monthly, a day or two per month) to matters relating to the corporation. Also, it is unlikely that a company could operate if all important business decisions required a consensus of seven, ten, or fifteen directors.

What really happens is that under normal circumstances, almost everything the board does is based upon work done by the management and presented to the board in what is expected to be final form for its approval. A company's annual business plan is prepared by the management and essentially finalised before it is

1 MINUTE READ

The corporate statute in Delaware and almost every other state of the US says that the affairs of a corporation are managed by or under the direction of the board of directors. This sounds as though the board plays the principal role in managing a corporation – but in fact a corporation is run by its management, not its board. While the role of a board is expanding, boards still are not involved in the day-to-day management of corporations. That is fortunate. It is unlikely that a company could operate if all important business decisions required a consensus of all the directors.

Under normal circumstances, almost everything the board does is based upon work done by management

presented to the board for approval. The same is the case with regard to the annual budget and any long-term strategic plan. Financial statements are completed and audited (or reviewed) by independent auditors before they are presented to the audit committee or the entire board for approval. The directors are required to sign a publicly-traded corporation's annual report on Form 10-K, but directors typically don't get a draft of the Form 10-K, which often is more than 100 pages long, until a few days before it is going to be filed, and get little – if any – opportunity to ask probing questions of the management that might uncover inaccurate statements in the Form 10-K.

There is nothing wrong with the role of a board of directors described above. But it is different from what courts, government agencies, and Congress seem to think it is.

In 2019, the Delaware Supreme Court refused to dismiss a suit against the directors of a large ice cream company that was badly hurt when its ice cream became tainted by listeria bacteria, which led to several fatalities. The management had received inspection reports warning that condensation was dripping from pipes and there were other sanitation problems in its plants, and received laboratory reports that product samples had tested positive for listeria. It had not told the directors about these reports, but the Delaware Supreme Court nonetheless found the directors to have failed to meet their oversight responsibilities because they had not created a committee or put in place any other process to monitor food safety. The Delaware Supreme Court said this created an inference that the directors' lack of attentiveness rose to the level of bad faith indifference.

An interesting question is why the management didn't tell the board about the reports at an early stage. Perhaps they were trying to hide the problem from the board (the CEO has been accused of concealing it from the customers). But it is at least as likely that the management felt it was their job to fix what was wrong, and that there was no need to get the board involved. And if it hadn't been for the listeria outbreak and the resulting deaths, the management would have been correct. The pipes would have been fixed and the board probably would never have known, or cared, that there had been a maintenance problem that had been addressed by the management.

The Securities and Exchange Commission (SEC) and the major US stock exchanges have also taken positions with regard to directors that complicate their roles. For many years they have promoted the benefits of corporations having independent directors. That is a sensible position if the principal role of the directors is to make sure the senior managers properly manage the corporations of which they are directors. But if directors are going to be responsible for making operating decisions, most of them should at least have industry experience. It is unlikely that a director who had had a long career as a senior member of an accounting firm would have recognised the danger caused by condensation dripping from pipes in an ice cream plant.

The Sarbanes-Oxley Act of 2002 and stock exchange rules adopted a year later significantly changed the role of directors. The SOX Act requires that every publicly traded company have an Audit Committee consisting entirely of independent directors that, among other things, selects and oversees the accounting firm that audits the company's financial statements, sets the compensation of that accounting firm, and receives reports from that accounting firm regarding matters relating to the corporation's financial statements and internal controls.

Stock exchange rules had required audit committees well before the SOX Act was passed. However, the SOX Act was more specific than then existing stock exchange rules in assigning responsibilities to audit committees. It also contained provisions requiring independent auditors to communicate various types of concerns to audit committees. The requirements of the SOX Act (which became part of the Securities Exchange Act of 1934) and the prospect of SEC enforcement of those requirements caused directors to take much more seriously the responsibilities of audit committee members. Importantly, the responsibilities the SOX Act and related SEC rules impose on audit committees are things directors are capable of doing. Neither the SOX Act nor the SEC rules under it make the audit committee responsible for the substance of financial statements. Management is responsible for that.

Shortly after the SOX Act was passed, both the New York Stock Exchange (NYSE) and Nasdaq adopted rules that further expanded the role of directors. The new NYSE rules required that each listed company have a compensation committee and a nominating/corporate governance committee, each consisting entirely of independent directors. Nasdaq has similar requirements.

More importantly, the rules adopted by the NYSE shortly after passage of the SOX Act require that the non-management directors hold regularly scheduled meetings without management being present and that at least once a year, the independent directors meet separately. Nasdaq soon adopted similar requirements.

The need for non-management directors to meet periodically without management present resulted in a major change in the way public company directors viewed themselves. No longer were they primarily a sounding board for management. When non-management directors meet separately, the almost inevitable discussion topic is how the

It is much easier for independent directors to be critical of management when nobody from management is present

management (including the CEO) is performing. This creates a significant crack in the collegiality that has long typified the relationship between the directors and the CEO of most corporations. It is much easier for independent directors to be critical of management when nobody from management is present.

Statutory and judicial corporate law in Delaware and elsewhere has not always been consistent in defining the role of directors. In Delaware, despite the broad sounding mandate of Section 141(a) of the DGCL ('The business and affairs of every corporation shall be managed by or under the direction of the board of directors'), the legislature has usually been realistic about what directors can be asked to do. Section 141(e) of the DGCL says that a director will be fully protected in relying on the records of the corporation and upon information, opinions, reports or statements of any of the corporation's officers or employees, by board committees, or by any other persons selected with reasonable care by or on behalf of the corporation (a provision that sometimes seems to be overlooked by the Delaware courts). Another provision of the DGCL permits a corporation to eliminate the personal liability of a director to the corporation or its stockholders for monetary damages for breach of the director's fiduciary duty of care.

The Delaware courts have, in most instances, been realistic in their views of what directors can be expected to do. Famously, in most instances, they refuse to second-guess board decisions that are anywhere in the range of possibly reasonable business judgments – but not always. Occasionally they hold a board accountable for things that require expertise far beyond what can be expected of non-management directors (such as the knowledge that there was condensation dripping from pipes and that it could contaminate ice cream). Not infrequently, courts determine that directors should have recognised red flags that are a lot more visible with the benefit of hindsight than they would have been before problems surfaced.

A principal means by which directors are becoming involved in what traditionally has been management decision-making is through the creation of board committees. Many companies use their audit committees, or create special committees, to monitor risk management, to make litigation decisions (particularly if there is at least a theoretical management conflict of interest), to investigate claimed improprieties, and in a variety of other circumstances.

A Nasdaq rule giving temporary relief from a stockholder approval requirement to facilitate financings needed because of the Covid-19 pandemic conditioned the relief on certification by the audit committee that the financing is needed for pandemic-related reasons, and that a reasonable effort to obtain financing elsewhere was made, but was not successful. Of course, in most instances, an audit committee will only be able to make that certification by relying on what it is told by the management.

The use of board committees creates an independent review of corporate decisions or problems. It can work well with regard to governance, legal or financial issues. It is normally not suited to operating matters.

An area where courts frequently assign principal responsibility – not just oversight responsibility – to directors is M&A transactions, and particularly, sales of the companies of which they are directors. Transactions in which controlling stockholders or members of senior management may have personal interests that differ from those of stockholders generally (such as transactions between corporations and other companies in which their controlling stockholders have interests) usually are negotiated on behalf of the corporations by committees of independent directors, with little or no management participation on behalf of the corporations. Approval of a transaction both by a committee of independent directors and by independent stockholders causes courts in Delaware and elsewhere to defer to the business judgment of the committee members even if the transaction normally would be subject to a court review of its entire fairness.

It is not unrealistic for courts to assume that most companies will have independent directors who are able to negotiate a sale of a company, particularly when the independent directors have the assistance of financial and legal advisers. However, courts sometimes assume a level of board involvement in transactions that goes beyond what it is reasonable to expect. For example, courts sometimes criticise CEOs for beginning discussions of possible transactions without prior board authorisation to do so. But CEOs of many companies are constantly engaging in exploratory discussions about possible transactions, and it would be an unreasonable imposition to involve the board before there is a serious possibility that a transaction will take place.

If the board's role is primarily to consider plans and proposals presented to it by the management, what is meant by the statement in Section 141(a) that the business and affairs of every corporation shall be managed by or under the direction of the board of directors, or similar provisions in other state corporate statutes? The principal significance of that statement is to make it clear that the management reports to the board, not to the stockholders. That is an important component of the Anglo-American approach to corporate governance. It is not the approach taken in all countries.

The fact that directors are not involved in the actual management of a corporation does not mean they don't have a significant role to play in how a corporation is managed. The fact that the board will have to approve something usually leads management to put together a carefully thought-through analysis for presentation to the board, rather than making decisions on the basis of intuition or emotion. Further, the fact that boards are not involved in day-to-day decision-making gives non-management directors a perspective that isn't unduly influenced by short-term operating needs or desires. And, of course, the board is the principal protection against poor or dishonest management or actions that benefit managers at the expense of the corporation and its stockholders.

In short, the fact that directors are not involved in the day-to-day management of a corporation is not a bad thing. It is probably a good thing. In any event, it is the reality. Companies are run by management, not by directors. Any attempt to have an even slightly complicated business run by directors rather than management would almost certainly be doomed to failure.

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Competition essentials

Gönenç Gürkaynak and **Öznur İnanılır** of **ELIG Gürkaynak Attorneys-at-Law**
unpick the key aspects of Turkey's merger control regime. A pending Draft Competition Law has now been suspended

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Turkey's primary piece of merger control legislation is the Protection of Competition Law No. 4054 of December 13 1994. Communiqué 2010/4 on Mergers and Acquisitions Requiring the Approval of the Competition Board (Communiqué 2010/4 of October 7 2010) is the secondary piece of legislation. The Competition Authority (Authority) is the enforcement authority and the Competition Board (Board) is the decision-making body.

One notable aspect of the regime is that Turkish merger control rules do not provide a pre-notification mechanism with a submission of a draft notification form. Otherwise, the Authority closely follows developments in other jurisdictions, especially in the EU. In fact, its guidelines are in line with EU competition law regulations and seek to maintain harmony between EU and Turkish competition law instruments. Apart from looking to the EU regime, the Authority also evaluates developments in the Turkish market and takes any necessary steps to stay aligned to its own aims and policies.

Jurisdiction test

Turkey's competition rules capture any merger between two or more undertakings, as well as any acquisitions of control by any entity or person of another undertaking's assets or a part or all of its shares or instruments that grant management rights. These transactions are all notifiable if they result in a permanent change of control.

Joint-ventures (JVs) are considered acquisition transactions. To qualify as a concentration subject to merger control, a JV must be of a full-function character and satisfy two criteria: the existence of joint control in the JV and the JV being an independent economic entity established on a lasting basis.

Pursuant to the presumption regulated under Article 5(2) of Communiqué No. 2010/4, control may be acquired

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Gönenç heads the competition law and regulatory department of ELIG Gürkaynak Attorneys-at-Law, which currently consists of 45 lawyers. He has unparalleled experience in Turkish competition law, with over 20 years of experience. Gönenç represents multinational companies and large domestic clients in over 35 Turkish Competition Authority investigations each year, as well as about 15 antitrust appeal cases and over 85 merger clearances.

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Öznur became a partner in the regulatory and compliance department in 2016 and has extensive experience in all areas of competition law, in particular compliance to competition law rules, defence in investigations alleging restrictive agreements, abuse of dominance cases and complex merger control matters. She has represented various multinational and national companies before the Turkish Competition Authority. Öznur has authored and co-authored articles published internationally and locally in English and Turkish pertaining to her practice areas.

through rights, contracts or other instruments which, separately or together, allow de facto or de jure exercise of decisive influence over an undertaking. In particular, these instruments consist of ownership or operating rights over all or part of the assets of an undertaking, and those rights or contracts grant decisive influence over the structure or the decisions of an undertaking. Control may be acquired by right holders, or by those persons or undertakings who have been empowered to exercise such rights in accordance with a contract, or who, while lacking such rights and powers, have de facto strength to exercise such rights.

A transaction is subject to the Competition Board's approval if the aggregate Turkish turnover of the parties exceeds TL100 million (approximately $17.6 million) and the Turkish turnover of at least two of the parties each exceeds TL30 million. The Board's approval is also needed in acquisitions where the Turkish turnover of the transferred assets or acquired businesses exceeds TL30 million and the worldwide turnover of at least one of the other parties exceeds TL500 million. In merger transactions, transactions where the Turkish turnover of any of the parties in the merger exceeds TL30 million and the worldwide turnover of at least one of the other parties exceeds TL500 million are subject to the Board's approval.

Article 7 of Law No. 4054 prohibits all concentrations leading to a dominant position and the significant lessening of competition in a product market. While the question on whether the transaction is subject to the Board's approval should be taken into consideration within the scope of secondary legislation (the notification thresholds specified under Communiqué No. 2010/4), the question of whether the same transaction creates competition law sensitivities should be assessed within the scope of the primary legislation (Article 7 of Law No. 4054).

The assessment of whether a transaction creates competition law sensitivities is independent from the question of whether the transaction is subject to the Board's approval within the scope of Article 7 of Communiqué No. 2010/4. As per the hierarchy of norms, the fact that a transaction is not subject to the Board's approval would not influence the assessment of the same transaction in terms of its merits.

Article 7 of Law No. 4054, which regulates the control of mergers and acquisitions, prohibits any merger between one or more undertakings or acquisitions by any undertaking from another undertaking (including transactions among global technology and online companies), which creates a dominant position or strengthens a dominant position, and which may result in a significant lessening of competition in a market for goods or services within the whole or a part of the country.

Therefore, Law No. 4054 deems mergers or acquisitions that significantly diminish competition illegal, regardless of whether the relevant turnover thresholds are exceeded or not. The jurisdictional threshold provided under Communique No. 2010/4 acts as a filter by excluding some transactions from the notification obligation, as such transactions do not attain a certain economic size.

Foreign-to-foreign mergers

Turkey's merger control regime does not exempt foreign-to-foreign transactions. If one of the turnover thresholds is triggered, a foreign-to-foreign deal will be notifiable. Law No. 4054 defines an "effects criteria", with the key criterion being whether the undertakings concerned impact Turkey's goods and services market. Even if the relevant undertakings do not have Turkish subsidiaries, branches, sales outlets or other local structures, the transaction could still be subject to merger control if the relevant undertakings have sales in Turkey and the merger therefore impacts the Turkish market.

Furthermore, the Competition Authority is empowered to exchange information with certain regulatory authorities around the world, including the EU Commission Competition Directorate-General (DG Comp). Article 43 of Decision No. 1/95 of the EC-Turkey Association Council (Decision No. 1/95) authorises the Authority to notify and request the DG Comp to apply relevant measures if the Competition Board believes that a transaction realised within EU territory may adversely affect competition in Turkey. This provision grants reciprocal rights and obligations to the parties (EU-Turkey). Although, there have been cases where the Authority has exchanged information with the EU Commission and other competition authorities, the EU Commission has been reluctant to share evidence or arguments with the Authority in the few cases where the Authority has explicitly asked for them.

The Authority's research department also makes periodic consultations with relevant domestic and foreign institutions and organisations.

Notification

Filing is mandatory once the parties' turnovers exceed the thresholds. The existence of an affected market is not sought in assessing whether a transaction triggers a notification requirement.

If the parties violate the suspension requirement or do not notify the transaction, the Board imposes a turnover-based monetary fine. The minimum fine in 2019 is TL26,027.

If there is a risk that the transaction might be viewed as problematic under the dominance test and the transaction is closed before clearance, the Authority may launch an investigation. It may order structural or behavioural remedies to restore the situation to that of pre-closing and impose a fine up to 10% of the parties' annual turnover. Executive members who have a significant role in the infringement may also receive monetary fines of up to 5% of the fine imposed on the undertakings.

A notifiable concentration is invalid with all its legal consequences, unless and until it is approved by the Board.

Even though there is no specific deadline for filing, it is advisable to file the notifiable concentration to the Authority at least 45 calendar days before closing (a transaction is deemed closed on the date the change of control occurs (Article 10, Communiqué)).

The filing can be made by either one of the parties to the transaction or jointly, and there is no filing fee. There is also no specific deadline for filing but it is advisable to file the transaction at least 45 calendar days before closing (a transaction is deemed closed on the date when the change of control occurs (Article 10, Communiqué)). However, there is an explicit suspension requirement (namely that the transaction cannot be closed before obtaining the approval of the Board), which is set out under Article 11(1)(a) of Law No. 4054 and Article 10(5) of Communiqué No. 2010/4.

The notification form is similar to the European Commission's Form CO. Certain additional documents are also required (such as the transaction documents and their sworn Turkish translations and annual reports.)

Review process

After a preliminary notification review, the Board decides either to approve or to further investigate the transaction (Phase II). There is an implied approval mechanism where a tacit approval is deemed if the Board does not react within 30 calendar days of a complete filing. If the information requested in the notification form is incorrect or incomplete, the notification is deemed filed only on the date when this information is completed after the Board's request for data. A Phase II review takes about six months and may be extended for only one additional period of up to six months.

During either phase, the Authority can send written requests to the parties, to any

Key

- Indicates a regime in which regulation is predictable, light touch and low impact (green)
- Indicates a regime in which regulation is generally predictable or moderately intrusive (orange)
- Indicates a regime in which regulation is unpredictable or highly intrusive (red)
- Jurisdiction test
- Notification
- Review process and timetables
- Judicial review

	JURISDICTION TEST			NOTIFICATION				REVIEW PROCESS AND TIMETABLES			JUDICIAL REVIEW
	Types of M&A and JV caught	Thresholds for notification	Foreign-to-foreign mergers	Mandatory or voluntary	Filing fees	Filing requirements/deadline	Pre-notification contacts	Timetable for clearance	Substantive test	Remedies available	Ability to appeal
Turkey ELIG Gürkaynak Attorneys-at-Law	green	orange	red	red	green	orange	green	green	green	orange	orange

other party relating to the transaction or to any third parties, such as competitors, customers or suppliers.

If the Authority asks for another public authority's opinion in reviewing a transaction, the applicable time periods for the approval mechanism automatically reset to the date on which the relevant public authority submits its opinion to the Authority.

The substantive test for clearance is the dominance test. Efficiencies may play a more important role in cases where the combined market shares of the parties exceed 20% for horizontal overlaps and the market share of either of the parties exceeds 25% for vertical overlaps. The Board may consider efficiencies to the extent they operate as a beneficial factor.

Parties to a proposed transaction can provide commitments to remedy substantive competition law issues relating to a concentration under Article 7 of the Competition Law (Article 14, Communiqué) and the Authority stipulates that structural and behavioural remedies can be imposed to restore the situation as before the closing (*restitutio in integrum*). Parties have the discretion to offer and submit behavioural or structural remedies (Guidelines on the Remedies that Are Acceptable by the Competition Authority in Mergers and Acquisitions (Guidelines)) and although structural remedies take precedence over behavioural remedies, in some cases the Board has accepted behavioural remedies.

The Board will neither impose nor ex-parte change any submitted remedies. In the event the Board considers the submitted remedies insufficient, it may allow the parties to make further changes to its remedies. If the remedy is still insufficient to resolve the competition concerns, the Board may block the transaction.

Parties can submit proposals for possible remedies either during the preliminary review (Phase I) or the investigation period (Phase II). While parties can submit the commitments during Phase I, notification is deemed filed only on the date of the submission of the commitments. In any case, a signed version of the commitments that contains detailed information on their context and a separate summary should be submitted to the Authority. The Authority's Remedy Guidelines also provide a form that lists the necessary information and documents to be submitted in relation to the commitments.

The Board's final decisions can be submitted to judicial review before the administrative courts by filing a lawsuit within 60 days of the receipt by the parties of the Board's reasoned decision. Rights of judicial review are available only to the parties to the decision. Third parties can challenge the Board's decision before the competent judicial tribunal, provided that they prove their legitimate interest. The judicial review period before the administrative court usually takes about 24 to 30 months.

Looking ahead

In 2019, important merger control decisions concerning high-value transactions were taken by the Authority. One highlight was the Board's *Nidec/Embraco* decision regarding the transaction concerning the acquisition of sole control of Embraco, Whirlpool Corporation's compressor manufacturing business, by Nidec Corporation (April 18 2019). After a Phase I review the Board took the transaction to a Phase II review, due to competition law concerns arising from the deal. Notwithstanding this, the transaction was approved pursuant to a commitment package submitted to the EU Commission which involved Nidec divesting its own light commercial compressor and household compressor businesses. The Board concluded that those commitments would eliminate the horizontal and vertical overlaps in Turkey regarding the sales of household reciprocating hermetic cooling compressors, reciprocating hermetic light commercial cooling compressors and the sales of condenser units.

The Board also conditionally approved Harris Corporation's acquisition of sole control over L3 Technologies (June 20 2019) in a Phase I review. The Board held that commitments had completely eliminated the overlap between the parties and that therefore, the transaction did not result in the creation or strengthening of a dominant position, nor did it significantly impede competition. In line with the commitments submitted to the Commission, Harris committed to divest its businesses for night vision devices and image intensifier tube Technologies used in these devices to eliminate the vertical overlap.

With respect to the legislative reforms, the Draft Competition Law, which was issued by the Authority in 2013 and officially submitted to the Presidency of the Turkish Parliament on January 23 2014, is now null and void following the start of a new legislative year of the Turkish parliament. To re-initiate the parliamentary process, the draft law must again be proposed and submitted to the presidency of the Turkish Parliament. At this stage, it remains unknown whether the Turkish Parliament or the government will renew the draft law.

CAPITAL MARKETS

FUNDING INSURANCE COMPANIES

When the usual rules don't apply

Baker McKenzie lawyers explain the challenges faced by regulated insurance companies when seeking leveraged debt financing

The process by which financial sponsors or strategic corporates evaluate the ability to finance the leveraged acquisition of a company, or by which lenders or investors evaluate whether or not to loan to or invest in a particular leveraged credit, are driven by a number of factors – the size and profitability of the business, the industry and jurisdiction(s) of the corporate borrower, the cashflow generation available to service debt, plus any number of internal and external factors. These considerations typically lead to an analysis of leverage levels, the availability of structural protections, and the ability of operating companies to fund their businesses while servicing their debt.

But what if the nature of a particular market:

- hinders the ability of creditors to receive customary structural support from borrowers, such as asset security or corporate guarantees from operating subsidiaries;
- potentially limits a creditor's ability to enforce on its claims in the event of a default, including following a business downturn;
- means that traditional measures such as debt/Ebitda leverage may not properly reflect the healthiness (or lack of healthiness) of a business; and/or
- puts additional non-market restrictions on the ability of subsidiaries to send cash up to a holdco debtor or to pay dividends to shareholders?

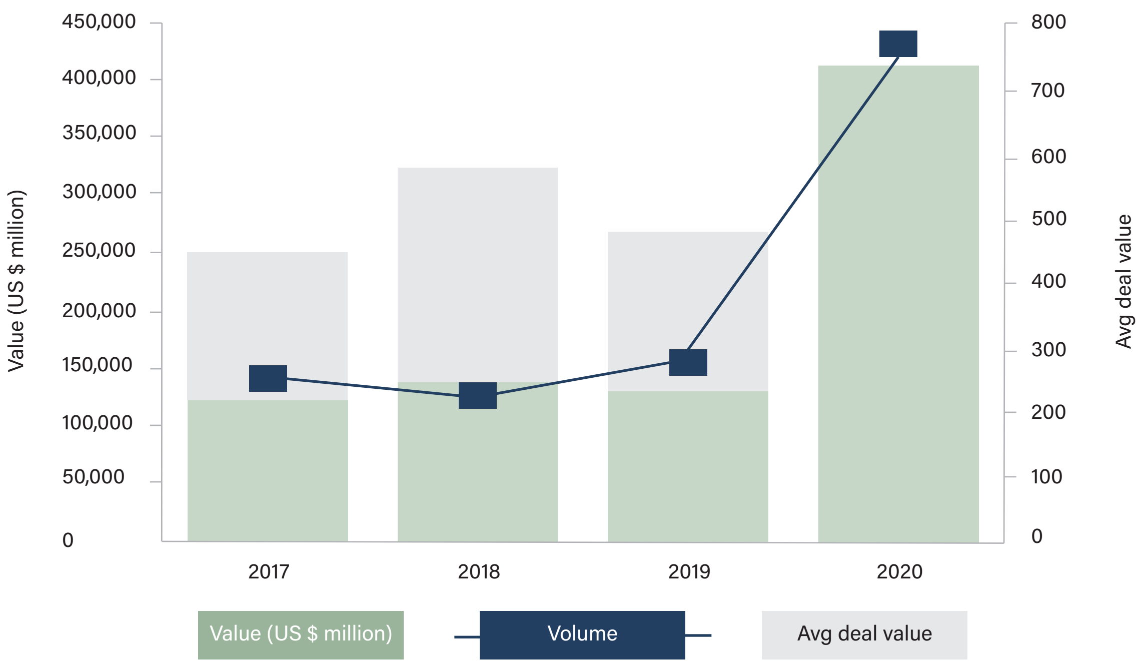
These are some of the factors that become relevant in connection with a leveraged financing for a regulated insurance company, whether for a sponsor or company when trying to ensure compliance with regulatory requirements, or for potential creditors who need to confidently evaluate an insurer's corporate's strength and the protections provided by the financing structure.

This article considers some of the challenges faced by market participants when a regulated insurer seeks to tap the financial debt markets, in the US and internationally.

1 MINUTE READ

Regulated insurers typically rely on customer premium payments and investment returns to fund their day-to-day operations. But from time to time, regulated insurers seek to raise money through other available market sources, for example, to fund an acquisition or make a strategic investment. Likewise, regulated insurers themselves have increasingly been subject to buyouts by financial sponsors who typically look to leverage their investment with debt financing. In this article, Baker McKenzie lawyers consider some of the challenges faced by market participants when a regulated insurer seeks to tap the leveraged debt markets.

Figure 1: Borrowings by Insurance Companies - Value and Volume - 2017-2019



We discuss some alternate metrics and structures often used in these financings, some mitigating factors, and some factors for which market participants just need to play through the differences to get a deal done.

A brief history of debt financing in the regulated insurance market

Insurers traditionally fund their operations through the receipt of customer premium payments and complex money management strategies that take into account risk-return models and regulated capital adequacy requirements. Still, like any company in any industry, insurance companies need to consider all sources of funding when building the optimal capital structure, including third party lending in its traditional forms. Financial sponsors, who typically operate a leveraged investment approach, are increasingly looking to regulated insurance assets. Traditionally, financial sponsors have focused on the lighter-touch regulated insurance brokerage businesses, but there have been a number of recent high profile regulated insurance buyouts – which suggests that regulators and financial sponsors are becoming increasingly familiar with each other and the innovative debt capital structures used to finance these acquisitions.

Figure 1 sets out third party borrowing by insurance companies for the year 2017-2019.

How to measure financial strength

Unlike in traditional leveraged finance models, Ebitda or consolidated cashflow metrics for a regulated insurance business may not be a representative measure of true liquidity, as a substantial amount of capital may be 'locked up' in the regulated group as a result of capital maintenance rules or other regulatory requirements that serve to restrict value leakage. These cashflow metrics may, however, be appropriate for non-regulated segments of the group's operations. Identifiable distributable reserves for the regulated group can provide a better indication of the amount of capital that is available to service debt from time to time, but must be considered after factoring in any discretionary capital buffer and is not directly comparable to traditional liquidity metrics, which can further complicate the picture when trying to assess the financial viability of both the regulated and unregulated aspects of the business.

Consequently, covenants in debt documentation for regulated insurance borrowers are less likely to include many of the financial tests that are considered standard in other parts of the leveraged finance market, including debt/Ebitda leverage ratios. Alternative financial tests deployed in the regulated insurance space include measuring consolidated net worth, additional solvency protections (typically reflecting regulatory requirements), and a leverage ratio test that utilises an equity- or asset-based denominator (for example, the sum of debt and consolidated net worth), which often includes restrictions on netting of regulatory cash and may also exclude debt-like obligations of operating subsidiaries under certain insurance products.

Regulated insurance markets: what's different?

Overview

The global insurance industry is highly regulated, with many internationally and locally-focused organisations providing oversight. Internationally, groups like the International Association of Insurance Supervisors (IAIS), an arm of the Financial Stability Board (FSB), seek to establish standards and to identify risks that support the stability of the international financial markets, which is balanced against the need to ensure that policyholders are treated appropriately. These regulatory initiatives are similar to Dodd-Frank in the US, where insurance industry regulation is primarily state-driven, with federal oversight

Figure 2: Financial tests in regulated insurance deals

		Deal X	Deal Y	Deal Z
Product		Syndicated loan	Syndicated loan	Senior facilities
Regulated vs. unregulated business?		Regulated	Regulated	Regulated
Leverage ratio	**Numerator**	Consolidated total debt Not calculated net of cash Excludes obligations of any insurance subsidiary under any primary insurance policy, reinsurance agreement or other insurance or reinsurance product	Consolidated total debt Calculated net of unrestricted (statutorily and otherwise) cash in an aggregate amount not to exceed $25.0 million, to the extent such cash is subject to a lien and deposited in an account subject to a control agreement, in each case, in favour of the collateral agent Excludes obligations with respect to insurance products underwritten by an insurance subsidiary and obligations under any reinsurance agreements or retrocession agreements or in connection with certain permitted investments of insurance subsidiaries	Net debt Calculated net of operational cash, i.e. cash and cash equivalents held by the group less cash and cash equivalents held by the insurance group in order to meet its targeted solvency levels Does not exclude obligations under or with respect to insurance products
	Denominator	Sum of consolidated total debt (see above) + consolidated tangible net worth (see below)	Sum of consolidated total debt (see above) + consolidated net worth (see below)	Adjusted EBIT Derived from consolidated operating profit of the insurance group
Interest coverage ratio	**Numerator**	N/A	N/A	Adjusted EBIT (see above)
	Denominator	N/A	N/A	Net finance charges
Solvency ratio	**Definition**	N/A	N/A	Calculated on the same basis as solvency is tested by the relevant regulator
Net worth test	**Definition**	Consolidated tangible net worth = consolidated stockholders' equity less consolidated intangible assets	Consolidated net worth = consolidated stockholders' equity less the amount of certain investments	N/A

established in the wake of the market destabilisation caused by the financial crisis from the prior decade. The key objectives of these regulations include promoting global competitiveness, reducing inefficiencies and complexity, providing for comparability of products and markets, aligning industry standards, and promoting financial stability.

These considerations lead to a unique set of issues in the regulated insurance space. Debt financing, including in the context of the acquisition of regulated insurance assets, generally follows traditional forms, but, in the case of a regulated insurer with an additional set of hurdles, are similar in many ways to the issues facing other FIG [financial institutions group] financings. These include:

Managing (and access to) the relevant regulator(s)

Similar to other regulated industries, financial sponsors face additional complexity in the context of competitive bid processes

Figure 3

for regulated insurance assets. While this is a jurisdiction-by-jurisdiction analysis and regulators are interacting with financial sponsors more frequently, access to the relevant regulator may not always be available at the bid stage to approve the financial sponsor's proposed acquisition structure, including in particular the amount of debt that can be incurred in or above the regulated group. Nonetheless, this is often required to provide a certain funds bids in order to compete with trade buyers. Accordingly, financial sponsors may run multiple commitment papers or structures with their lenders (across different leverage levels) and/or agree to finance the acquisition with a 100% equity commitment, and take the risk of confirming their financing structure with the relevant regulator after signing the sale and purchase agreement.

Ability to upstream cash

The ability to upstream cash from regulated operating companies in order to make interest payments on external debt (or to pay dividends to equity investors) is often limited in these structures, including by capital adequacy rules or the need for ad hoc regulatory approval, as well as by customary limitations such as the availability of distributable reserves. If debt at a holding company is to be serviced via interest payments on shareholder loans, such loans may need to include restrictions on early prepayment and/or a lengthy non-call period in order to qualify as permissible capital under the applicable solvency regulations.

Credit support restrictions

Solvency requirements, among other factors, may limit the pool of collateral and guarantees that may be available to grant in support of a debt financing, particularly from a regulated group. In addition, the terms of the debt may need to provide for the automatic release of security or guarantees granted by non-regulated entities in the group if such entities subsequently fall within the scope of regulation.

Single points of enforcement through share pledges become particularly important in these structures. Local regulations may prohibit share pledges over target entities, so establishing a non-regulated holdco structure can provided critical protections (see financing case study). Similarly, intercreditor arrangements with other creditors should be established to confirm the expected ranking of claims in an enforcement scenario. An indirect or direct change of control over a regulated entity (or in certain jurisdictions, acquisitions of equity or other ownership rights by a third party) may require pre-approval from regulatory authorities, thereby increasing the risk that lenders will not be able to enforce key share pledges or impede a distressed sale.

Holdco and PIK financing structures

These structures are more prevalent in insurance deals in light of the security/ guarantee and debt service restrictions discussed above, as financial sponsors look to add their leverage structure above the regulated group.

Local law considerations

Local counsel should be approached early in any proposed financing process to advise on the foregoing issues and structural considerations, including in particular any structural ringfencing of the regulated group and the extent to which local laws or regulations restrict the ability of regulated entities to grant security and/or guarantees for the benefit of creditors. Local counsel may also be well-placed to advise on the risks of any particular financing structure being rejected by, and to guide related discussions with, the relevant regulator.

Financing case study

The hypothetical case study below considers some of the issues faced when structuring a leveraged debt financing for a regulated insurance company. In this sponsor-driven example, a newly formed bidco (BidCo) acquires a regulated European insurance provider and its consolidated subsidiaries (Target Group) through a holding company structure.

The hypothetical financing is comprised of PIK [payment in kind] facilities (by 'FinCo HoldCo') and Senior Facilities (by FinCo).

Key structuring considerations

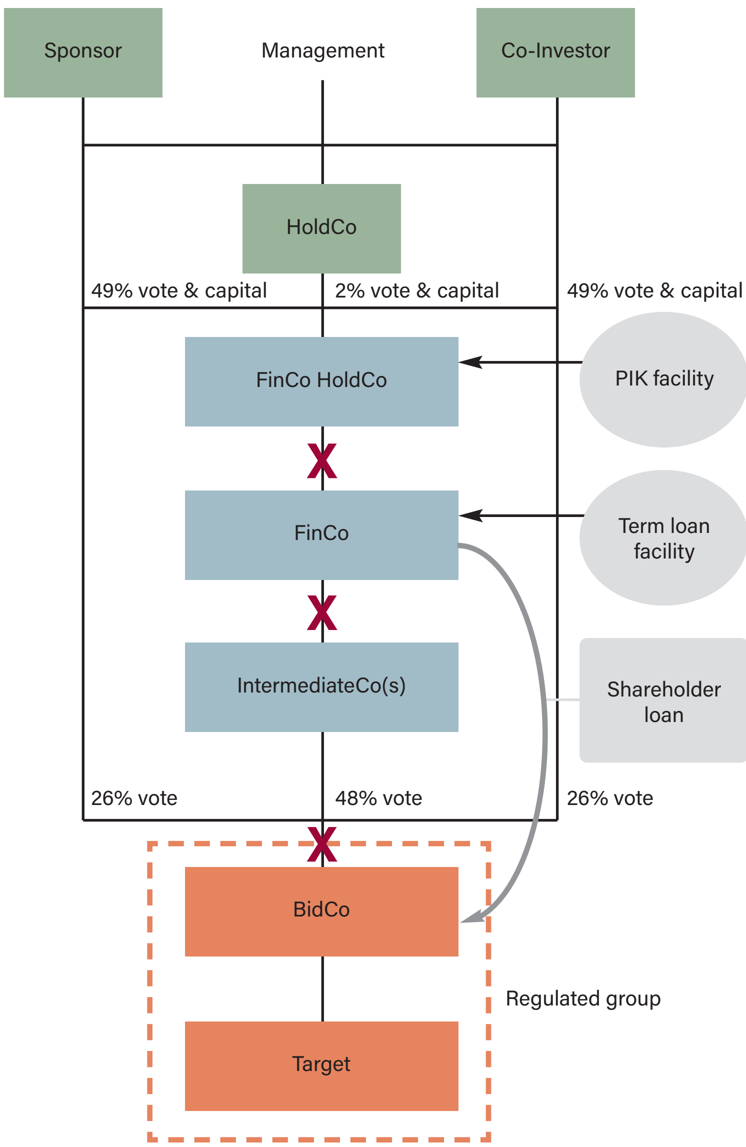
Ringfencing of regulated group:

- The target group is subject to full regulatory supervision and capital adequacy/solvency requirements. Due to local regulatory requirements, the sole shareholder of the target group (BidCo) is subject to the same regulatory regime and comprises part of the regulated group.
- The financing structure is meant to ensure that HoldCo, FinCo HoldCo, FinCo and IntermediateCo(s) (each as shown in figure 4) are not subject to regulatory oversight as no single holdco or investor entity (including the sponsor/co-investor) owns more than 50% of the share capital and voting rights in any member of the regulated group. Depending on the type of activities undertaken by the regulated group and the jurisdictions involved, this ringfencing can also be achieved by a placing a non-EEA holdco borrower above the regulated group.

Credit support:

- Senior facilities are not guaranteed but benefit from security over intra-group loans made by FinCo to BidCo, as well as pledges over shares of Finco, IntermediateCo and BidCo and (potentially) Target Group (if local regulation allows).

Figure 4



- PIK facilities benefit from (i) guarantees by FinCo HoldCo and HoldCo and (ii) certain topco share pledges, pledges over shares of FinCo HoldCo, and the assignment of certain receivables owing to HoldCo.
- No Target Group guarantees and no Target Group assets apart from shares may be pledged due to regulatory solvency requirements.

Covid-19's impact on the insurance industry

As discussed above, insurance companies rely on premiums paid under policies and portfolio management to generate revenues, with the requirements for third party financing often limited to one-off needs. In the context of this article, the main effects of the Covid-19 crisis may be that insurance companies delay or cancel opportunistic transactions, such as acquisitions or strategic investments. On the flipside, the crisis may provide opportunities to invest in undervalued assets.

Risks facing the insurance industry in general due to the pandemic include:

- **Payment risk** Delayed payments from policies balanced against the expectation that insurers will still pay out on claims, or a decrease in payment volumes (e.g., if consumers buy fewer houses, cars, etc. which require insurance backing).
- **Investment risk** Insurers' investment portfolios may be significantly impacted, both in terms of value and interest income. Additionally, interest income revenue streams may be impacted as interest rates continue to fall.
- **Expanded coverage scope** The market is unsettled with respect to coverage for business interruption and other losses for claims resulting from the Covid-19 pandemic.

While the usual rules of leveraged finance don't always apply to regulated insurance companies, market participants have adapted to these challenges and developed innovative financing structures to enable insurance companies and financial sponsors to access debt financing on terms that, where possible, mitigate the risks to lenders and investors who provide such financing. While it is difficult to assess the financial impacts of the Covid-19 pandemic on the insurance industry and what the mid- to long-term future holds for M&A activity for insurance assets and the debt capital markets generally, this article highlights that insurance companies and financial sponsors (and their advisors) who are well prepared to face the sector-specific issues and address these issues early in the debt financing process, will have a strategic advantage in mitigating the risks associated with financing regulated insurance assets and getting the deal across the line with their financiers.

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CAPITAL MARKETS
SWISS BEARER SHARES

Switzerland restricts bearer shares

Prager Dreifuss lawyers discuss how the Global Forum Act targets beneficial ownership transparency

1 MINUTE READ

Mark Meili and Manuel Vogler of Prager Dreifuss outline the effects of the new Swiss rules on the disclosure of beneficial owners and the related restrictions on Swiss bearer shares. This article focuses on the Swiss implementation of the recommendations of the Global Forum Act. The authors outline what steps companies and holders of shares, in particular bearer shares, need to take by a certain deadline in order to comply with the new rules, and what sanctions may be expected in cases of non-compliance.

The Financial Action Task Force (FATF), headquartered at the OECD in Paris, is regarded as one of the leading international bodies for combating money laundering and terrorist financing. It regularly reviews its members' national regulations as to the status of the implementation of its 40 recommendations, so too in Switzerland. As a result of FATF's findings in its first evaluation in 2012, Switzerland introduced the Federal Act for Implementing Revised FATF Recommendations of 2012 (FATF Act) on July 1 2015. The main objective of the FATF Act was to improve the national transparency provisions governing bearer shares. In particular, a purchaser of bearer shares in a Swiss joint stock corporation has since been obliged to report the acquisition to the respective company within one month.

The number of acquired shares is irrelevant; the acquisition of a single bearer share is sufficient to trigger the reporting requirement. Further, any person who alone or in joint agreement with third parties acquires shares in a Swiss company (Ltd or LLC) and thereby reaches or exceeds the threshold of 25% of the share capital or voting rights, has since been obliged to notify the company of the first and last name and address of the beneficial owner. Additionally, companies now have to keep a register of the holders of bearer shares as well as of the beneficial owners reported to the company. The register must be maintained in such manner that it can be accessed in Switzerland at any time.

Further, the documents on which the notice was based must be retained for 10 years following a person's deletion from the register. Shareholders and governing bodies of companies that fail to comply with these measures can face substantial private and criminal law sanctions if their actions contribute to money laundering and insufficient diligence in financial transactions.

Problems and concerns

Within the OECD, the Global Forum on Transparency and Exchange of Information for Tax Purposes (Global Forum) ensures that international standards regarding transparency and the exchange of information for tax purposes are complied with and implemented in a uniform manner internationally. Like the FATF, the Global Forum also reviews the national regulations of its member states as to the levels of their transparency. For this purpose, the Global Forum started peer reviews in the area of administrative assistance in tax matters on request and came to the conclusion that Switzerland's regulations were largely compliant with the international standards in July 2016.

However, in a second round of peer reviews which commenced in 2016 and put an emphasis on *inter alia* the identification of beneficial owners, the Global Forum concluded that the Swiss measures on the transparency of bearer shares were not sufficiently effective. The main criticism was that the measures introduced by the FATF Act in 2015 did not ensure the flawless identification of beneficial owners of bearer shares. This led to the Swiss government starting a rushed legislation process to implement the recommendations of the Global Forum in order to obtain a good assessment at the end of the second peer review round in 2020. As a result, the Federal Act on the Implementation of Recommendations of the Global Forum on Transparency and Exchange of Information for Tax Purposes (Global Forum Act) entered into force in Switzerland on November 1 2019.

Swiss approach to improve transparency of beneficial ownership

Partial abolishment of bearer shares

The principal measure imposed by the Global Forum Act is the partial abolition of bearer shares for joint stock companies. There are two exceptions: bearer shares issued in the form of intermediated securities held by a Swiss custodian designated by the company and bearer shares of publicly listed companies which may still be issued. The intermediated securities must be held on custody accounts with a financial institution (e.g. bank or securities dealer). To prove that they fulfil any of the two exceptional provisions, the companies must file a notice with the commercial register.

Transitional regime for pending bearer shares

In order to grant affected companies sufficient time to implement the new measures of the Global Forum Act, the legislator has provided a transitional regime. From November 1 2019, when the Global Forum Act came into force, joint stock companies have a period of 18 months to amend their articles of association and convert the existing bearer shares into registered shares (unless they fulfil one of two exceptions mentioned above). Hence, the affected companies have until April 30 2021 to convert their bearer shares into registered shares. The same deadline applies for the notification (to the commercial register) of joint stock companies fulfilling any of the two aforementioned exceptions.

Automatic conversion

Bearer shares that are still issued at the end of the transitional period on May 1 2021 will automatically be converted into registered shares by operation of law. The competent commercial register office will record this change in the commercial register including a note showing that the commercial register documents differ from the entry records. This note remains until the company's articles of association have been amended to comply with the new legal situation. Until the articles of association have been amended, the commercial register is bound to reject any requests to register other changes to the articles of association in the commercial register.

Despite the conversion of the bearer shares into registered shares, such shares will retain their existing nominal value, voting and financial rights. The conversion of the bearer shares will also be effective towards third parties who plan to purchase such shares. In order to transfer the converted shares, they will have to be endorsed and the new purchaser will have to request the company to register his details (name, address) in the share register.

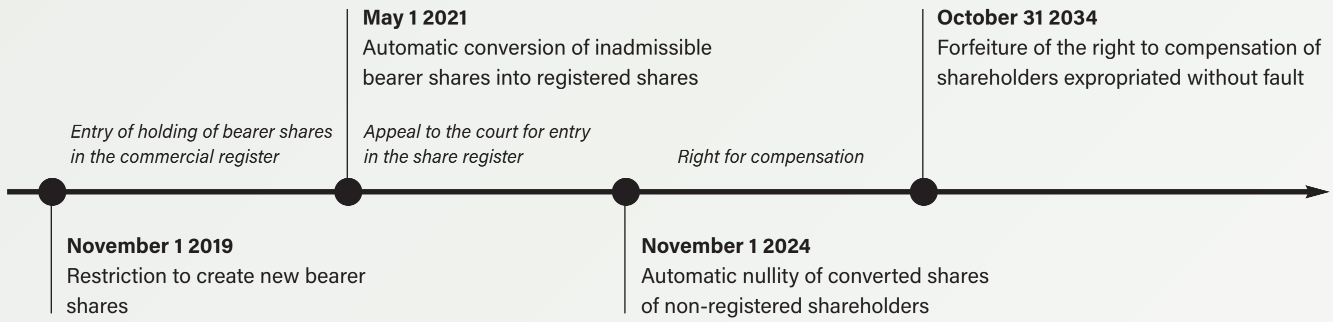
Consequences for holders of bearer shares

Since the FATF Act entered into force, purchasers of bearer shares have the obligation to notify to the company their first and last name and their address within one month since the purchase of the shares. All holders of bearer shares who have complied with these disclosure duties will be registered by the respective company in its share register after the conversion of the bearer shares. Shareholders who fail to fulfil their reporting obligations will not be registered after the conversion of the bearer shares into registered shares and will lose their voting and property rights. Furthermore, the fact that the shareholder failed to report the required information will be recorded in the share register. Within five years of entry into force of the Global Forum Act (i.e. at the latest by October 31 2024) and with the company's prior approval, defaulting shareholders have the possibility to request from the court that they be registered in the share register. If the request is successful, the shareholder will be registered and again be fully entitled to the shares. So far it is not clear under which conditions the company shall give its approval and under which conditions the court will decide in favour of the requesting shareholder. Presently, it appears that the court will merely verify that the shareholder is in fact the entitled owner of the shares and the shareholder then has to request the company to be registered in the share register.

Cancellation of bearer shares

Where defaulting shareholders fail to ensure their reinstatement within the five-year period, their shares will become null and void by law and the shareholders will lose all their shareholder's rights. The shareholders will thus be expropriated by the law. This measure is irreversible for the affected shareholders. The only option still available to the shareholders will be to apply to the court and demonstrate that they were not at fault for failing to disclose their shareholding and thus have a right to compensation in the amount of the fair value of their former shares. The right to compensation will lapse within a 10 year period since the entry into force of the Global Forum Act on October 31 2034. However, the chances for expropriated shareholders to be compensated will in reality be slim, as they themselves are in most cases to blame for the failed reporting and therefore have no valid claim for compensation. Accordingly, this measure will be of limited use. Finally, it must be noted that a compensation can in any event

The transitional regime of the abolition of bearer shares can be summarised as follows:



only be paid out if the company has sufficient freely disposable equity.

Clarifications of reporting obligations

Apart from the partial abolition of bearer shares, the Global Forum Act also amended the obligation to disclose the beneficial owners of shareholders who, by themselves or by agreement with third parties, acquire shares in an unlisted company and thus reach or exceed the threshold of 25% of the share capital or voting rights.

As a consequence, the Global Forum Act aligned the term beneficial ownership with the Swiss accounting principle of corporate control. Accordingly, if the purchaser of at least 25% of the shares of a company is a legal entity, each natural person who controls the purchaser must be reported as the beneficial owner if any of the following requirements are fulfilled:

- the natural person directly or indirectly holds a majority of votes in the highest management body;
- the natural person directly or indirectly has the right to appoint or remove a majority of the members of the supreme management or administrative body; or
- the natural person is able to exercise a controlling influence based on the articles of association, the foundation deed, a contract or comparable instruments.

If a natural person cannot be identified, the purchasing shareholder must give notice of this fact to the company whose shares were acquired. This negative disclosure ensures that the acquirer of the shares fulfils the notification obligations.

The legislator further clarified the disclosure obligations for listed companies and their affiliates. If the acquiring shareholder is controlled by such a company or controls a listed company, it must only give notice of this fact to the company and provide details of the company's name and registered office. A natural person as beneficial owner does not have to be identified in this case.

A new provision is that shareholders must give notice to the company within three months of any change to the first name or surname or of the address of the beneficial owner. This deadline ensures that shareholders report such changes in due time and avoid sanctions aimed at shareholders who fail to update the formalities of their declaration.

Sanctions for non-compliance

Civil law

As explained above, shareholders may have an obligation to report a beneficial owner to the company when they acquire shares. Swiss law provides for sanctions for shareholders who fail to give such notice. For as long as shareholders fail to comply with their obligations to give notice, the voting rights and property rights conferred by the shares are suspended.

Companies may also be sanctioned if they do not comply with their obligations to register its shareholders and beneficial owners. Companies are obliged to keep the share register and the register of its reported beneficial owners in accordance with the new regulations. This means that when a transfer of shares is reported to the company, it has the obligation to examine it from both a formal and a substantive point of view. Further, the company has a duty to update the share register within a reasonable period. In general, the same duties apply in relation to the company's register of its reported beneficial owners, though it is doubtful whether the company has the duty to actively identify the beneficial owners of its shares. If the company does not fulfil its legal obligations, any shareholder, creditor or the commercial registrar may request the court to take the required measures to remedy this organisational defect. In practice, an organisational defect will exist if a shareholder has made a notification to the company but the company fails to update the share register or register of its reported beneficial owners or does so incorrectly. The court may allocate the company a grace period, under threat of its dissolution, within which to re-establish the lawful situation.

As previously explained, under the new regulations joint stock corporations may only continue to issue bearer shares if (i) they have equity securities listed on a stock exchange or (ii) the shares are issued as intermediated securities held by a Swiss custodian designated by the company. As of May 1 2021, a new provision will be put in place which stipulates that an organisational defect exists if a joint stock corporation has issued bearer shares but does not fulfil either of the two exceptional provisions to do so. As a consequence, any shareholder or creditor or the commercial registrar may request the court to take the required measures. The court may then order the conversion of bearer shares into registered shares.

Criminal law

Until the recommendations of the Global Forum implemented in Switzerland in 2019, a violation of reporting obligations under

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company law had consequences only under civil law. The Swiss legislator decided that in order to create effective and clear consequences in connection with the new transparency provisions, the criminal law also needed to be amended. The Swiss Criminal Code now provides for sanctions for shareholders and governing bodies of companies that violate the beneficial ownership transparency provisions. The Swiss legislator thus introduced a regime that exceeds the recommendations of the Global Forum.

In particular, any shareholder who willfully fails to give notice of the beneficial owner of shares is liable to a fine up to CHF 10,000 ($10,277). The scope of this criminal provision also includes an obligation for the shareholder to report changes in the first name, surname or address of the beneficial owner. An erroneous, incomplete or late declaration can also be sanctioned. This may lead to problems and uncertainties because there are still situations in which it is unclear who actually needs to be reported as the beneficial owner (e.g. in case of shareholders agreements).

On the company level, a governing body is liable to a fine up to CHF 10,000 if he or she willfully fails to keep the share register or the register of the beneficial owners of the shares in accordance with the regulations. This can also mean a failure to correctly keep the register of shareholders and the register of beneficial owners or a failure to adequately store the registration documents. It is to be noted that only those who are legally obliged to keep the register are liable (e.g. the members of the board of directors or the persons to whom the obligations were validly delegated). The company itself cannot be liable.

Advice to companies and holders of Swiss (bearer) shares

Companies and shareholders in Swiss companies holding (bearer) shares should do the following, irrespective of whether they are domestic or foreign holders:

- Joint stock corporations which have issued bearer shares need to assess whether they fulfil any of two the exceptional provisions that allows them to continue to issue bearer shares. If they do, they need to register this fact in the commercial register until May 1 2021.
- On the other hand, joint stock corporations which may no longer issue bearer shares, should pro-actively convert bearer shares into registered shares. If the bearer shares are converted by law on May 1 2021, joint stock corporations must ensure that the conversion is properly reflected in the articles of association and the commercial register.
- All companies need to analyse whether their corporate housekeeping instruments (share register, register of reported beneficial owners) are compliant in view of the new criminal sanctions.
- Shareholders of non-listed joint stock corporations who hold bearer shares or more than 25% of the share capital in any company, need to carefully review their existing filings and cure any deficiencies immediately. If holders of non-listed bearer shares fail to comply with the transparency requirements by May 1 2021, they must apply to the court for registration in the commercial register. If the additional five-year deadline is missed, they may be expropriated and lose their rights without compensation.

Outlook

The implementation of the measures of the Global Forum Act by the Swiss legislator will without doubt improve transparency regarding shareholders and beneficial owners of Swiss companies. Bearer shares will be partially abolished and converted into registered shares. Only few joint stock corporations still qualify to issue bearer shares. In each case the shareholders will have to be made transparent and the beneficial owners will have to be reported. Companies and shareholders urgently need to undertake the necessary steps to comply with the legal requirements.

All of these new obligations entail the risk that not all of those affected will be aware of the new duties and may suffer negative consequences. Ignorance could even lead to unnecessary criminalisation of shareholders and board members. The legal and business communities therefore need to work together to analyse the required actions and find practicable and pragmatic solutions to this new framework.

CAPITAL MARKETS
SWISS PROSPECTUS RULES

Exchange offers under Switzerland's new prospectus regime: a guide

Homburger lawyers René Bösch, Benjamin Leisinger and Pierina Janett-Seiler summarise the new Swiss prospectus regime, with a special focus on exchange offers and consent solicitations

1 MINUTE READ

The new prospectus regime in force in Switzerland since January 1 2020 also applies to exchange offers addressed to investors in Switzerland. While the new regime provides for a new general ex-ante approval requirement for prospectuses, there are numerous statutory exemptions available that may be relied upon to avoid a Swiss prospectus and/or Swiss prospectus approval requirement. Depending on the specific circumstances, some of the exemptions are more practical than others. If investors, or certain investors, in Switzerland shall be excluded from the exchange offer, recommended selling restrictions are available for use in the exchange offer documents.

Initiated by the Covid-19 pandemic and the financial consequences on many issuers, consent solicitation exercises and/or exchange offers have become more frequent across the world. Switzerland remains the world's largest wealth management centre for international assets. It is, therefore, no surprise that consent solicitation exercises, *e.g.*, in advance of bondholder meetings, or exchange offers are also extended to Switzerland or Swiss investors, respectively. In light of this, the authors take the opportunity to highlight Switzerland's new prospectus regime and the impact on exchange offers in particular.

The new Swiss prospectus regime

On January 1 2020, the new Swiss Financial Services Act (the FinSA) and its implementing ordinance, the Financial Services Ordinance (the FinSO), entered into effect. The FinSA encompasses a new modernised prospectus regime for the Swiss capital markets. With certain customisations for debt and equity instruments as well as collective investment schemes, derivatives and structured products, the new Swiss prospectus regime is designed to apply uniformly to all financial instruments. The new regime came into effect on January 1 2020, whereby certain elements of the new regime apply with immediate effect; others only after certain transition periods.

New *ex-ante* approval requirement

Under the new prospectus regime, the FinSA and the FinSO require that, in principle, any prospectus be approved prior to (i) a *public offering of securities* in Switzerland, and/or (ii) the *admission to trading of securities* on a trading venue (exchange or multilateral trading facility) in Switzerland. The approval must be obtained from a so-called 'reviewing body' (sometimes also referred to as a review office), a new authority licensed and supervised by the Swiss Financial

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Market Supervisory Authority FINMA (FINMA). As a primer in the Swiss regime, the term public offering includes both public primary and public secondary offerings, as well as combinations of the two.

The prospectus approval requirement will only apply following a transition period expiring six months after FINMA has licensed the first reviewing body, but no earlier than October 1 2020. Per June 1 2020, FINMA has issued respective licenses to SIX Exchange Regulation (affiliated with SIX Swiss Exchange) and Regservices (affiliated with BX Swiss). Accordingly, the transition period expires on December 1 2020.

The notion of a public offering

The FinSA and FinSO define a public offering as any communication to an unlimited number of persons in Switzerland that (i) contains sufficient information on the terms of the offer and the financial instrument itself and (ii) is customarily intended to draw attention to a certain financial instrument and to sell it. The FinSA only regulates the offer to investors to acquire a financial instrument; it does not subject cash tender offers, *i.e.*, the offer to existing holders to sell a financial instrument to the issuer or tender agent, to a Swiss prospectus requirement. Consent solicitation exercises without any elements of exchange and/or further investments by Swiss investors do not trigger a prospectus requirement under the FinSA, either.

However, issuers often combine consent solicitations, where the mere consent to change certain terms of existing securities is requested, with exchange offers. In exchange offers, existing investors also have an opportunity to invest in, or otherwise receive in exchange, other securities from the same issuer or any of its affiliates. In such a case, it has to be carefully analysed whether an investment decision is made by the investors or not. If this were the case, a Swiss prospectus requirement is triggered unless (i) the exchange offer qualifies as a mere private placement in Switzerland or, alternatively, (ii) an exemption from the prospectus requirement under the FinSA applies.

A private placement consists of a communication to a limited number of (potential) investors in Switzerland that are also approached by means typical for such private placements. If, for example, an issuer knows, or has a list of, the Swiss investors who hold its securities and sends a communication exclusively to them to inform them about the exchange offer, no public offering exists in our view. In contrast, if the securities are freely tradeable (*e.g.*, because of their listing on the SIX Swiss Exchange or BX Swiss) and the issuer only sends the exchange offer information to the investors via the financial information systems (*e.g.*, via SIX SIS), a public offer would be deemed to take place.

Exemptions from the prospectus requirement

Even if a public offering takes place or is envisaged in Switzerland, the FinSA provides for a set of explicit exemptions from the prospectus requirements, which are, to a large extent, modelled along the EU Prospectus Regulation as well as the previous practice and regulations of the SIX Swiss Exchange.

The exemptions can be divided into three categories, namely (i) exemptions based on the type of the offering, (ii) exemptions based on the type of the security and (iii) exemptions in connection with admission to trading. In connection with exchange offers, the exemptions based on the type of the offering and those based on the type of the security are of specific relevance.

Exemptions based on the type of the offering

Exempt from the prospectus requirement are public offerings (i) addressed solely to professional clients within the meaning of the FinSA (*e.g.*, banks, asset managers, insurance companies, other entities under prudential supervision, enterprises and investment structures for high net worth individuals in each case featuring a professional treasury unit, or large corporates), (ii) addressed to less than 500 prospective retail investors (private clients) in Switzerland, (iii) with a minimum investment amount of CHF 100,000 (approximately $103,500) or the equivalent in a foreign currency, (iv) of securities with a minimum denomination of CHF 100,000 or the equivalent in a foreign currency, or (v) of securities that account for an aggregate investment amount not exceeding CHF 8 million over a 12-month period.

In the context of exchange offers and the reliance on the exemption of public offers to up to 500 retail investors in Switzerland, it should be noted that the analysis must be done on a look-through basis. This means that an exchange offer, *e.g.,* to 20 private banks in Switzerland, could in reality be addressed to several thousand retail investors in Switzerland who hold the respective securities in their securities accounts with such private banks. Such ultimate holders are the investors relevant for the exemption. It may prove difficult in practice to establish the real number of retail holders of the securities in Switzerland. In such cases, a reliance on another exemption, *e.g.*, by requiring minimum exchange tenders of CHF 100,000 per investor for eligible participants, is advisable.

Exemptions based on the type of the security

Further exempt from the Swiss prospectus requirement are public offerings in Switzerland of certain types of securities, including (i) equity securities issued outside the scope of a capital increase in exchange for previously issued equity securities of the same class (*e.g.*, in connection with a share split), (ii) equity securities exchanged for securities of the same issuer or any of its affiliates, (iii) equity securities delivered as a result of a conversion of debt instruments of the same issuer or any of its affiliates, (iv) securities tendered in a public takeover, if the relevant disclosure is equivalent to a Swiss prospectus, or (v) securities offered within the framework of a merger, spinoff or transfer of assets, if the disclosure is equivalent to a prospectus.

Automatic approval of certain foreign prospectuses

If there is a prospectus requirement and no exemption applies under the FinSA, a noteworthy novelty of the new Swiss prospectus regime is the automatic approval of certain foreign prospectuses. If a prospectus has already been approved in accordance with the standards of certain recognised foreign jurisdictions set forth on the Swiss reviewing body's list, the requirement to have the prospectus reviewed and approved by a reviewing body may instead be met simply by filing the prospectus with a reviewing body and by publishing it.

Exemptions from *ex-ante* approval requirement

In order to guarantee that the Swiss bond market will retain its advantageous and historical short time to market, FinSA introduced an exemption from the *ex-ante* approval requirement for certain securities specified in the implementing ordinance. The FinSO names straight bonds, convertible and exchangeable bonds, bonds with warrants attached, mandatory convertible notes, contingent convertible notes (CoCos) and write-down bonds as well as structured products with a duration of 30 or more days as covered by the exemption, to the extent certain conditions are met. Such conditions include, most importantly, the requirement that a Swiss bank or securities firm issues a confirmation to the issuer that the most important information about the issuer (and, in the case of guaranteed debt securities, the guarantor), as well as the most important information about the debt securities, is publicly available at the time the prospectus is published. If an issuer is able to take advantage of this exemption, review and approval of the relevant prospectus by the reviewing body will only take place *ex post* rather than *ex ante*.

Contents of the prospectus

If a FinSA prospectus is prepared, it must be in an official language of Switzerland (German, French or Italian) or in English. The specific content requirements are outlined in the annexes to the FinSO. Although based on the previous practice and regulations of SIX, the FinSO also provides some additional requirements, such as the requirement to include an easily comprehensible summary or the requirement to include a disclaimer if benefiting from an exemption from the *ex ante* approval requirement (see above). In addition, the FinSA now explicitly permits that certain information may be incorporated into the prospectus by reference, provided that such information has been published prior to, or concurrently with, the relevant prospectus.

Basic information document

Whenever financial instruments other than shares, straight bonds or other financial instruments without a derivative character are offered to retail investors (private clients) in Switzerland, the manufacturer of such financial instrument (usually the issuer) has to prepare a so-called basic information document (*Basisinformationsblatt*, also referred to as Swiss KID) containing all information for the investment decision in an easily comprehensible way. This requirement may also be met by a European key information document (KID) under the packaged retail and insurance-linked investment products, or Priips regulation.

Position paper on selling restrictions

If an issuer decides not to extend the exchange offer to Swiss investors, adding certain selling restrictions in the exchange or tender offer memorandum is advisable. The leading Swiss banks and the primary Swiss law firms active in the capital markets have prepared a 'position paper on legends and selling restrictions for cross-border offerings of securities (excluding collective investment schemes and structured products) into Switzerland under the prospectus regime of the Swiss Financial Services Act'. The paper provides for a brief overview of the Swiss prospectus regime, features a checklist for determining prospectus requirements under the FinSA, and sets forth applicable legends and suggested selling restrictions.

ASIA-PACIFIC FINTECH SPECIAL FOCUS 2020 CONTENTS

ASIA-PACIFIC FINTECH SPECIAL FOCUS 2020

JAPAN

Getting a grip

Clear new regulations on cryptoasset derivative transactions and custody services come into force in Japan. Shunsuke Aoki, Ken Kawai and Akihito Miyake of Anderson Mōri & Tomotsune take a look

The regulatory environment in Japan for cryptoasset derivative transactions and cryptoasset custody services has been significantly changed as a result of amendments to the Financial Instruments and Exchange Act (FIEA) and the Payment Services Act (PSA), which came into force on May 1 2020. The changes have impacted foreign business operators engaging in cryptoasset derivative transactions and custody services.

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Cryptoasset derivative services in Japan

Prior to its most recent amendment, the FIEA did not regulate cryptoasset derivative transactions, although Japan was hosting a significant volume of cryptoasset derivative transactions mainly in the form of contracts for difference (CFDs) on margin at Japanese cryptoasset exchanges. To protect users and ensure that only appropriate transactions are conducted, however, the FIEA was amended to regulate cryptoasset derivative transactions by including cryptoassets, along with their prices, interest rates, etc. on the list of assets underlying derivative transactions that are subject to regulation.

The FIEA uses "derivative transactions" as a general term to encompass market derivative transactions, over-the-counter (OTC) derivative transactions and foreign market derivative transactions. Each of these is then further classified into sub-categories (such as futures transactions, CFD transactions, option transactions and swap transactions) with references to either "financial instrument" or "financial indicator".

As a consequence of the inclusion of "cryptoassets" and standardised instruments of cryptoassets created by financial instruments exchanges within the definition of "financial instruments", and the inclusion of cryptoasset prices, interest rates, etc. within the definition of the "financial indicators", respectively, cryptoasset derivative transactions will now be

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Ken Kawai has extensive experience advising financial institutions, fintech start-ups, investors and corporate clients on complex finance and financial regulatory matters. Ken focuses primarily on the fintech industry, and regularly advises fintech companies, financial institutions, international organisations and industry organisations on legal issues surrounding fintech, including the complex legal framework governing cryptocurrencies, and blockchain. Ken also specialises in derivatives, and has counselled global banks, broker-dealers and investors on regulatory matters and best practices in respect of derivatives and related products. He derives his deep and practical knowledge in this area from his 17 year career at MUFG Bank, where he was involved in derivatives trading and marketing. Ken's practice also involves cyber-security for financial institutions, personal data protection and e-commerce.

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Akihito Miyake covers a wide range of financial regulatory matters. He especially focuses on all aspects of legal issues related to the asset management businesses. He has significant experience providing legal services and advice in relation to the formation, offering and distribution of various types of investment funds both inside and outside Japan; the registration of asset managers and distributors acting in Japan; the operations of financial instruments businesses regulated in Japan; business deployment in the Japanese market; inbound investments by foreign asset managers; and outbound investments by domestic investors. His recent experience also encompasses support in various crypto-related projects such as formation of cryptoasset investment funds and security token offering platforms and advice on cryptocurrency copy trading services.

subject to the provisions of the FIEA, regardless of the type of derivative transaction involved. Derivative transactions involving the exchange of cryptoassets for other cryptoassets will also covered by the FIEA.

Regulatory requirements and exemptions differ depending on the type of derivative transaction in question. In this connection, the Financial Services Agency (FSA) published a statement – in response to public comments regarding amendments to subordinate legislation in respect of the FIEA and PSA – to the effect that the provision of a trading platform with an order book indicating buy and sell orders of cryptoasset derivative transactions would be deemed "OTC cryptoassets derivative transactions", as defined in the FIEA, unless the trading platform is operated by a financial instruments exchange licensed under the FIEA or an overseas counterpart.

Based on this statement, it is generally believed that most cryptoasset derivative transactions conducted in Japan (or involving Japanese residents) will likely be deemed OTC cryptoasset derivative transactions.

Foreign cryptoasset derivative businesses

Handling OTC cryptoasset derivative transactions or acting as an intermediary, broker or agent in relation such transactions constitutes a Type I financial instruments business (Type I business), as defined by the FIEA. Accordingly, a company engaging in such transactions will have to register as a Type I financial instruments business operator (Type I operator).

Any entity looking to be a financial instruments business operator and to engage in the Type I business must establish a domestic sales or business office and meet certain asset requirements, including having a stated capital of at least JPY50 million approximately ($466,000); net assets of at least JPY50 million; and a capital-to-risk ratio of at least 120%.

Notwithstanding the above, a foreign cryptoasset derivative business operator that is permitted to conduct OTC cryptoasset derivatives transactions under the laws and regulations of its home jurisdiction is exempt from such registration requirements if it conducts such transactions with certain professional entities in Japan, including and limited to:

1. The Japanese government or the Bank of Japan.
2. Financial instruments business operators and financial institutions that engage in OTC cryptoasset derivative transactions in the course of their business.
3. Financial institutions, domestic trust companies (excluding domestic custodial trust companies) or foreign trust companies (excluding foreign custodial trust companies), provided that they conduct OTC cryptoasset derivative transactions for investment purposes or for the account of trustors under trust agreements.
4. Financial instruments business operators that engage in investment management business, provided that such entities conduct activities relating to investment management business.

It is noteworthy that no conventional exemption for non-securities related derivative transactions provided to certain professional customers (including qualified institutional investors and companies with capital amounts of JPY1 billion or more) is available under the FIEA to OTC cryptoasset derivative transactions, in light of the high-risk nature of these transactions.

Although OTC cryptoasset derivative transactions may include the physical exchange or delivery of cryptoassets, this physical exchange or delivery of cryptoassets is exempt from the regulations applicable to cryptoasset exchange services under the PSA, unless they involve the management of customers' cryptoassets, as explained in more detail below (Cryptoasset custody services).

Rules of conduct

Under the FIEA, financial instruments business operators that provide customers with OTC derivative transactions are subject to various rules of conduct.

Loss-cutting rules generally refer to a mechanism through which an open position will be compulsorily liquidated by an offsetting transaction to prevent any further losses, if the appraised loss reaches a certain level. The Cabinet Office Order on Financial Instruments Business, etc. (Cabinet Office Order) imposes an obligation on financial instruments business operators to establish and observe loss-cutting rules in connection with their OTC cryptoasset derivative transactions with individual customers.

Leverage regulations generally mean regulations obligating business operators to require their customers to deposit margin exceeding a certain ratio of the transaction amount (i.e., the notional principal). If a financial instrument business operator engages in cryptoasset derivative transactions, it will be prohibited from entering into transactions with customers without requiring their customers to deposit the necessary amount of margin; and continuing in transactions with customers without requiring their customers to deposit margin to make up any shortfall in the required deposit, at a certain time every business day.

The amount of margin required to be deposited by a customer differs depending on whether the customer is an individual or a corporation. Customers that are individuals are required to deposit a margin equivalent to 50% of the value of the customers' cryptoasset derivative transactions (i.e., a leverage ratio of up to two times). Corporate customers, on the other hand, are required to deposit a margin equivalent to the value of the customers' cryptoasset derivative transactions, multiplied by either (a) 50% or (b) the cryptoasset risk assumption ratio, as calculated using historical volatilities specified in the public notice of the FSA's commissioner.

These leverage regulations will come into force on May 1 2021. It should be noted, however, that the rules of the Japan Virtual and Cryptoassets Exchange Association (JVCEA), which are in effect, limit leverage ratio to no more than four times; except that a Type I operator may choose to use the aforementioned cryptoasset risk assumption ratio.

The JVCEA is a self-regulatory association certified by the FSA in respect of both cryptoasset exchange services and cryptoasset derivative transactions. Although a Type I operator is not obliged to join the JVCEA, it is generally understood that the rules of the JVCEA are virtually applicable to and binding on all Type I operators. This is because the FSA, in practice, requires all Type I operators to establish internal controls that are comparable to those required under the rules of the JVCEA.

The FIEA also imposes the obligation on a financial instruments business operator to entrust its customers' funds to a trust company or a trust bank to ensure that such funds are refundable to customers, even in the event of the insolvency of the operator.

Countering risk

Type I operators are required to calculate their capital-to-risk ratio, and to report such ratio at the end of every month to the FSA or relevant local finance bureau, as well as when such ratio falls below 140%. Type I operators whose capital-to-risk ratio falls below 120% will be subject to a business improvement order. Where their capital-to-risk ratio falls below 100%, they will be subject to an order for suspension of business or rescission of registration.

For this purpose, the capital-to-risk ratio means the percentage derived by dividing the total value of a business operator's stated capital, reserve fund and other items as prescribed in the Cabinet Officer Order – after deducing the total value of its fixed assets and other items as prescribed in the Cabinet Office Order – by the total value of its market risk, counterparty risk and basic risk. The specific method of calculating a business operator's capital-to-risk ratio is prescribed in the relevant public notice.

The value of a business operator's market risk is calculated by either a standardised approach or an internal control model. Under the standardised approach, a business operator's market risk is calculated by the aggregation of values equivalent to equity risk, interest rate risk, foreign currency risk, commodity risk and cryptoasset risk. The value of cryptoasset risk in turn is calculated under the assumption that the market risk of cryptoassets and cryptoasset derivative transactions holds a risk weightage of 100%. Under the internal control model, on the other hand, the value of a business operator's market risk is calculable using value-at-risk, with the FSA commissioner's approval.

The value of counterparty risk is equal to the aggregate exposure of a business operator to its counterparties (less the collaterals received), multiplied by a certain risk weightage as specified in the relevant public notice. The risk weightage for transactions relating to cryptoassets falls within the category with the highest percentages.

Type I operators that hold cryptoassets will have to include within the value of their basic risk the total market value of its cryptoassets that are not managed with cold wallets or other equivalent means.

Additionally, a Type I operator that deposits cryptoassets with a third party will assume credit risk vis-à-vis such third party in relation to the right to claim the return of such crypto assets. Furthermore, if the third party does not manage, or if it is indeterminable whether such third party is managing the deposited cryptoassets with cold wallets or other equivalent means, the Type I operator will be required to take the deposited cryptoassets into account when calculating the value of its counterparty risk and basic risk, respectively.

Cryptoasset custody services

Before the PSA's amendment, it was generally understood that the mere management of users' cryptoasset and the transfer of such cryptoassets to an address designated by users does not meet the PSA's definition of a cryptoasset exchange service. This is because the PSA had previously only provided that the management of users' funds or cryptoasset in connection with the sale or purchase of a cryptoasset or the exchange of a crypto asset for another crypto asset; or any intermediary, brokerage or agency service, constitute provision of a cryptoasset exchange service.

To address concerns that cryptoasset custody services share common risks with existing cryptoasset exchange services, including risks associated with leakage of users' cryptoassets, bankruptcy of service providers, and money-laundering and terrorism-financing, the amended PSA now designates the "management of cryptoassets for the benefit of another person" (cryptoasset custody services) as an additional type of cryptoasset exchange service. Consequently, managing cryptoassets, regardless of whether any sale and purchase is involved, now constitutes provision of cryptoasset exchange service. A person engaging in a cryptoasset custody service will have to register as a cryptoasset exchange service provider (CAESP). It should be noted that there is no professional investor exemption for this registration requirement under the PSA.

In this context, the Revised Guidelines on Crypto Asset explains what constitutes the management of cryptoassets for the benefit of another person: "although whether a service constitutes management of cryptoassets should be determined based on the actual circumstances, a service will constitute the management of cryptoassets if the service provider is in a position in which it may transfer its users' cryptoassets (such as, for example, if the service provider owns a private key with which it may transfer its users' cryptoassets solely or jointly with its related parties, without the users' involvement)."

Accordingly, it is understood that if a service provider merely provides its users with a cryptoasset wallet application (i.e., a non-custodial wallet) and the users manage private keys by themselves, this service would not constitute a cryptoasset custody service. On the other hand, if the provider of a trading platform for cryptoasset derivative transactions accept deposits of users' cryptoassets as margins in a wallet managed by it, it would constitute the provision of a cryptoasset custody service.

A CAESP must not only meet requirements relating to the assets, personnel, corporate organisation and establishment of internal regulations, but also manage customers' funds separately from its own, and entrust customers' funds to a trust company or any other similar entity. A CAESP must also manage its customers' cryptoassets (the entrusted cryptoassets) separately from its own cryptoassets. Furthermore, a CAESP must manage 95% or more of the value of its total entrusted cryptoassets with fully-offline wallets or by other technical means that have the equivalent safety levels of fully-offline wallets.

ASIA-PACIFIC FINTECH SPECIAL FOCUS 2020
JAPAN

New beginning

Japan's One-Stop Financial Service Intermediary and New Regulatory Framework for Payment Services, by Akihito Miyake, Ken Kawai and Shunsuke Aoki of Anderson Mōri & Tomotsune

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The rapid development of information and communication technologies in recent years has enabled entrepreneurs to create and offer innovative services to the financial industry. In particular, there has been a growing need for one-stop online platforms enabling access to financial services of various kinds. There has also been a rise in demand for convenient cashless payment services. Against this backdrop, since November 2017 the Financial Services Agency (FSA), Japan's financial regulator, has been looking to refine the financial regulatory framework with the aim of enhancing user convenience and safety.

After extended discussions, the FSA eventually submitted a bill to the Diet on March 6 2020. The bill is designed, among other things, to introduce a new category of business termed a "financial service intermediary", and to refine the existing regulatory framework for payment services. The bill was passed by the Diet on June 5 2020.

Introducing the One-Stop Financial Service Intermediary

Among the online platforms that have experienced increasing demand are mobile apps that enable users to check their bank accounts and apps that recommend suitable financial services (such as loans, securities investments and/or insurance products) to users based on their financial situation, income and expenditure and personal needs.

Under the financial regulatory regime in Japan, service providers offering mobile apps of this kind are regarded as "intermediaries" for banks, securities firms, investment advisers/managers and/or insurance companies. Such intermediaries are required to be licensed or registered separately under vertically segmented legislation, including the Banking Act, the Financial Instruments and Exchange Act and the Insurance Business Act. These pieces of legislation subject service providers to the instructions and

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supervisory oversight of the banks, securities firms, investment advisers/managers and/or insurance companies to which such service providers act as intermediaries. This makes it difficult for these service providers to introduce a wide range of financial services, and this in turn limits their ability to promote greater user convenience.

To resolve this issue, the bill introduces a new category of business called the "financial service intermediary". Under the bill, financial service intermediaries will be permitted to recommend deposit, money transfer, loan, securities investment and/or insurance products to users or to intermediate between such users and the relevant financial service providers.

Specifically, the bill enables a financial service intermediary to do this through a single registration as a financial service intermediary under the new Act on Offer of Financial Services (New Act), renamed from the existing Act on Sale of Financial Instruments. The New Act will not require a financial service intermediary to be tied to any specific financial service provider. This will enable financial service intermediaries to offer a wide range of financial services as a one-stop shop. Furthermore, the New Act will enable financial service intermediaries that meet certain conditions to send remittance orders to banks for and on behalf of users and/or provide bank account information to users through electronic means upon user request. Qualifying financial service intermediaries can do so by filing a simple notification with the FSA under the New Act, without having to undergo registration as an electronic settlement agent under the Banking Act.

As financial service intermediaries will not be tied to or subject to the supervision of any specific financial service providers, these intermediaries may not offer financial services as an "agent" of any financial service provider, but will instead be required to hold sufficient security deposits to meet the needs of its own intermediary business. Additionally, a financial service intermediary will not be permitted to accept users' money for and on behalf of any financial service provider. Furthermore, the scope of financial services that a financial service intermediary may recommend to users are limited to those that do not require advanced explanation.

The scope of this limitation is still uncertain at present and will be clarified through subordinate regulation to be subsequently published. It is generally understood, however, that the limitation prohibits financial service intermediaries from recommending complex financial products and services, such as structured or foreign currency-denominated deposits; unlisted stocks, bonds issued by unlisted companies, derivatives or margin trading services; or variable or foreign currency-denominated insurance policies/annuities. Instead, it is generally understood that financial service intermediaries will be allowed to recommend simple financial products and services, such as saving accounts; fixed-term deposits, housing loans, credit card loans and money transfer services; government and local bonds, listed stocks, bonds issued by listed companies, units/shares in investment trusts/corporations and ETFs; and non-variable life and non-life insurance products.

As a financial service intermediary may deal with a wide range of financial services, it will have to comply with certain codes of conduct stipulated under the applicable legislation, such as the Banking Act, the Financial Instruments and Exchange Act, the Insurance Business Act and/or the Money Lending Business Act. As it is a common requirement globally for financial service intermediaries to disclose to users, upon request, the fees and reimbursements they will receive from those financial service providers for which they act as intermediaries, the New Act will impose a similar code of conduct on financial service intermediaries in Japan. The New Act will also require financial service intermediaries to provide users with an explanation of key matters and to properly handle users' information.

The New Act is also expected to establish a certified self-regulatory organisation for financial service intermediaries, although it will not be mandatory for financial service intermediaries to be members of this organisation.

The New Act and related amendments to other legislations will take effect within one and half years following the New Act's promulgation.

A new payment services framework

The existing Payment Services Act (PSA) contemplates a category of businesses called the money transfer business operator. Such business operators are registered under the PSA and are permitted to provide users with money transfer services for up to JPY1 million (approximately $9,000) per transfer.

Service providers wishing to provide users with money transfer services for amounts over JPY1 million per transaction are required to be licensed as a bank under the Banking Act or as a depository institution other than a bank under the relevant legislation. The licensing requirements applicable to bank or depository institutions, however, are extremely stringent. For example, banks are required to have capital of at least JPY2 billion, unlike money transfer business operators, which are not subject to any minimum capital requirements. Nevertheless, money transfer business operators are required to maintain security deposits of an amount that is at least equivalent to the higher of JPY10 million or 100% of their unsettled financial exposure plus enforcement costs.

Moreover, the existing regulatory framework in respect of money transfer business has become too rigid and out-of-date to encourage a greater use of cashless payments. For example, service providers wishing to provide high-value money transfer services without providing other traditional banking services, such as loans, are required to obtain full banking licenses. Meanwhile, those providing money transfer services in respect of only small amounts of up to tens of thousands of yen are required to comply with all the requirements applicable to money transfer business operators that contemplate money transfers of up to JPY1 million per transaction. Accordingly, the amended PSA has refined the regulatory framework surrounding money transfer business operators to group them into the three categories (discussed below), to take into account the amount of funds contemplated in their money transfer businesses.

The first category is the "Type 1 money transfer business operator" (Type 1 Operator). Business operators in this category may provide users with money transfer services without a limit on the amount of money transferred. These business operators will have to submit a business implementation plan to the FSA to obtain FSA approval for the business. Further, as accepting and retaining deposits is generally prohibited, Type 1 Operators can only receive funds from a user when it has specific remittance instructions from the user; the business operators must then immediately transfer the relevant funds in accordance with the user's instructions. Type 1 Operators will also have to engage in the money transfer business in accordance with the business implementation plan approved by the FSA.

The second category is the "Type 2 money transfer business operator" (Type 2 Operator). Business operators in this category will be subject to largely the same regulatory framework as that applicable to existing money transfer business operators. What this means is that such business operators may transfer a user's funds up to the limit of JPY1 million per transaction. However, Type 2 Operators will additionally be required, under the amended PSA, to ensure that they do not receive or retain any user funds that are unlikely to be transferred. It is expected that Type 2 Operators will be required to return such user funds.

The third category is the "Type 3 money transfer business operator" (Type 3 Operator). These business operators may provide money transfer services in respect of small amounts only. The applicable limit will be prescribed in the relevant subordinate regulation, to be subsequently published. However, it is generally expected that Type 3 Operators will be able to transfer up to tens of thousands of Japanese yen per transaction, per user. Accordingly, Type 3 Operators are expected to be prohibited from accepting and retaining user funds exceeding the applicable limit.

Rules of conduct

As noted above, money transfer business operators are required under the current PSA to maintain security deposits. These security deposits can be made in any of the following three ways: making a cash deposit with an official depository; entering into a security deposit agreement with a designated bank or insurance company; or entering into a trust agreement with a trust bank or company.

However, the existing PSA does not allow the concurrent use of these three methods. There is also a time lag of up to one week between the date on which the amount of the security deposit is calculated and the date on which the security deposit is adjusted. Additionally, security deposits maintained using the first two options above are calculated on a weekly basis, while security deposit amounts maintained using the third option are calculated on a business daily basis.

In response to these issues, the amended PSA permits the concurrent use of all three options. Furthermore, the amended PSA unifies the frequency of calculation of the security deposit to more than once a week and shortens the one-week time lag mentioned above. As a result, Type 1 Operators will be required to make cash deposits, calculated on a business daily basis, to an official depository within the prescribed period stated in the relevant subordinate regulations to be published (which will perhaps be two business days). Type 2 or 3 Operators will be required to make regular cash deposits that are calculated periodically, at least once a week, within one week of calculation at the latest. In each case, it will not be necessary to make cash deposits with an official depository in respect of the amounts under the second or third option.

Furthermore, the amended PSA permits a Type 3 Operator to maintain security deposits in a less cumbersome manner. Specifically, cash deposits can be deposited with a segregated bank account maintained by the Type 3 Operator itself, on the condition that the operator undergoes an audit by a certified public accountant or audit firm. This new framework will not only enhance user protection but also make money transfer business operators easier to use.

The amended PSA also clarifies the definition of “money transfer”. Under the definition, service providers offering a split-the-bill mobile app for the use of individuals will be regulated as money transfer business operators, while service providers receiving proceeds on behalf of their business clients and escrow service providers will likely remain unregulated.

In view of this, it will be essential under the amended PSA to examine the nature of each and every service to determine whether it is subject to the regulations applicable to money transfer business operators.

The amended PSA will take effect within a year of its promulgation.

ASIA-PACIFIC FINTECH SPECIAL FOCUS 2020

ASIA-PACIFIC

What lies ahead

Grace Fung and Karen Man of Baker McKenzie discuss how regulations across Asia-Pacific are shaping the digital transformation of the financial services industry

Technology is driving an evolution in the global financial ecosystem that is affecting every participant, from end-user to financial institution and regulator, across different sectors and different continents. The financial system was once connected through intermediaries and exchanges, but digital transformation is changing that and may even displace those traditional roles.

A few important drivers have catalysed the speed and demand for digital transformation. In particular, the Covid-19 pandemic has provided a significant impetus for being online; it is now the new norm.

This digital journey highlights competing priorities for regulators which include supporting or increasing competition, strengthening financial stability, maintaining financial integrity and ensuring protection for investors, as detailed in the IMF Policy Paper "Fintech: The experience so far" (June 2019). Innovation creates opportunities, but also new threats. Regulators have been actively and increasingly working together to formulate new policies, laws and regulations to provide an open environment which encourages growth at the same time as facilitating financial system stability and protecting the public interest.

Digital marketing and data

In APAC, technology giants operating e-commerce platforms and social media and messaging systems are reshaping various financial sectors, including digital payments, loans, banking, and wealth and asset management. Globally, there is a trend of increasing consolidation, with a growth in M&A transactions targeting competing social media and messaging giants. Why?

Data is one of the most precious assets in this new age. Through sophisticated analytics, artificial intelligence (AI) and application programming interfaces (API), data – particularly user patterns and behaviours – can enhance

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Grace regularly advises financial institutions on structuring new products/ services, compliance with regulatory changes, and handling inspections and investigations. Grace is also active in the fintech space.

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financial services, add new features and create new service offerings. However, digital marketing across sectors and jurisdictions gives rise to important legal and regulatory considerations.

Marketing regulated financial products and services could be subject to local licensing and authorisation requirements. Many securities and banking regulations in APAC have extra-territorial effect. For example, in Hong Kong SAR (Hong Kong), product offering restrictions and licensing requirements under the Securities and Futures Ordinance (SFO) could apply to onshore and offshore marketing targeted at Hong Kong SAR clients or investors. Australia has recently implemented a revised licensing arrangement that is specifically directed at offshore financial services providers under the updated Regulatory Guide 176 (RG 176), issued by the Australian Securities and Investments Commission (ASIC).

Cross-border data transfer and data protection for individuals continues to require jurisdiction-specific analysis. Regulators have increasingly emphasised ethical accountability for the collection and the use of personal data and encouraged the adoption of privacy-by-design and privacy-by-default when developing fintech initiatives. The Hong Kong Monetary Authority (HKMA) has been actively working with banking industry associations and the Hong Kong SAR Privacy Commissioner for Personal Data (PCPD) to give more guidance on the proper use of personal data in the online environment. The PCPD has issued specific guidance related to big data, AI and fintech with recommended frameworks and practices. The PCPD is also undertaking a formal review of amendments to the Hong Kong SAR data privacy legislation to align with global standards.

Data privacy and security regulators are becoming more aggressive and tougher on businesses with poor data protection practices. They continue to adopt more expansive data breach notification requirements and impose direct regulation on data processors. We expect higher penalties will apply for non-compliance moving forward.

Another key consideration is API data protection. APAC is keeping pace with global trends, epitomised by the EU's Payment Service Directives. In September 2017, the HKMA announced the open API framework as one of the seven initiatives to prepare Hong Kong SAR for a new era of smart banking. The framework contemplates four phases, with the second phase starting at the end of 2019. The HKMA provided further guidance on sound consumer protection practices last year, focusing on areas including on-boarding checks and on-going monitoring of third party service providers, setting up clear liability and settlement arrangements with partnering service providers to compensate for client loss, and implementing complaint handling and redress mechanisms. In Australia, the Consumer Data Right (CDR) legislation is scheduled to take effect in certain aspects of banking in July 2020.

Finally, the use of AI in financial services is gathering greater focus and is being supported by regulators in APAC. AI offers both improved efficiency and accuracy in areas ranging from client-facing services to internal processes, risk management and potentially regulatory reporting. However, regulators also recognise the potential risks. In November 2019, the Monetary Authority of Singapore (MAS) announced a partnership with the financial industry to create a responsible AI and data analytics (AIDA) adoption framework, referred to as the Veritas project, as part of a national AI strategy. Its aim is to enable financial institutions to evaluate AIDA solutions against key principles of fairness, ethics, accountability and transparency.

In November 2019, the HKMA issued two circulars to the industry on high-level risk management principles on the use of AI and the related consumer protection issues. The high-level principles addressed the four key themes of governance and accountability, fairness, transparency and disclosure and data privacy and protection.

The regulatory fragmentation in APAC means that solutions for one jurisdiction are not always transportable to another. Interoperability between APAC jurisdictions is needed to enable the financial services industry and consumers to take full advantage of opportunities. The participation by 17 regulators, including the UK's Financial Conduct Authority, the HKMA, Hong Kong Securities and Futures Commission (SFC), Singapore's MAS and Australia's ASIC in the Global Financial Innovation Network (GFIN) 2019 Cross Border Testing Pilot, demonstrates the willingness of regulators to collectively consider how to streamline and address these problems globally.

On-boarding and KYC

Anti-money laundering (AML) and countering the financing of terrorism (CFT) remain a global focus. Technology represents a source of risk but also offers means of a radar and shield, through tools that can help track and mitigate AML risks. Business transactions and money flowing across different jurisdictions via sophisticated multi-layer technology systems and increasing non-face-to-face transactions have heightened the risks of crimes. This makes the identification and management of AML risks more complex. Specifically, as reported by the Financial Action Task Force (FATF), money laundering and fraud risk relating to Covid-19 has increased. The reasons include the increased number of online transactions, as well as increases in phishing attacks, business email compromise scams and ransomware attacks.

In APAC, regulators are generally open to innovative approaches in electronic-KYC (eKYC), as long as the corresponding risks can be managed and mitigated. This can be achieved through tools including artificial neural networks (ANN) and other AI technologies and data analytics.

APAC regulators are continuing to apply a risk-based approach for AML assessment and the same applies to remote client on-boarding. For example, in Hong Kong SAR, when the SFC revised its AML regulatory guidelines in 2018, it indicated that it did not intend to prescribe specific examples of the types of new and developing technologies that would be suitable, thereby allowing future flexibility. The HKMA has a similar approach under its Supervisory Policy Manual AML-1.

In addition to general AML requirements, it is not uncommon for financial regulators to impose specific requirements for regulated products and services. For example, in Hong Kong SAR, the SFC has imposed additional requirements under the SFC code of conduct on financial intermediaries conducting non-face-to-face client on-boarding. Singapore's MAS recently published AML guidelines applicable to digital payment token services and specified payment services.

APAC governments have taken active steps to digitise identification information of residents and citizens. For example, in Singapore, the MAS, the Smart National Digital Government Office (SNDGO) and the Government Technology Office are developing the National Digital Identity Platform, which will enable digital document execution along with proving identity. Part of this is already possible using the MyInfo personal service. Financial institutions relying on MyInfo do not need to obtain additional identification documents to verify a client's identity and users are relieved of the burden of filling forms repeatedly. Like any database holding personal information, there are important security questions that arise regarding access to these central databases and protection and security of their data.

The use of electronic signatures (e-signatures) enables clients to execute and return documentation without the need to meet physically. E-signatures can be used in multiple APAC jurisdictions but their recognition as a legally valid form of execution has to be considered on a case-by-case basis, and depends on the nature of the subject documentation.

In Hong Kong SAR, the formation of contracts by means of electronic records and the use of e-signatures are governed by the Electronic Transactions Ordinance. Such use is generally recognised except for certain categories of documents, such as the creation and revocation of a trust or power of attorney. In Japan, e-signatures are recognised as a method of entering into agreements as well as satisfying the conditions for the presumption of legal authenticity. However, if the validity of the contract is contested, the authenticity of the signature must still be proven in court. Proper risk controls and authentication measures still need to be implemented to mitigate against the risks of fraudulent or unenforceable use of e-signatures.

Digitalising products and services

The APAC region continues to see transformations in businesses across many financial areas including virtual banks, robo-advisers and virtual assets related businesses.

For players who wish to enter into, or expand, in the digital arena, it is important to consider the applicable legal and regulatory requirements.

APAC-based banking regulators have issued new guidelines for the authorisation of virtual banks and similar requirements generally apply as for traditional banks. However, regulators focus more on the additional risks arising from these business models, particularly on how AML risks and technology and cybersecurity risks are addressed and how any outsourcing arrangements are structured and implemented.

The HKMA issued a new virtual banking guideline in 2018, emphasising financial inclusion and sustainability, and allowing non-financial institutions to become a majority shareholder of a bank. The virtual bank licences are for retail banks and the HKMA has granted eight licenses since March 2019 to virtual banks which will launch on a rolling basis in 2020.

Singapore's MAS released the digital banking initiative in 2019, which allows both bank and non-bank players to conduct digital banking businesses. Unlike Hong Kong SAR, there are two types of digital banking licences: full bank and wholesale bank. The focus is on the value proposition, sustainability and contribution to Singapore's status as a financial centre.

In Malaysia, Bank Negara Malaysia has issued an updated Exposure Draft of its proposed Licensing Framework for Digital Banks.

In a lot of APAC jurisdictions there is no separate licensing regime for robo-advisers but there is specific guidance on compliance requirements. In 2019, in Hong Kong SAR, the SFC issued its Guidelines on Online Distribution and Advisory Platforms, which apply to financial intermediaries providing order execution, distribution and/or advisory services in respect of investment products via online platforms. The focus is on proper design of systems, disclosure to clients, risk management, governance, review and monitoring and record keeping. In 2018, in Singapore, the MAS issued its Guidelines on Provision of Digital Advisory Services, which apply to financial institutions offering digital advisory services and focus around the following areas: governance and supervision of algorithms, technology risk management, prevention of money laundering, disclosure of information, and suitability of advice.

The way in which virtual assets businesses are regulated continues to pose difficult questions for regulators globally and they either use existing laws or have implemented new laws. In Australia, ASIC's information sheet on initial coin offerings (ICO) and cryptoassets (INFO 225) was refreshed in May 2019. This provides guidance on how the Corporations Act 2001 may apply to cryptoassets. Under this legislation, persons dealing in financial products must hold an Australian financial services licence. Importantly, ASIC notes that each cryptoasset will need to be assessed on an individual basis, taking into account its specific rights and features.

In Singapore, the MAS has emphasised the need to hone in on the structure and characteristics (including the rights attached to a cryptocurrency or a digital token) to determine if it falls within the category of a capital markets product regulated under Singapore securities regulations. The New Payments Service Act, which came into force in January 2020, regulates digital payment tokens, including bitcoins. Digital payment token dealing and exchange services are also subject to the licensing regime.

In Hong Kong SAR, the SFC applies the licensing arrangements under the current legal regime to any platform operator offering securities (as defined under the SFO) and enables licensing for operators who are willing to offer a single platform for securities products alongside non-securities products. Any such platform operators need to comply with the new licensing criteria and continuing compliance requirements outlined in the SFC's position paper published in November 2019.

Cloud, crypto and DLT

Financial services firms are increasingly using private or public cloud services to access, store, share, use and analyse information – such as client data and transaction patterns – together with other tools including AI and API.

Cloud computing carries numerous risks from rapid cross-border data flow and limited control over data storage locations which create issues around data retention, data security and cross border transfers. APAC data regulators have issued various guidance notes on cloud computing. For example, the Singapore Personal Data Protection Commission included a new chapter 8 in its Advisory Guidelines (Advisory Guidelines) on the Personal Data Protection Act for selected topics, specifically addressing cloud services. While not legally binding, the Advisory Guidelines confirmed that any outsourced cloud provider is required to have reasonable security arrangements to safeguard personal data that it may be processing.

APAC financial regulators are also paying more attention to cloud arrangements. In Hong Kong SAR, the SFC has recently issued a circular on external electronic data storage.

No discussion about cryptocurrency trading is complete without considering the extent to which central banks are considering their own arrangements. In 2018, the Bank for International Settlements identified numerous reasons why central banks may wish to develop digital currencies (CBDC). While providing the general public with an alternative to cash is one reason why a CBDC may be explored, efforts within APAC have tended to be aimed at removing bottle necks in cross-border trade settlement. This is largely because of the view that alternative payment systems already offer the public efficient and cheaper ways to move funds. The payment space continues to see new entrants covering similar services aimed at retail clients and also SMEs.

Distributed ledger technology (DLT) or blockchain, continues to provide interest to regulators, banks and exchanges as they look to increase the speed of settlement and clearing infrastructure and securities registration processes for dematerialised securities.

Project Ubin in Singapore involves the MAS partnering with the Bank of Canada to enable cross-border digital settlements. Similarly, Project Inthanon-Lionrock involves the HKMA partnering with the Bank of Thailand to enable settlement between banks in both jurisdictions. It is likely that development of these sort of arrangements will accelerate, as trade and logistic pipelines seek to return to pre-pandemic levels and normalise throughput.

The Australian Stock Exchange for its part started work on replacing its existing Clearing House Electronic Sub-register System (CHESS) system in 2015 with a plan for using DLT announced in 2016. The Hong Kong SAR Stock Exchange has embarked on a similar project to deal with settlement and clearing on northbound Hong Kong SAR – PRC stock connect transactions. These initiatives are in addition to the 2018 confirmation by the Singapore Exchange (SGX) and the MAS that they had capability to settle tokenised asset transactions across multiple platforms.

Vibrant regulatory regime

The APAC region will continue to demonstrate a vibrant range of offerings as regulators continue their positive engagement with industry participants and seek to enable the development and implementation of new technology and services for consumers. Funding for new digital ventures has shifted from West to East. Existing and emerging players can undertake larger funding rounds to enable them to support continued growth and increase speed to market. Legal and regulatory change in APAC continues at a rapid pace. The fragmented nature of the markets requires advance planning, good guidance and flexibility to achieve success under such a dynamic framework.

ASIA-PACIFIC FINTECH SPECIAL FOCUS 2020

INDIA

New vision – payment intermediary

Rachit Bahl, Rohan Bagai and Arjun Uppal of AZB & Partners review the RBI's new regulatory framework for payment intermediaries, issued in March 2020, and how it fits into India fintech revolution

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Over the last few years, India has witnessed huge disruptions in the fintech landscape. One key trend that has consistently powered this is the emergence of non-bank intermediaries that offer online payment solutions for digital transactions in the e-commerce space. This proliferation of e-commerce intermediaries has propelled the adoption of electronic payments and induced payments ecosystem stakeholders to innovate and provide technologically advanced and new age payment solutions to enable customers to transact seamlessly and help merchants to accept payments in a secure and timely manner. These intermediaries act as a bridge between the merchants of goods and services and the buying customers.

Indian regulators have recognised this trend and have tried to keep pace with the rapidly changing environment by attempting to create a balance between technology and customer expectations.

To safeguard customers' interests and ensure intermediaries facilitate the collection of customer payments and remit those, without undue delay, to the merchants, who have supplied goods and services, the Reserve Bank of India (RBI) introduced the regulatory framework for payment intermediaries (intermediaries) in 2009.

Regulation of intermediaries

Over the years, intermediaries engaged in facilitating collection of customers' electronic payments and onward settlement of those payments to merchants have been governed by the "Directions for opening and operation of Accounts and settlement of payments for electronic payment transactions involving intermediaries" that were issued by the RBI in November 2009 (Intermediary Directions).

The Intermediary Directions were issued under the Payment and Settlement Systems Act, 2007 (Payment Systems Act), which regulates payment systems in India. A

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Rachit has extensively advised several multinational clients on various issues relating to privacy laws in India, setting up payment systems, implementation of electronic payment solutions, functioning of payment intermediaries and nodal bank account operations in India.

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Rohan Bagai has over 12 years of experience advising clients in the fintech, payments and e-commerce space on a host of legal, regulatory and compliance issues. This includes obtaining authorisations from the Reserve Bank of India (RBI) to operate payment systems in India for the issuance of pre-paid payment instruments (PPIs) such as gift cards and e-wallets, the launch of bill payments businesses and the introduction of new-age electronic payment methods such as a unified payment interface (UPI).

Rohan has considerable experience in negotiating contracts with banks and non-banks, card networks, payment aggregators and gateways on various types of payments facilitation arrangements. Rohan has recently advised clients on the proposed Personal Data Protection Bill, 2018, regulations governing online intermediaries, and the directive relating to localisation of payments data.

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payment system is a system that enables payments to be effected between a payer and a beneficiary and includes clearing, payment and/or settlement services. While the Payment Systems Act does not prescribe the scope of a clearing or payment service, a settlement service means settlement of payment instructions and transactions involving payment obligations. Under the Payment Systems Act, an entity that wishes to operate a payment system is required to obtain prior authorisation from the RBI.

The Intermediary Directions, however, provided a special dispensation to intermediaries that freed such bodies of the requirement to obtain an authorisation from the RBI. This was granted because intermediaries facilitate the collection and settlement of funds through an internal account of a bank (nodal account) and are not involved in actual clearing, payment or settlement services for payment obligations between customers and merchants.

With the largescale adoption of digital payments, rapid changes in the payment systems and emergence of numerous players in the payments ecosystem, the RBI, under the "Vision Statement on Payment and Settlement Systems in India: 2019-2021", expressed its intention to revamp the existing regulations for intermediaries and introduce comprehensive guidelines to regulate various facets of payment related activities carried out by payment gateway service providers and payment aggregators.

Towards this objective, the RBI released a discussion paper on the "Guidelines for Payment Gateways and Payment Aggregators" in September 2019, seeking public comments on how the new guidelines should look and the nature of regulatory intervention and prescriptions that would be appropriate for the industry.

Based on the feedback received, and having considered the critical functions performed by intermediaries in the online payments space, the RBI issued the "Guidelines on Regulation of Payment Aggregators and Payment Gateways" (Guidelines) in March 2020. The Guidelines were proposed to come into effect from April 1 2020, however, the RBI has recently deferred it to September 30 2020.

Aggregators versus gateways

Under the Guidelines, the RBI categorises intermediaries into payment aggregators (aggregators) and payment gateways (gateways).

The aggregators are intermediaries that help merchants make available payment methods (for electronic payments) to customers; collect payments from customers; pool funds received from customers towards the amounts due to merchants; and transfer fund to merchants to settle customers' payment obligations.

On the other hand, gateways are intermediaries that provide technology infrastructure to route and facilitate the processing of online payments. They are technology providers that offer support for and integrate routing and processing of electronic payments, for instance by disseminating transaction data. The RBI has created this distinction between intermediaries (under the Guidelines) based on the role that an entity plays in handling funds.

In a nutshell, aggregators are intermediaries that actually handle of funds; and gateways are intermediaries that have no connection to the funds.

Who needs authorisation?

Any non-bank entity that wishes to operate as an aggregator will be required to obtain RBI authorisation to operate a payment system under the Payment Systems Act. However, entities that propose to function as gateways do not require any RBI authorisation.

The Guidelines also govern the operations of existing intermediaries (to the extent that their activities constitute those of an aggregator), as well as e-commerce marketplace entities that perform aggregator functions. They require such entities to obtain an RBI authorisation by June 30 2021. The e-commerce marketplaces that intend to continue their aggregator business also need to separate the marketplace business.

The key conditions that aggregators need to adhere to are:

- Local presence: aggregators must be structured as a company incorporated in India.
- Capitalisation: aggregators must have a minimum net-worth of Indian rupees 15 crores at the time of applying for authorisation, which will need to be increased to Indian rupees 25 crores within 3 financial years and thereafter maintained going-forward.
- Governance: aggregators must be professionally managed and operated. The promoters must satisfy the "fit and proper criteria" prescribed by the RBI. A declaration is also required from the aggregator's directors, with information about proceedings against them.
- Governance: aggregators need to disclose information about merchants' policies, customer grievances, privacy policy and other terms and conditions, on their website or mobile application. They must also have board approved policies for disposal of complaints and dispute resolution mechanisms and timelines for processing refunds.
- Anti-money laundering: aggregators need to adhere to the guidelines relating to know your customer (KYC), anti-money laundering (AML) and combating financing of terrorism (CFT) under the "Know Your Customer (KYC) Directions" issued by the RBI, as well as the provisions of the Prevention of Money Laundering Act, 2002.
- Merchant related compliances: aggregators need to have a board-approved merchant onboarding policy and must perform background and antecedent checks of merchants to ensure that they do not have a *malafide* intention to dupe customers or sell fake, counterfeit or prohibited products. Aggregators must also ensure merchants' infrastructure complies with Payment Card Industry-Data Security Standard (PCI-DSS) and Payment Application-Data Security Standard (PA-DSS). They additionally need to ensure the security and privacy of customer data by merchants, as a part of which merchants have been restricted from storing customer's card details.
- Customer grievances: aggregators need to implement a customer grievance redressal and dispute management framework. Also, aggregators need to designate a nodal officer to handle regulatory and customer grievances.
- Security and risk management: aggregators need to have a board-approved information security policy and also need to put in place a strong risk management system, adequate information and data security infrastructure and systems for prevention and detection of frauds.
- Audits: similar to most payment systems, aggregators also need to conduct an annual system audit and cyber security audit.

Nodal account and escrow account: while intermediaries were required under the Intermediary Directions to maintain a nodal account with a scheduled commercial bank in India, the Guidelines direct non-bank aggregators to operate an escrow account with a scheduled commercial bank (escrow account) to collect, pool and disburse funds to merchants.

Like a nodal account, the escrow account is also highly regulated. The Guidelines prescribe a list of debits and credits that are permitted to and from the escrow account, as well as settlement timelines from the escrow account to merchants. While interest is not payable on the amount held in the escrow account, the aggregator may agree with the bank to transfer a "core portion" of the amount from escrow account to another account, on which interest may be payable.

Tech Recommendations: in addition to the authorisation requirement and the wide-ranging framework for aggregators, the Guidelines lay down certain baseline technology-related recommendations (Tech Recommendations). These include requirements in respect of information security governance, data security standards, security incident reporting, cyber security audits, IT governance, data security in case of outsourcing and measures to be taken in relation to the competency of staff and vendor risk management, amongst other things. Adherence to the Tech Recommendations is mandatory for aggregators and optional for gateways, which may implement them as a matter of good practice.

The path ahead

With the introduction of the Guidelines, the RBI has distinguished intermediaries into two distinct groups: aggregators, which handle funds; and gateways, which are not exposed to funds.

The role that an intermediary intends to perform in collection, processing and settlement of funds, in terms of handling the funds, is the decisive factor behind whether an intermediary is considered an aggregator, which will need an authorisation from RBI, or a gateway, which can benefit of a much more liberal regime. Being directly regulated by the RBI, an aggregator will need to satisfy a substantially higher level of regulatory requirements than a gateway, for whom the adherence to the Tech Recommendations is also optional, i.e. Gateways are not under a mandatory regulatory requirement to adhere to the Tech Recommendations.

A liberalised approach for gateways is a welcome move from the RBI for tech-apps, pure-play tech gateways and IT service providers, none of which touch funds. To operate as a gateway, an intermediary will need to ensure that it does not facilitate the collection of payments from customers, pooling of funds, or settlement of funds to merchants to discharge customers' payment obligations.

As a departure from the Intermediary Directions, any intermediary that handles funds and consequently operates as an aggregator, will need to have a local presence. Through the Guidelines, the RBI has placed an emphasis on customer protection and security and fraud prevention. Aggregators need to put in place effective consumer grievance redressal and dispute management frameworks, and appoint a nodal officer for regulatory and customer grievance handling, among other things.

Besides customer protection, the Guidelines introduce incremental merchant-related obligations. Some of these requirements could be operationally quite burdensome and challenging for aggregators. In today's times, even e-commerce marketplaces do not provide any assurances with respect to the quality of the merchants' products that are sold on their websites; hence expecting aggregators to conduct product-related checks for merchants may not be reasonable. On most occasions, aggregators may not even be aware of the nature of the product for which a payment is being made.

Fate of the Intermediary Directions

The Guidelines do not expressly supersede the Intermediary Directions, as a result of which two divergent schools of thought on the fate of the Intermediary Directions seem to have emerged in the industry.

While the popular view is that the spirit in which Guidelines have been introduced by the RBI is to govern operations of all kinds of intermediaries going-forward, irrespective of whether they handle funds as aggregators or route online transactions using their technological infrastructure, as gateways. The discussion paper on the Guidelines published prior to the issuance of the Guidelines in September 2019 made it clear that the RBI's intent was to revise the existing framework embodied in the Intermediary Directions. Hence, it is unlikely that two sets of regulations will regulate intermediaries simultaneously. Accordingly, any interpretation that the Guidelines and the Intermediary Directions co-exist may not be correct.

However, on the other hand, there is a section in the industry arguing that the absence of an overriding provision under the Guidelines is indicates that the RBI wants the Intermediary Directions to continue to exist, at least until June 2021 – the time period granted to existing intermediaries to migrate to the Guidelines. They contend that the RBI proposes to regulate only pure play payment intermediaries (namely, aggregators and gateways that are involved in providing payment processing services to merchants) through the Guidelines. In this regard, this view seems to suggest that merchant aggregator websites or e-commerce marketplaces that collect payments on their own platforms and facilitate the settlement of such payments to their end merchants (as an ancillary function) should still continue to be governed by the Intermediary Directions.

In our view, in the absence of any such distinction drawn by the RBI, the regulatory framework under the Guidelines should be applicable to all intermediaries, agnostic of whether they undertake payment facilitation for their own websites and marketplaces or for third-party merchant websites. In this context, it is imperative to note the Guidelines unambiguously clarify that e-commerce marketplace entities that perform aggregator functions need to separate the aggregator function from their marketplace activities and apply for an authorisation as an aggregator.

We expect the RBI to come out with guidance and clarifications to put these discussions to rest.

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EGYPT

Managing Covid-19

A Q&A with the Matouk Bassiouny & Hennawy team on the ability to furlough employees, reduce salaries, freeze annual raises and other key employment issues under Egyptian law in light of Covid-19

Covid-19 is fundamentally impacting day-to-day business operations worldwide. Many offices have been shut down and many companies have ordered employees to work from home, while taking steps to remain virtually open. Consequently, the world economy has come to a halt and there is no doubt that there will be adverse pressure on business revenues, which will mean that businesses may not be able to sustain current payroll costs.

Below Matouk Bassiouny & Hennawy has compiled a list of commonly asked questions surrounding labour laws in Egypt, the impact of the pandemic on labour relations in Egypt and employers' abilities to take certain economic measures that could have an impact on their employees.

Can an employer unilaterally reduce salaries?

Generally, no. Apart from limited reductions for disciplinary reasons, employers cannot unilaterally reduce salaries.

There are two limited exceptions to this rule in the Egyptian Labour Law. The first is where there is a compelling event or circumstance, outside an employer's control, which prevents employees from working despite showing up for work. In such cases, employers may reduce the salaries by up 50% of an employee's salary for the duration of the event or circumstance.

A second exception is in cases where the employer has the right to terminate the employment contract for economic reasons (an issue further addressed below). Employers may instead decide to decrease employees' wages, as long as they do not go below the statutory minimum wage. However, employers must first obtain approval from a governmental committee assembled for this purpose. We note however that this is a lengthy and bureaucratic process as the committee does not convene regularly and current

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lockdown measures may even prolong that process. In any event, if this course of action is pursued, employees have the right to terminate employment contracts and are entitled to an end-of-service compensation. This compensation is equivalent to the gross salary of one month for each of the first five years of employment, and the gross salary of one and a half months for each year exceeding that.

It is possible that the Covid-19 pandemic could fulfil both of these exceptions, however this must be determined on a case-by-case basis, taking into consideration the economic impact of the pandemic on an employer's business.

Can an employer freeze salaries?

Egyptian Labour Law states that all persons governed by the Labour Law are entitled to a minimum annual raise of 7% of their basic salary. The basic salary referred to here is not the employee's actual basic salary, but rather the salary upon which social insurance contributions are calculated. This is currently capped at EGP7,000 ($441) per month, and therefore the annual increase is actually EGP490 or less.

Apart from this minimum annual raise, employees are not normally entitled to a salary increase except if a salary increase is stipulated in a contract or internal regulations, in which case it becomes mandatory; if a salary increase has become an acquired right, in which case it also becomes mandatory – a salary increase would become an acquired right if the same salary increase has been granted generally (namely to all employees or to a class of employees) for at least three consecutive years; or if there is a collective labour agreement that stipulates an annual increase between representatives of employers, such as the Egyptian Tourism Federation and Egyptian Banks Federation, and representatives of employees, such as union organisations. These latter types of annual increases usually range between 10% – 20% of the basic salary on which social insurance is calculated.

These circumstances are not impacted by the Covid-19 pandemic, and as such employers can only freeze salaries if none of the above circumstances are fulfilled.

Can an employer reduce variable compensation that is based on performance ratings?

In most cases, yes. However, if an employee has earned the same bonus year after year, while maintaining the same performance rating, there is a risk that the employee could claim that they have acquired a right to the same bonus payment.

Once again, this is not impacted by the Covid-19 pandemic.

Can an employer force employees to take vacation time?

Yes. Employees are entitled to a minimum annual leave of 21 calendar days. This is increased to 30 calendar days if they have been employed for more than 10 years or they are over 50 years old.

It is up to the employer to determine the dates of annual leave according to work requirements and circumstances. An employee is obliged to take leave on the date and for a period of an employer's choosing. If an employee refuses in writing to take the leave specified by the employer, the employee's right to financial compensation for unused leave is forfeited.

Can an employer lay off employees for economic reasons?

In principle, yes. Employers may use their discretion to fully or partially close down their establishment, or reduce its size or activities, and accordingly, the size of their workforce. In order to do so, the employer must follow a specific set of procedures whereby they must submit a request to the competent committee at the Ministry of Labour, along with sufficient evidence that the establishment is facing unexpected economic circumstances under which is has become inevitably necessary to cut down its workforce.

If the committee approves the request, the employer will have the right to lay off certain employees with compensation or modify their employment terms (reduce their salaries). The employer must notify the employees, as well as the relevant union organisation, of the request and the decision issued by the committee to totally or partially close down the establishment or to reduce its size or activities.

If the employer's collective labour agreement does not include objective criteria for selecting which employees should be laid off, the employer must consult the relevant union organisation after the issuance, but before the implementation of the decision. Seniority, family burdens, age, professional capabilities and skills of employees are among the criteria that can be used as determining factors. In all cases, these criteria must take into account the balance between the interests of the employer and employees.

Affected employees can file a grievance against the decision to cut down the workforce to a separate committee, which would convene solely for this purpose. If such a grievance were to be filed, the decision to cut down the workforce would be suspended until a ruling on the grievance is issued. The committee considering the grievance would then also determine the date of implementation of the decision to cut down the workforce.

Employees laid off through this process are entitled to an end-of-service compensation equivalent to the gross salary of one month for each of the first five years of service and the gross salary of one and a half months for each year exceeding that.

That being said, this is also a lengthy and bureaucratic process. These committees do not convene regularly, and Covid-19 lockdown measures may further prolong the process.

Can an employer impose a short-term furlough or reduce employee working hours by a certain percentage, with a corresponding percentage of reduction in pay?

In our view, an employer cannot unilaterally impose these types of measures on employees. If an employer wishes to pursue this course of action, they must seek the approval of the government committees, the processes for which are outlined above in the first and fifth question.

What are the employer's health obligations in light of Covid-19?

Under the Egyptian Labour Law, employers must take all necessary measures to protect employees from the risk of infection with bacteria, viruses, fungi, parasites and other biological hazards whenever the nature of the work exposes the workers to the conditions of their infection. Employers must take preventative measures to minimize the negative risks that arise from (or are aggravated by) their absence, such as those related to first aid and hygiene.

Failure to abide by this rule incurs a penalty of imprisonment for a minimum period of three months and/or a minimum fine of EGP1,000, not exceeding EGP10,000. The penalties double in cases of repeat offences.

Both penalties of imprisonment and fines are obligatory if failure to abide by the regulations of safety, professional health and security in the workplace results in death or major injury.

On the March 14 2020, the Ministry of Health and Population issued decree no. 145 of 2020, which lists Covid-19 under the first section of infectious diseases stated in law no. 137 of 1958. According to this law, employers must now inform the competent health authority of any employee that is infected or suspected of being infected with Covid-19. Employers are otherwise are subject to penalties (namely, a fine or two months imprisonment).

Overall, there are certain limited measures that employers can take in response to Covid-19 in regard to their payroll costs. It is difficult to predict how the government and courts would respond to businesses resorting to such cost-cutting measures on a mass scale. It also remains to be seen whether the government will step in with certain bailout measures to prop up eligible employers during the pandemic, such as a wage subsidy scheme.

AFRICA MARKET MAKERS 2020

EGYPT

Banking on change

Mohamed Hashish of Soliman Hashish & Partners looks to the future of Egypt's banking laws and reviews the New Draft Banking Law, which is making its way onto and will diverge substantially from the previous regime

Egypt is one of the three largest economies in Africa and is strategically positioned at a crossroads between east and west, making it a significant player in international trade in the Middle East and Africa (MENA) region. It is also home to the Suez Canal, a key artery in global trade that connects the Mediterranean Sea with the Red Sea.

Egypt's total area is 1,010,408 square kilometres, including 995,450 square kilometres of land and 6,000 square kilometres of water. According to the Egyptian Central Agency for Public Mobilization and Statistics, the population grew to over 100 million in 2020, divided among 27 governorates, 217 cities and 4,617 villages. Governorates with the highest population are Cairo (10.8%), Giza (8.6%) and Sharqiyya (7.4%).

The Egyptian government has been working hard to attract more foreign direct investment (FDI). As a consequence of these efforts, fDi Markets 2017 categorised Egypt as one of the top five destinations globally for greenfield FDI in 2016 and Forbes named Cairo as one of the top 10 cities in the world to launch a tech start-up in 2016.

According to fDi Intelligence's latest fDi Report 2020: "Egypt replaced South Africa as the second ranked destination by projects in the region, experiencing a 60% increase from 85 to 136 projects". This ranking covers the MENA region. Furthermore, Egypt led MENA countries in capital investment in 2020, attracting 12% of all capital investment with a total value of $13.7 billion. Financial services were one of the top five sectors for these projects in MENA in 2019.

In general, the Central Bank and Banking Sector Law No. 88 of 2003 bans any natural or legal person from practicing any banking activity, as prescribed by the law, in Egypt without being licensed by and registered with the Central Bank of Egypt (CBE). This restriction does not

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apply to any public legal person that operates banking activities within its scope of incorporation or international financial institutions (IFI) that were empowered to do so in Egypt by virtue of any special law or international treaty. These IFIs include the International Monetary Fund (IMF), the World Bank Group and *Agence Française de Développement* (AFD).

Banking activities are defined under the Banking Law as: "any activities of receiving deposits, providing refinancing, loans, facilities, contributing to share capitals in local companies as well as any other activities that is considered a banking activity as per the banking custom, on a regular basis and as the main business activities of any person carrying out these activities." This definition is also used un the Egyptian Trade Code.

Any person violating the restriction above will face imprisonment for a period of 24 hours to three years and/or a minimum fine of EGP5,000 ($317) and maximum fine of EGP50,000, in accordance with the Banking Law.

There are currently 38 banks operating in Egypt. The latest licence issued by the CBE to approve a new bank in Egypt was for Arab International Bank on June 5 2012. Since then, the CBE has not issued any new licences in Egypt, so the only way that any non-registered bank has been able to operate in Egypt is through the acquisition of a registered bank.

"A profit bonanza for Egyptian banks is ripening the industry for acquisitions. If only there were more willing sellers" – this is how Bloomberg has described the banking sector in Egypt. Over the past eight years Egypt seen only a few, albeit very large, M&A deals in the banking sector. These include Qatar National Bank Alahli's (QNB) acquisition of National Société Générale Bank Egypt (NSGB) in 2013, Emirates NBD's acquisition of BNP Paribas Egypt in 2013 and Attijariwafa bank's acquisition of Barclays Bank Egypt in 2017. Newspapers have recently reported discussions relating to a potential acquisition of Bank Audi Egypt by First Abu Dhabi Bank.

No one can deny the rapid global change in the banking and finance sector, notably the transition into fintech. The banking sector in Egypt, a country that witnessed two revolutions in 2011 and 2013, has undoubtedly been impacted by rapid global change as well as by local political upheaval. This was more than enough for the Egyptian Government, encouraged by the CBE, to propose an entirely new draft for the Banking Law (New Draft Banking Law). The New Draft Banking Law was prepared based on advice from international consultancy firms, a comparative study of other countries' laws, international standards, the Basel Framework, recommendations from the OECD, World Bank and IMF, and recommendations from CBE-registered banks.

As per the Egyptian Constitution, the New Draft Banking Law was submitted to the Egyptian House of Representatives for review and approval. After an almost five month review, the House of Representatives introduced several amendments to the New Draft Banking Law that was approved in principle by the House of Representatives on May 5 2020.

New framework, new provisions

There are several important new provisions in the New Draft Banking Law, as amended by the House of Representatives which represent a marked break with the existing legal framework.

The New Draft Banking Law doubles down a restriction under the Companies Law (the Egyptian Companies Laws No 159 of 1981) that prohibits any member of an Egyptian-registered bank's board of directors from being appointed to the board of more than one Egyptian-registered bank or of an insurance company. It also prohibits any such board member from providing management or consultancy services to an insurance company or to more than one Egyptian-registered bank. The New Draft Banking Law highlights that this restriction will be imposed on anyone acting as a board member either in person or as a representative of any entities; this was not explicitly stated under the Companies Law's existing provisions.

All persons that are subject of the New Draft Banking Law are required to legitimise their position by no later than one year. The CBE can extend this by no more than two years.

The New Draft Banking Law will enter into force the day following the date on which it is published in the Egyptian Official Gazette, which diverges from the CBE's proposal that the law enter into force 30 days after publication.

The New Draft Banking Law adopts the same definition of 'banking activities' used by existing banking law.

The required minimum paid-in capital for the CBE will be increased to EGP10 billion instead of the EGP3 billion required by the existing law. The governor of the CBE will also be blocked from serving more than two successive four-year terms, which contrasts with the absence of any limits under the existing law.

The new law will allow the CBE to enter into loan agreements with local and international entities, however there are important existing provisions that will control this activity. According to the Egyptian Constitution, the House of Representatives is entrusted with approving the state's public budget. The executive authority – the President, the Government of Egypt (including the CBE) and any local administration – cannot borrow, obtain facilities or engage in any project that is not included in the state's public budget, unless parliament approves. The Public Budget Law also imposes a similar restriction on the executive, stipulating that it "may not enter into loan or get engaged in projects that are not included in the State's public plan or budget resulting the utilization of amounts from the State's treasury in the future without having an approval from the Parliament".

The new law will compel the CBE to prepare its financial position statement on a monthly instead of weekly basis.

The CBE will be allowed to enter into MoUs, agreements and/or protocols with its similar non-Egyptian supervisory entities to allow them to conduct an inspection of any registered bank in Egypt that is affiliated to any non-Egyptian bank subject to the supervision of such entities abroad.

The required minimum paid-in capital for banks in Egypt will become EGP5 billion, up from the existing EGP500 million requirement, while the minimum paid-in capital for branches of non-Egyptian banks will continue as $50 million.

The New Draft Banking Law requires each registered bank in Egypt to evaluate all its risk, especially its investments and loan portfolio risks, on a quarterly basis instead of semi-annual basis, as under the existing rules. Banks registered with the CBE will only be able to use the outsourcing services of providers that are registered with CBE.

The law relaxes and extends the deadline for the Notary Public Office to review any commercial mortgage request from seven days to 15 days. It also increases the minimum capital for credit bureaus in Egypt to EGP200 million from EGP5 million.

The Military Prosecutor (or any of its delegates) and Military Felony Court in Cairo are both empowered under the new law to obtain any data on any customer of an Egyptian-registered bank.

No one is now allowed under the New Draft Banking Law to operate or provide a payment system without a CBE licence. This new restriction is applied to all persons, whether natural or juristic, carrying out such activity inside Egypt or providing such services abroad to any residents in Egypt except for stock exchanges, futures exchanges, securities settlement systems, licensed central clearing, depository and registry systems, custodian banks and internal systems of the Egyptian Ministry of Finance that do not include payment, collection, set off or clearance of payment.

The New Draft Banking Law includes a chapter dedicated to fintech which includes, for the first time in Egypt, the possibility of issuing or marketing cryptocurrencies as long as it has been licensed by the CBE's board of directors.

The required minimum paid-in capital for currency exchange companies in Egypt will be EGP50 million, instead of EGP5 million under the existing banking law, while the required minimum paid-in capital for money transfer companies in Egypt will be EGP24 million, up from EGP5 million.

Auditors are required under the New Draft Banking Law not to audit more than two registered banks and more than three currency exchange companies in Egypt.

The New Draft Banking Law explicitly excludes the CBE, as well as any entity that is subject to its supervision, from the application of the Egyptian Consumer Protection No. 181 of 2018 and the Egyptian Antitrust Law No. 3 of 2005.

Foreign entrants and minority holdings

Under the New Draft Banking Law, branches and subsidiaries of non-Egyptian banks will have to obtain approval from the CBE's supervisory authority to be eligible for registration in Egypt.

The new law imposes a $50,000 fee, to be paid to the CBE, for reviewing any new application to register branches of non-Egyptian banks with the CBE and a EGP1 million fee for reviewing any new application to register a new bank with the CBE. Any person carrying out the banking activities stipulated by the law without authorisation in Egypt will face a prison sentence stretching from 24 hours to three years, as is the case under the existing law, and/or a fine of between EGP100,000 to EGP1,000,000, up from the existing EGP5,000 to EGP50,000 penalty.

The New Draft Banking Law also requires CBE approval for any stake over 10% in any Egyptian-registered bank, and this also includes any holding held through global depository receipts (GDRs). As with the existing law, the new law will require any holding between 5% to 10% of the issued capital of any registered bank in Egypt to be notified to the CBE. In a further development however, the new law extends this requirement to include the voting right in such a bank as well.

The New Draft Banking Law adopts the same requirement under the existing law to obtain prior approval from the CBE's board of directors to hold 10% or over in any registered bank in Egypt; however, the New Draft Banking Law introduces an additional remedy for any unapproved ownership of shares whereby the distribution of dividends and any voting rights associated with such shares must be ceased; and the shares must be transferred no later than six months from the date on which the holding was acquired, otherwise the CBE will be have the right to request the Egyptian Financial Supervisory Authority (FSA) to appoint a brokerage firm to sell the shares. This new remedy is in addition to imposing a fine of between EGP1 million to EGP2 million, which is an increase from the EGP100,000 to EGP200,000 penalty allowed under the current rules. The New Draft Banking Law also imposes this requirement on GDRs. By contrast, the existing law does not include any explicit provision applying this requirement to GDRs. It is also worth noting that Commercial International Bank is the only registered bank in Egypt that has issued GDRs.

Non-Cash Payment Law

Aside from the New Draft Banking Law, a new Non-Cash Payment Law was issued on April 17 2019 under Law No. 18 of 2019 regulating use of non-cash payment methods. The Executive Regulation relating to this Non-Cash Payment Law should have been issued by the Prime Minister by no later than six months since after April 17 2019. However, this Executive Regulation has not been issued as required by the Non-Cash Payment Law.

The Non-Cash Payment requires all governmental authorities, entities, public juristic persons and companies that the Egyptian Government owns the majority or the entire of its capital to settle all financial obligations due to and social insurance subscriptions due on their members, employees and experts by any non-cash payments except for travel allowance abroad.

The Non-Cash Payment Law requires all private sector entities of any kind to:

- settle all payments due to or social

insurance subscriptions due on their employees, experts, chairs, board members and committees by non-cash payments as long as the total number of such employees or the aggregate amount of their monthly salaries exceed the limits to be determined by the Executive Regulation;

- settle all tax, customs duties, fees and fines; and
- repay instalments for any loan and insurance premium.

All governmental and private sector entities mentioned above are also required, within the thresholds to be determined by the Executive Regulations, to settle any payment by non-cash payment related to:

- Payments to suppliers, contractors, service providers, or any other counterparty;
- Loans;
- Dividends distribution;
- Rent, purchase or allocation fees; and
- Any other types of payment to be determined by the Prime Minister.

Any person that violates the above requirements will face a fine of between 2% to 10% of the payment made in cash subject to a cap of EGP1 million.

AFRICA MARKET MAKERS 2020

NIGERIA

Changing landscape

Kenechi Ezezika and **Kofoworola Toriola** of **OAKE Legal** review Nigeria's new merger control framework and how it impacts foreign mergers with a Nigerian component

There has been significant change in the legal framework and market practice for mergers and acquisitions in Nigeria in recent times and more change is expected. Worthy of note is the new regulatory regime for mergers and acquisitions heralded by the passage of the Federal Competition and Consumer Protection (FCCP) Act in 2019 (the Act). The Act repealed sections 117 – 130 of the Investments and Securities Act, 2007 (ISA), stripping the Securities and Exchange Commission (SEC) of its regulatory powers over mergers and acquisitions in Nigeria and creating a new commission with powers to, among other things, regulate mergers and acquisitions in the country. The FCCP Act empowers the FCCP Commission to review all mergers and business combinations in order to ensure that they do not impede or distort the market or stifle competition. The oversight extends to mergers between non-Nigerian entities that result in a change of control of a Nigerian business.

The ISA did not provide clear rules on foreign mergers resulting in change of control of a Nigerian business. As such, parties to such mergers did not typically seek the approval of the SEC, although in certain instances, parties would notify the SEC, particularly in the cases where the merger would have required notification to the SEC if it was being conducted by Nigerian entities or where a Nigerian public company was involved. In contrast, sections 2(3)(d) and 92(1)(a) of the Act extends the FCCPC Commission's oversight to foreign mergers that result in a change of control (directly or indirectly) of a Nigerian business or asset.

Prior to November 2019, the provisions of the rules and regulations of SEC (SEC Rules) applied to all merger transactions. This is because the FCCP Commission and SEC had issued a joint advisory and guidance note on May 3 2019 stating that the SEC Rules will guide the process for obtaining approval for mergers pending the issuance by the FCCP Commission of its own rules in this regard. The

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FCCP Commission issued the Guidelines on Simplified Process for Foreign to Foreign Mergers with Nigerian Component (the Guidelines) in November 2019. The Guidelines only apply to foreign mergers with a Nigerian component.

Four pillars

The Guidelines have four key components: a simplified/standard approval process; a notification threshold/requirement; an application fee; and an expedited process.

There is a simplified approval procedure for foreign mergers with Nigerian component. The intention behind the Guidelines is to simplify the process for obtaining the FCCP Commission's approval in relation to foreign mergers with a Nigerian component. The documentation required to support an application for approval is significantly less than is prescribed by the SEC Rules for obtaining approval to purely local mergers. The documents specified in the Guidelines include:

- an information memorandum showing the effect of the transaction on the Nigerian market;
- the merger transaction document(s);
- audited financial statements for the financial year immediately preceding the notification;
- an executive summary of the transaction for publication by the FCCP Commission;
- a power of attorney granting authority to the relevant Nigerian representative(s) to undertake the necessary filing with or notification to the FCCP Commission; and
- non-confidential summary of the merger to be published by the FCCP Commission.

This documentation requirement is significantly less than required for local mergers, for which applicants must, in addition to the documents listed above, also submit draft financial services agreement(s) with the merging parties and their financial advisers; signed and notarised consent letters of directors and parties to the merger; list of claims and litigation of the merging parties; and draft proxy forms for each of the merging parties.

Regarding the notification threshold, the FCCP Commission has issued a Notice of Threshold for Merger Notification further to section 93(4) of the Act (the Threshold Notice). The Threshold Notice requires notification of a merger to be given to the FCCP Commission prior to its implementation where: the combined annual turnover of the acquiring undertaking and the target undertaking in, into or from Nigeria is at least N1 billion (approximately $2.78 million); or the annual turnover of the target undertaking in, into or from Nigeria equals or exceeds N500 million. Mergers below these thresholds do not require prior notification to the FCCP Commission unless a notification is specifically required by the FCCP Commission. S 167 of the FCCP Act, defines a target as: "an undertaking, which as a result of a merger, the whole or part of whose business would be directly or indirectly controlled by an acquiring undertaking or would directly or indirectly transfer control of the whole or part of its business to an acquiring undertaking".

Given that the thresholds are denominated in naira, the currency exchange rate plays a key role in determining where a foreign merger with Nigerian component requires the prior approval of the FCCP Commission. The Threshold Notice requires turnover in foreign currencies to be converted to naira at the prevailing exchange rate determined by the Central Bank of Nigeria. In view of the recent "adjustment" of the naira against the US dollars, some of the transactions which would have fallen below the notification threshold as at March 2020 will now be classified as a large merger under the Threshold Notice, and will therefore require the prior approval of the FCCP Commission.

The Guidelines prescribe fixed and variable fees for the processing of applications for approval depending on the nature of the merger. The fixed fee portion is a welcome development, when juxtaposed against the graduated processing fees prescribed by the SEC Rules. The SEC Rules prescribed fees that were fully based on the value of the transaction or the assets being acquired.

The fee applicable to transactions involving undertakings with a combined turnover of N1 billion and above is N3 million or 0.1% of the combined turnover, whichever is higher. A fixed application fee of N2 million will be paid where the annual turnover of the target undertaking in, into or from Nigeria equals or exceeds N500 million. The parties are not required to pay a separate filing fee, in addition to the processing fee and the fee for an expedited process, if applicable (see below). This is again in contrast to an application for approval to a local merger where the parties pay both filing and processing fees as prescribed by the SEC Rules.

The Guidelines also introduced an expedited procedure option for parties. Under this option, the FCCP Commission is expected to conclude its review of the transaction and issue a decision within 15 days of application. The time starts to run from submission of *all* documents required by the Guidelines. This procedure requires payment of an expedited procedure fee of N5 million, in addition to the relevant processing fee. Applications under this procedure are considered more quickly than the standard procedure which will typically take 60 days to complete. Where adequate documentation is not submitted under the expedited procedure, and a notice of deficiency is issued by the FCCPC Commission, the application will be moved to the standard applications list and will no longer be processed under the expedited procedure.

Monitoring foreign mergers

In March 2020, the FCCP Commission released its draft Merger Review Regulations (the Draft Regulations). The Draft Regulations seek to provide a regulatory framework for the review of mergers, including foreign mergers with a Nigerian component.

The Draft Regulations seek to expand the provisions of section 92(1) of the FCCP Act in relation to foreign mergers with a Nigerian component. Paragraph 9 of the Draft Regulations defines foreign mergers requiring the approval of the FCCP Commission to include a merger that will occur purely as a result of a transaction involving undertakings wholly domiciled outside Nigeria, if it has a local component materiality, such as having subsidiaries in Nigeria. This is notwithstanding that such a merger does not attain the turnover requirement prescribed by the Threshold Notice. As stated earlier, a transaction is notifiable where it meets the prescribed threshold requirement. Where a merger does not satisfy this condition, there should be no requirement to notify the FCCP Commission except in the case of a small merger that, in the opinion of the FCCP Commission, can lessen competition.

The Draft Regulations also provide for the appointment of a local legal representative to aid with the notification process on behalf of the parties to a transaction. It has been suggested that this provision should be expanded to include financial advisers, as was applicable under the SEC Rules.

Welcome development

The Guidelines are novel and are a welcome development. They address the uncertainties that had hitherto surrounded the treatment of local mergers or business combination that result from foreign mergers.

It is our expectation that the provision of the Draft Regulations, which seeks to expand the provisions of the FCCP Act by requiring the approval of the FCCP Commission for foreign mergers with material local component notwithstanding the combined turnover, will be amended to align with the provision of the Act to ensure uniformity.

AFRICA MARKET MAKERS 2020
SUDAN

Greener pastures

Mahmoud Salah Bassiouny and Yassir Ali of Matouk Bassiouny in association with AIH Law Firm review Sudan's investment framework and the impact that the lifting of US sanctions has had on doing business in the jurisdiction

The Republic of the Sudan has undergone a complex development process since achieving independence in 1956. Though Sharia was originally the main source of Sudanese law, the constitutional document for the transitional period of 2019 (the Transitional Constitutional Document) is anchored in common law principles. As a result, the legal system today is a mixture of Sharia law and common law principles. However, this transitional period expires 39 months after the signing of the Transitional Constitutional Document in August 2019. A new constitution is expected to be issued following this date.

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Key authorities and the legal framework

Sudan issued its Transitional Constitutional Document in the aftermath of the revolution of December 2018. In parallel to the judiciary authority, three transitional governmental authorities govern Sudan: the Sovereignty Council, the Council of Ministers and the Transitional Legislative Council. It is worth noting that the Legislative Council is not yet established and that accordingly its competence is jointly assigned to the Sovereignty Council and the Council of Ministers.

The governance structure is a federal system and the national government exercises power to protect the sovereignty of Sudan, guarantee the safety of its lands and enhance the welfare of its people.

The legislative branch is represented by the Transitional Legislative Council. Though not yet established, is should in theory be composed of no more than three hundred members, with a 40% quota for women, and represent all the forces that contributed to the change in the 2018 revolution. The judicial branch comprises a Constitutional Court that handles issues relating to constitutional law as well as cases of human rights. The judicial system in Sudan is independent from the executive and legislative authorities.

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The Sudanese judicial system hierarchy is: the Supreme National Court, the highest court in the land; the courts of appeal, which hear cases from lower courts; and the several different courts of first impression. The executive branch comprises the executive authority, embodied by the Sovereignty Council. The Council represents the position of head of state and is comprised of 11 members chosen by the Transitional Military Council and the Forces of Freedom and Change, a large Sudanese political coalition, along with the Council of Ministers. The prime minister is appointed by the Sovereignty Council based on the choice of the Forces of Freedom and Change.

Below the federal level, the 18 states of Sudan oversee and govern public services at the local level.

Sudan has entered into several bilateral investment treaties (BITs) with different countries, some of which are in full force while others have only been signed. The BITs that Sudan has fully implemented include those with China (1999), Egypt (2001), Ethiopia (2000), France (1978), Germany (1963), India (2003), Islamic Republic of Iran (1999), Netherlands (1970) and Switzerland (1974). The signed BITs, which are not yet in force, include those with Algeria (2001), the Belgium-Luxemburg Economic Union (2005), Italy (2005), Kuwait (2001), Malaysia (1998) and Turkey (2014).

Sudan has also entered into several multilateral investment treaties. The Investment Agreement for the Comesa Common Investment Area in 2007 has not yet been ratified, but the Interim Economic Partnership Agreement between the European Union and ESA (Eastern and Southern Africa) became effective in 2012. The Agreement on Investment and Free Movement of Arab Capital among Arab Countries in 1970 was later followed by the Agreement on Promotion, Protection and Guarantee of Investments amongst the Member States of the Organization of the Islamic Conference in 1988.

Sudan has signed and ratified the ICSID convention, which was entered into force in Sudan in 1973 and grants foreign investors the right to subject any dispute involving the Sudanese government to arbitration under ICSID rules.

The Investment Disputes Court has been established in accordance with the Investment Law to settle the investments related matters. All such investment-related disputes will be referred to this specialised court unless the parties have agreed to refer the matter to arbitration or reconciliation. Additionally, disputes governed by one of the following treaties to which Sudan is a party are also exempt from referral to the investment courts to settle their issues:

- the Unified Agreement for the Investment of Arab Capital in Arab States 1980;
- the Agreement for Settlements of Investment Disputes among Arab States 1974;
- the Agreement for Settlement of Investment Disputes between States and citizens of other States 1965; or
- the General Agreement for Economic, Technical and Commercial Co-operation among Member Sates of Islamic Conference 1977, and any other agreement to which Sudan is a party.

Sudan is a party to the New York Convention on the enforcement of foreign arbitral awards. Furthermore, Sudan issued the new arbitration act in 2016 that allows

Sudan to enforce national and international arbitral awards, as long as they are in compliance with the applicable law. In order to be enforceable, the arbitral award cannot contradict a decision previously issued by the Sudanese courts and there must be reciprocal enforcement between Sudan and the country where the arbitral award was issued.

The right to arbitrate outside of Sudan, does not prejudice the purview of Sudanese courts to review the validity of an arbitral award prior to its enforcement.

History behind the sanctions

The sanctions on Sudan were first initiated in 1997 when US President Clinton issued Executive Order (EO) 13067, which imposed a comprehensive trade embargo on Sudan and blocked the assets of the Government of Sudan. In 2006, under the Bush administration, EO 13400 was issued, targeting those involved in the conflict in Sudan's Darfur region. This was followed by EO 13412, which exempted the then-regional Government of Southern Sudan, as well as certain specified areas, from most of the prohibitions under the Sudan sanctions programme.

On January 13 2017, President Obama issued EO 13761, "Recognizing Positive Actions by the Government of Sudan and Providing for the Revocation of Certain Sudan-Related Sanctions". This stipulated that if the Government of Sudan continued its positive actions to reduce violence in the region, sanctions would be lifted. On October 12 2017, the Trump administration revoked EO 13067, lifting the comprehensive trade embargo on Sudan and unblocking the assets of the Government of Sudan. It is also worth noting that Sudan is no longer on the US Department of State's list of countries certified as not cooperating fully with US counterterrorism efforts.

Because of the revocation of the US sanctions, the Sudanese market is now open to US persons to engage in trade. However, the Treasury Department's Office of Foreign Assets Control (OFAC) still requires licensing for certain exports and re-exports to Sudan involving agricultural commodities, medicine and medical devices as a result of Sudan's inclusion on the State Sponsors of Terrorism List. Other licenses are required for export to Sudan in different sectors such as software and technology. Furthermore, US and non-US persons still need to obtain any licence required by the Department of Commerce's Bureau of Industry and Security to export or re-export to Sudan certain items (including commodities, software and technology) that are on the Commerce Control List and if those transactions implicate certain end-use or end-user concerns.

Investment incentives

The legislative framework in Sudan provides several incentives for investments.

The National Investment Encouragement Act of 2013 (Investment Act) aims to facilitate foreign investment by introducing into legislation the concept of fairness and equal treatment for both domestic and foreign investors, whether for public or private sector investments. The Investment Act creates a "one-window" system in which all the competent investment-related authorities are located on the same premises. It is also worth reiterating that Sudan has signed and implemented several bilateral and multilateral investment treaties.

According to the approved list of applicable investments issued by the National Authority for Investment (Authority), capital imported to fund the establishment of projects is exempt from VAT. The Authority can grant a project an exemption from customs duties on the capital required for the setup and preparations of a project and on transportation, excluding administrative vehicles (as defined under the Investment Act). We note that customs duties exemptions are currently suspended as per the decision of the Supreme Committee for Economic Emergencies on April 24 2020.

The Investment Act also provides that:

- Assets and properties of a project will not be subject to nationalisation, seizure, confiscation or appropriation, unless for public policy or unfair compensation reasons;
- Funds of a project will not be subject to seizure, confiscation, appropriation, freezing, attachment or receivership, unless with a judicial decree or order;
- Invested capital will be repartitioned in the event that a project is either not executed, liquidated or subject to disposal by any means after obtaining the approval of the Authority and all legal obligations are met;
- Machinery, equipment, goods, apparatus, transport conveyances or other ancillaries imported on account of the project will be re-export sold or assigned in the event that the project is not executed, whether wholly or partially, after all legal obligations are met;
- Transfer of profits and financing cost of foreign capital or loans in the currency by which the Central Bank of Sudan deals or the loan on maturity date, will be allowed after payment of all legally due obligations of the project;
- Importation of raw materials needed for the project and its products will be allowed.

Furthermore, investors enjoy the right to import and recruit foreign labour, according to the terms and conditions stipulated by the relevant laws and regulations. Foreign labourers, and their families, can obtain work and residence permits throughout the term of execution and operation of a project. However, it should be noted that the wages and allowances of foreign labourers on the project are subject to social insurance.

The Investment Act provides that relevant state authorities will register lands for industrial, service and agricultural projects. They will carry out detailed technical planning and surveys, and prepare maps, which they then pass onto the Authority. The Authority can then allocate investors the land they need to undertake national and strategic projects at an attractive rate and quickly. Investors will receive the land within a month of registering the purchase.

It is worth noting that mineral concession agreements are undertaken by the executive authority without requiring parliamentary approval. Typically, mineral concession agreements in Sudan are valid with the signature of the Minister of Minerals or his/her representative.

Dealing in foreign currencies is regulated under the parliament-issued Sudanese law of 1981, together with its regulation issued in 1999 (Foreign Currency Regulation). The Foreign Currency Regulation stipulates that direct investments into Sudan using foreign currencies must be actioned through a certified banks. The Foreign Currency Regulation states: "it is allowed to enter into any direct investment transaction from abroad without restrictions regarding the movement of the foreign currency […]". Investors are allowed to re-transfer any foreign currency exploited in the direct investment referred to above, provided that the foreign currency is registered with the Central Bank of Sudan in accordance with the requirements and circulars issued in this regard. That being said, the Foreign Currency Regulation sets a limit and provides that "the banks, entities, and persons certified to deal with the foreign currency are not allowed to sell it to their customers for the purpose of investment in financial instruments abroad."

Open for business

Since the Sudanese Revolution and the ousting of President Al Basheer, Sudan has embarked on several reforms primarily aiming to attract foreign direct investment and facilitate doing business in Sudan. Due to its unique geographical assets, which include red sea access, large tracts of arable land and a position as a gateway in between the Middle East and Africa, the Republic of Sudan is now very much open for business.

AFRICA MARKET MAKERS 2020

UNITED ARAB EMIRATES

Embracing change

Ahmed Ibrahim, Malack El Masry and **Dania Yassin** of **Matouk Bassiouny & Ibrahim** review some of the positive developments in the UAE legal environment despite the challenges of Covid-19

The World Health Organisation (WHO) declared the Covid-19 a pandemic in March 2020, and with a transmission rate higher than the seasonal flu, reported cases have continued to escalate globally. As Covid-19 continues to unfold, many ongoing and prospective commercial transactions in the United Arab Emirates (UAE) are facing an avalanche of uncertainty over when, if, and how these deals will or can be completed under the circumstances.

This is especially applicable for the more fragile industries that have been negatively impacted by Covid-19 restrictions and need immediate relief in the form of buyouts or JVs. As governments and public health authorities adjust their policies to respond to this challenge, UAE companies need guidance on how to best address the situation and limit the unprecedented disruption to their businesses.

As we are witnessing a new chapter in UAE's legal environment, we believe existing and potential investors interested in the UAE should keep an eye out for opportunities during Covid-19. Historically, economic crises often create opportunities for investors. In the case of the economic downturn caused by Covid-19, there is a high probability that interested investors will find opportunities in the accelerated sales at attractive prices of companies that are, unfortunately, facing financial difficulties. Furthermore, investors should also be on the lookout for companies going through a restructuring that requires investment to either maintain or expand its business due to the global changes resulting from the pandemic.

The UAE government has proven its ability to stand against the global pandemic's impact on its market by using advanced strategies, such as the implementation of legal technologies, as well as the liberalisation and structuring of foreign direct investment (FDI).

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Pandemic boosts digital transformation

Over the past few years, the current legal culture in general, and in the UAE specifically, has gradually steered away from traditional ways of doing business, thanks to the introduction of innovative technologies into the field. Covid-19 has forced the legal industry to accelerate this process of digital transformation.

Although digital transformation has been a priority for years in the UAE, the local legal industry has scarcely taken notice and has underestimated its need to adapt to such transformation, except in a few free zones. Certain UAE free zones, namely the Abu Dhabi Global Market (ADGM) and Dubai International Financial Centre (DIFC), have set the pace in implementing digital transformation to deliver commercial and legal services without delay or disruption. Even if not by choice, the global pandemic has sped up the UAE authorities' move towards digital transformation. Although one may argue that the UAE legal industry, and especially its mainland authorities, have not yet had time to process the rapid acceleration of digital transformation, the UAE has demonstrated that it surely can, when incentivised, alter entrenched methods of delivering legal services.

Countries such as the US and UK have been working to incorporate innovative legal technology for years, heling to make the transition to a virtual legal system amid the pandemic smoother. As many judges have stated in these jurisdictions, legal tech tools are lifesaving and have prevented delays in the justice systems. Similarly, the UAE, starting with the Dubai Courts, reformed its traditional legal system in the wake of Covid-19 by implementing digital transformation to its legal system, and holding hearings remotely at cessation, appeal and first instance level, except for criminal cases. The other emirates will surely follow suit to prevent any further delay in legal procedures.

The UAE was one of the few countries in the region working to implement legal tech in its legal system prior to Covid-19. Back in April 2018, the UAE announced the Emirates Blockchain Strategy 2021 (and the Dubai Blockchain Strategy), which seeks to transfer 50% of government transactions onto a blockchain platform by 2021. The strategy envisaged three strategic pillars: government efficiency; industry creation; and international leadership.

Fast forward to 2020, the UAE government is preparing to respond to the global pandemic with new and powerful tools in the legal system, such as digital transformation, in an effort to bring a new wave of economic opportunity and ensure that no interruptions occur in commercial transactions during this period.

New strategies have been carefully considered. Being more efficient and cost-effective, these strategies have a high probability of increasing the number of commercial transactions in the UAE by both foreign and local investors. There will be no need to postpone deals and no issue in successfully completing transactions using compatible and secured virtual systems.

For example, in order to effectively transfer shares in many countries in the region, including in mainland UAE, sellers and buyers must notify and obtain certain government approvals, for instance from the department of economic development in the relevant emirate (DED). In the UAE, the parties must also be physically present before the public notary in order to sign the share transfer documents. Once the documents have been signed, the notarisation process is deemed complete and the share transfer is completed by the DED's issuance of a new licence reflecting the new shareholding structure.

We have recently assisted clients in successfully completing transactions using new technologies in several emirates. The government is using a combination of online and video conference methods to help provide notarial and other governmental services in mainland Dubai and Abu Dhabi to establish companies for new joint-venture transactions and complete share transfers for M&A transactions.

Though the various processes in effect are straightforward, they are new both to the authorities and to the investors and are therefore, for now, still time consuming. The processes generally include the preparation and submission of applications/requests and continuous follow-up with the authorities to ensure successful completion. We are confident that in a few weeks, the processes will become more efficient and less time consuming.

Electronic signatures (e-signatures) are available, recognised and enforceable under UAE federal law and DIFC laws with certain limitations. ADGM laws do not, generally, provide for e-signatures, however, English law principles are applicable and may allow for such. If a document can be e-signed pursuant to ADGM law and submitted to the authorities if necessary, then it should be enforceable. E-signatures have not been used much in previous M&A transactions where parties usually require a wet ink signature, but we envisage that due to this climate they may soon become the norm.

We have also seen recent changes by the Securities and Commodities Authority (SCA). The SCA now requires shareholders of public joint stock companies to hold general assembly meetings virtually, register attendance online and cast electronic votes on the announced agenda items and on some corporate matters such as the election of members to the board.

This requirement does not apply to other types of companies, such as limited liability companies. Technological advances in this regard are yet to be seen, especially if the minutes of such meetings, whether board or general meetings, require authorities like the DED to reflect the resulting changes on the licence of the relevant companies, such as a change in the manager of a limited liability company in Dubai.

We constantly hear and read about the negative impacts of Covid-19 on many legal sectors, especially M&A, due to certain regulatory requirements for an effective share transfer, as mentioned above. However, we foresee a more optimistic future with the application of digital transformation that has been in the works in the UAE for years. Furthermore, many concerns in M&A transactions that typically took longer to successfully complete, can now be completed virtually in a more efficient and cost-effective manner.

Continuing down the path of liberalisation of the UAE market

While many jurisdictions are increasing scrutiny of FDI, the UAE government has chosen to take a different route by liberalising its market and opening its doors to a new pool of foreign investors. Previously, the UAE Council of Ministers announced the approval of a list of sectors and economic activities eligible for up to 100% direct foreign ownership in UAE onshore companies (UAE FDI Regulations).

In March 2020, amid the pandemic, the UAE government continued its efforts to further liberalise and diversify the market to meet global investment standards and attract investors. Its main move was to issue the UAE Cabinet's FDI Positive List Resolution, which was implemented immediately and heralds a major development for both existing and potential foreign investors. The Positive List Resolution provides clear instructions concerning the 122 economic activities made eligible under the UAE FDI Regulations exemption and sets out the minimum capital, requirements and conditions for each economic activity, as well as any available incentives. The Positive List Resolution stipulates the type of companies (FDI Company) that can apply for FDI exemption, namely limited liability companies and private joint stock companies (including single shareholder companies). Furthermore, it provides clear guidelines for the relevant committees that handle FDI applications in all the emirates to properly evaluate applications.

The Ministry of Economy has also published detailed guidance in the form of a Foreign Investor Guide, which, among other things, sets out the step-by-step process for the incorporation of an FDI Company in the UAE. The guide also specifies that existing companies can apply to convert into an FDI Company. If the applicant owns entities in several emirates and intends to obtain FDI exemption for those entities, the FDI exemption application must be submitted to each FDI committee in the relevant emirate, preferably simultaneously, and tick the same boxes for each emirate to ensure that the group as a whole obtains the exemption.

Our team has successfully obtained FDI exemptions for well-known entities in the UAE in the past. Based on our previous experiences and current applications, we can predict that the Positive List Resolution will encourage many more foreign investors to take advantage of this opportunity. The authorities, relevant committees and the applicants now have clear guidelines in place at the federal level.

Embracing the change is a challenge, but as all forward-thinkers know, challenges bring opportunities. The UAE government continues to rise to the challenges brought by Covid-19 and continues the fight to maintain its market integrity and investors' confidence. With this mindset, the UAE will surely come out stronger than before. Legal tech is one of the few silver linings of this frightening global pandemic. The developments present an opportunity to improve overall efficiency in order to adapt to a progressive and agile working environment. We can surely expect new laws, regulations and procedures to be introduced by the UAE government soon as the local market continues to adapt.

AFRICA MARKET MAKERS 2020

ALGERIA

Realities and challenges

Houda Sahri, Jean-Jérôme Khodara and **Nahla Djabi** of **Matouk Bassiouny** in association with **SH Avocats** review the flurry of pro-investment legal developments being ushered in by Algeria's government

In February 2019, President Bouteflika's announcement that he would run for a fifth term compelled hundreds of thousands of Algerians to flood the streets of several Algerian cities in opposition to yet another Bouteflika re-election. This so-called Hirak movement led to Bouteflika's resignation and the election of Abdelmajid Tebboune as the new president in December 2019. In addition to the continuing Hirak movement, the new regime also faces oil prices in free fall and a Covid-19 induced global recession.

While discussions are still ongoing and different stakeholders have conflicting visions, there seems to be a consensus that the economic model for Algeria established under Bouteflika, with its restrictions on foreign investment, is in dire need of swift and real change.

With this in mind, the new Algerian authorities have an ambitious structural reform plan to simplify regulations concerning companies, improve governance and transparency, reform the investment legal framework and modernise the financial sector. President Tebboune has announced that Algeria will not turn to external borrowing or increase the money supply as a solution to deal with its financial needs amid the sharp drop in oil prices. In this context, the Algerian political system understood the need to diversify the Algerian economy and become less dependent on the oil and gas industry, which still accounts for 96% of the country's exports.

With this objective in mind, the government has sent clear signals that it intends to boost foreign investment and that it is willing to alleviate some of the significant restrictions to foreign investment, namely the state's pre-emption right on the transfer of shares by or to foreign investors and the so-called 49/51 rule. In this article, we provide a recap of the circumstances which led to the introduction of these restrictions together with an update on the efforts to remove them. Finally, we provide a summary

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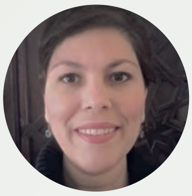

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on other recent and live legislative initiatives intended to boost foreign investment in Algeria.

The pre-emption right and 49/51 rule

The state's pre-emption right and the cap on any foreign shareholding in an Algerian company to 49% were initially introduced by the Supplemental Finance Law for 2009 (SFL 2009) on July 22 2009. These new rules were a direct result of Lafarge's 2008 acquisition of Orascom Construction Industries' (OCI) cement assets in Africa and the Middle East (including in Algeria) and led to the introduction of a series of stringent regulations rules in 2009 and 2010 to assert the Algerian government's control over foreign investments.

Since its introduction, the state's pre-emption right has changed several times, reflecting the political and social context in Algeria. Presently, three types of transactions can trigger the state to exercise its pre-emption right. They include the transfer of shares in an Algerian company by and/or to a foreign person or entity; of shares in an offshore company that owns shares in an Algerian company; and of shares in or assets owned by an Algerian company for a consideration deemed by Algerian tax authorities to be undervalued.

From a technical standpoint, several types of transactions that allow a controlling takeover of an Algerian company are omitted from the scope of the state's pre-emption right, for example a capital increase, transfer of business/assets, or contractual arrangements such as management agreements. It is critical to keep in mind the political background when analysing the Algerian state's right of pre-emption. Indeed, the Algerian state has considered exercising its pre-emption right on very few occasions, some of which were politically sensitive or otherwise considered to be strategic for the national economy.

The main purpose of the legislation on pre-emption is to grant the Algerian government a level of oversight on foreign investments in Algerian companies, regardless of whether the investment is structured by a transfer of shares or otherwise. In most cases, the Algerian government has merely threatened to exercise its right of pre-emption as an expression of disapproval, rather than a real intent to purchase. Generally, the Algerian government has resorted to the pre-emption right to veto controversial transactions, as was the case with the Total's recent acquisition of Andarco's assets in the region.

The new Supplemental Finance Law issued on 4 June 2020 (SFL 2020) removed the pre-emption right for all sectors, except for certain "strategic sectors" for which the pre-emption right has been replaced with a prior governmental approval process. Details of its implementation will be released with the upcoming executive regulations.

According to the 2016 Finance Law (FL 2016), "the involvement of foreigners in manufacturing, providing services or importation, is subject to the incorporation of a company whose registered capital shall be at least 51% owned by resident national Algerians". This 49/51 rule was also initially introduced in 2009 by Order 09-01 dated July 22 2009 approving the SFL 2009. Companies incorporated before 2009 with foreign ownership exceeding 49% were exempt from the 49/51 rule, but not allowed to register certain amendments to their commercial register, including any transfer of shares, until they complied with the 49/51 rule.

Once the 49/51 rule was introduced, Algerian foreign investment dropped drastically. The International Monetary Fund viewed the tough new conditions as a deterrent for foreign direct investment. Indeed, statistics show that in the period before the introduction of the rule, during 2007 and 2008, a significant number of investment projects were declared to the national investment authority (ANDI): 93 projects in 2007 and 86 projects in 2008. In the 2009 financial year, when the rule came in, there was a significant decrease in terms of the number of investment projects (four projects) and in terms of the project values and projected jobs.

The 2020 Finance Law (FL 2020), approved in December 2019, slackened the application of the 49/51 rule. The FL 2020 provides that the 49/51 rule will apply only to "production and service activities which are strategic for the national economy". According to the SFL 2020, the list of strategic sectors that will remain subject to the 49/51 rule includes mining, energy, defence, railroad infrastructure, airports, ports, and pharma. The 49/51 Rule has also been maintained for simple distribution activities, including the importation and resale of products in the local market.

A pipeline of pro-investment legislation

In addition to alleviating general restrictions such as the state's pre-emption right and the 49/51 rule, Algeria is also aiming to open the door to investment in several specific industries, including energy, the agri-food and manufacturing industries, tourism, paper, IT services, agriculture (which recorded a growth of 6.9% in 2018) and large retail outlets. There are a series of laws that have supported this policy.

The new energy law no. 19-14 of 2019 was adopted in December 2019, just a few weeks before the presidential elections, and was warmly welcomed by foreign investors. Although the new energy law maintains the 49/51 rule for the energy industry, it introduces significant tax incentives and new standards of contracts to replace the old concession contracts, which were not considered investor friendly. The new energy law also simplifies administrative procedures for investors.

In the most recent addition to e-commerce legislation no. 18-05 of 2018, a national base of e-suppliers was established within the National Center of Trade Register. The new e-commerce law has formalised e-contracts and clarified the obligations of e-suppliers, with the exception of a few products and services prohibited from e-commerce sale due their sensitive nature within Algerian society, including tobacco, alcoholic beverages and pharmaceutical products. Although the most important challenge for the development of an e-commerce market remains the limitation of online payments, the new legal framework for e-commerce as well as the adoption of an e-signature law no. 15-04 0f 2015 have had a positive impact on the investment environment and facilitated cross-border commercial transactions.

There has also been growing interest in the Islamic banking sector. Through various actions, Algerian authorities have expressed an openness to foreign investment to develop banking activities. The adoption of a new law in March 2020 defining Islamic banking transactions clarified the investment process and encouraged foreign players to enter this large and untapped market. In addition, the Central Bank of Algeria has allowed banks to introduce new products and services through a pre-approval process. We imagine this new framework will enable the strengthening of online payments systems and the introduction of other services including the e-wallet.

Leveraging off this momentum, a new Ministry of Micro-Enterprise and Startups was created to promote start-ups as an important lever for reviving the national economy. The prime minister underlined the importance of incubators, being the nucleus of companies, by promising to allow capital investment for start-ups in order to help meet their financing needs in early phases, particularly with feasibility studies and technical assistance, and diversify the financing tools intended for start-ups via crowdfunding platforms. Efforts are being focused on fostering a favourable climate. A specific legal framework for start-ups and micro-enterprises should be in place sometime in summer 2020, as announced by the minister in charge.

Other sectors also in the focus of the Algerian authorities include the agri-food industry. As commodities and food products remain the foremost items on Algeria's list of imports, and in an effort to rationalise imports, several projects to implement industrial facilities are in the pipeline that would not only serve the local market, but also promote exports to other African countries.

Finally, up until recently, foreign investors were prohibited from using international financing for their investment projects in Algeria and were required to use financing from local lenders. In a move to boost investments, the LF 2020 authorises the use of financing from international development finance institutions for projects that are strategic to the national economy. Furthermore, the SFL 2020 encompasses the right for foreign investors and their local partners to use international financing without the requirement for the project to be considered as strategic. As a result, foreign investors would be authorised to fund their projects in Algeria through facilities granted by foreign banks.

Sending the right signals

Faced with domestic political and social pressure for change and a challenging global environment with falling oil prices and the Covid-19 pandemic, the new Algerian government is sending strong signals that it is willing to attract foreign investors to boost the economy. The contemplated alleviation of the 49/51 rule and of the state's pre-emption right, together with several industry specific pro-investment legislations, may very well pave the way for a successful, and long awaited, opening-up of the Algerian economy, creating major business opportunities for investors in one the largest African markets.

Priority measures

Gabon responded quickly to Covid-19, leveraging off its experience with Ebola and Cholera. Matthieu Le Roux, Olivier Bustin and Carolina Reis of Vieira de Almeida (VdA) review the results of the government's actions and what the pandemic says about Gabon's future economic development

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On March 12 2020, the Gabonese Republic announced its first coronavirus case in the country. From that day on, the government implemented a series of measures to curb the spread of the virus and mitigate its effects on the social and economic wellbeing of the nation.

This swift response can possibly be explained by the preparation the country has had in dealing with highly contagious diseases such as Ebola and Cholera. In fact, the social habits, organisation and infrastructure that were developed under these outbreaks can now be recycled and put back into operation to better respond to Covid-19.

State of emergency

On April 12 2020, the President of the Republic of Gabon declared a State of Emergency. The State of Emergency is provided for in the Gabonese Constitution and is further regulated by Law 11/90. This specific regime applies in exceptional circumstances and enables the government to restrict certain individual freedoms and extend police powers to address an imminent threat resulting from serious breaches of public order, or events which, due to their nature and gravity, have the character of a public calamity.

The regime may be imposed on parts of the country or the whole territory. In this case the restrictions that have been adopted are of various kinds.

Regarding the right of movement, the Gabonese government provided for the closure of land, air (except cargo) and sea borders; the prohibition of all domestic and international passenger flights, except in cases of force majeure, medical evacuation and cargo; a ban on passenger trains, except freight trains and petroleum products; a curb on all non-essential travel, except for defence and security forces, essential SEEG personnel and their vehicles, medical personnel and their essential vehicles (such as ambulances), funeral staff and their vehicles and media personnel and

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their vehicles; a curfew between 6pm and 6am throughout the national territory; and restrictions on transportation.

From April 12 to April 27, Greater Libreville (Libreville, Owendo, Akanda and Pointe-Denis) was under a total lockdown. This measure implied the containment of each territorial zone (*arrondissements*) and the restriction of trips inside each *arrondissement* to ones required for essential activities related to food and health. Since April 28, Greater Libreville has been in a partial lockdown, with softened restrictions on circulation and the continuation of the 6pm and 6am curfew, subject to wearing a mask in public spaces. Nonetheless, travel between Greater Libreville and the rest of the country remains prohibited, except for supply and distress cases.

Businesses have been mandatorily closed, except for essential activities such as banks, petrol stations, grocery stores, bakeries, pharmacies, tyre fitters and garages, respecting social distancing rules imposing a one metre space between people.

In Greater Libreville, markets (supermarkets, grocery stores, and other) are open all week for the provision of food supplies

Gabon has been able to defy the more calamitous predictions of the virus's impacts and avoid the situation faced in Europe and America

in strict observance of barrier measures, social distancing and the wearing of masks and gloves. Private companies that have special dispensation, and public and para-public administrations, can continue with essential activities such as operating shops, health services, funerary institutions, household waste collection companies, security companies and pharmacies, among others.

Since the implementation of the partial lockdown, the progressive reopening of some businesses unrelated to the provision of food supplies, such as hairdressing salons, dry cleaners, garages and car parts, maintenance and tyre shops, is allowed.

The right of assembly and protest is equally restricted. In fact, meetings and gatherings are prohibited throughout the national territory while in case of *force majeure*, any gathering cannot exceed 10 people. The restriction on gatherings applies to all public events, including marches and meetings, concerts, leisure and recreation sites such as beaches and sports grounds, traditional ceremonies, funeral wakes, wedding celebrations and family events.

Both the freedom of worship and the freedom to learn and teach have been affected by the mandatory closure of all places of worship, specifically the closure of churches and mosques, where the government has recommended individual home prayer, and schools and universities, as well as the prohibition of religious celebrations and processions.

Finally, all acts of resistance to orders issued by public authorities as part of the state of emergency are prohibited. Any refusal to comply or any manoeuvre aimed at evading confinement constitutes the offence of endangering others, in accordance with article 384 of the Criminal Code, and exposes the perpetrator to legal proceedings.

Employment

On March 20 2020, the Gabonese Minister for Employment, Civil Service, Labour and Vocational Training, in charge of Social Dialogue, issued a statement imposing limits on the operation of business activities to ensure that companies could function adequately and support the country's economy. The limits included the cancellation of all meetings, symposia and workshops of over 10 people, as far as possible; the implementation of a system of part-time, rotating and remote working practices, adapted as far as possible to the specificity of each sector; and the restriction and regulation of the flow of workers within companies. The supervision and regulation of working hours for workers in situations of vulnerability, disability and illness, as well as for pregnant women, has equally been encouraged.

These measures have been supplemented by Ministerial Order No. 0054/MEFPTFPDS which details the work conditions for private sector non-essential service businesses during the period of the Covid-19-induced State of Emergency. Pursuant to Ministerial Order No. 54, opening times for non-essential private sector services are fixed at Monday to Friday from 7.30am to 2pm. This corresponds to the normal legal working time, and in this way wages have been maintained at a normal level. However, staff whose work is reduced below the duration provided for above may be paid in proportion to the hours worked.

These measures do not apply to companies working on a permanent basis and those belonging to essential sectors as defined in Decree No. 106/PR/MEFPTFPDS of April 10 2020, which designates the essential services and personnel of the public, para-public and private sector during the period of the State of Emergency related to Covid-19.

Ministerial Order No. 54 also urges employers to enforce the compulsory wearing of masks by all workers and to implement all preventive and protective measures in the workplace by providing thermo-flashes, hydro-alcoholic gels at the entrance to offices, shower rooms equipped with soaps, posted information notes on the respect of barrier set ups and social distancing in the workplace.

Anticipating the difficulties that businesses would inevitably encounter, Order No. 0052/MEFPTFPDS (Order 52) was adopted on April 10 2020 by the Gabonese Minister for Employment, Civil Service, Labour, Vocational Training, in charge of Social Dialogue. It provides a set of specific measures relating to temporary lay-off periods that may be implemented by employers, following government decisions to combat the spread of the Covid-19 pandemic.

Companies are required to make a submission to the appropriate Labour Inspector, requesting the latter's opinion on the temporary lay-off. Each file must include (i) information on the company (*fiche circuit*, turnover, payroll, quarterly declarations of salaries to the CNSS and CNAMGS) and on the industry sector concerned; (ii) the impact of the measures on the continuity of the activity; (iii) the total headcount of the company; (iv) employees affected by the measure, with indication of their surname, name, seniority, age and pay slips; and (v) the cost of the temporary lay-off (temporary lay-off allowance payment). The Labour Inspector then has 72 hours to give his opinion. Failing that, the opinion shall be considered positive by operation of law.

The grounds for implementing temporary lay-offs must exclusively result from the protection and prevention decisions made to stop the spread of the Covid-19 pandemic.

Employees affected by the protection and prevention measures to combat the spread of Covid-19 pandemic are entitled to receive an allowance of at least 50% to 70% of their gross monthly salary, excluding bonuses and allowances. This allowance shall be paid under the same conditions as regular salaries. Furthermore, salaries of low-income employees with monthly salaries between XAF80,000 ($133) and XAF150,000 shall be maintained in full.

During the entire period of inactivity, employees are required to remain on standby and employers reserve the right to use them if required and according to their job. Any employees who refuse to do so forfeit their right to the allowance during the temporary lay-off period.

Despite the provision of specific measures on temporary lay-off, employers are encouraged, during this period, to give preference to maintaining salaries; promoting remote working, shift-work or part-time work at the company's expense; resorting to the recovery time mechanism; and asking employees to take their annual leave ahead of schedule.

Tax obligations and financial measures

The Gabonese government has reduced the business license tax (*patente*) and of the summary tax (*ISL – impôt synthétique libératoire*) by 50% for small businesses and introduced tax rebates (CIT) for companies preserving jobs and showing solidarity and exemplarity in the current crisis situation. It has also granted tax exemptions on exceptional bonuses to employees who work during the lockdown period and postponed the deadline for the submission of tax returns (DSF), annual salary statements (DAS), transfer pricing returns (DPT), personal income tax returns for taxpayers under the categories *Bénéfices Industriels et Commerciaux* (BIC), *Bénéfices Non Commerciaux* (BNC) and *Bénéfices Agricoles* (BA) to July 31. The government also provided relief on corporate income tax (IS) and personal income tax (IRPP) payments, with the option of paying in three equal monthly instalments on April 30, May 31 and June 30.

Gabon introduced a penalty-free moratorium on the due dates on debts owed to banks by any company that has ceased its activities or is in serious financial difficulty due to the crisis. The government also established an emergency financing desk, backed by XAF225 billion, to provide immediate relief, in the form of bank loans offered on preferential terms, to the urgent cash flow needs of businesses – subject to being up to date with their tax and social security obligations and to maintaining jobs.

To help contain the social effects of Covid-19, the government established a state fund endowed with XAF25 billion. The fund will support the most fragile and economically weak members of society by helping them pay water and electricity bills; suspending rents for people without income; providing free public ground transportation; granting food aid to people in distress and in emergency situations; compensating the losses of the small landlords resulting from the suspension of the payment of the rents; topping up salaries of between XAF80,000 and XAF150,000; and providing financial aid to Gabonese nationals stranded abroad.

Additionally, economically weak policyholders with National Health and Social Security Fund insurance will benefit from an exemption from co-payments/user charges for a six month period as of April 27.

Pandemic learnings

With the implementation of these measures from an early stage, Gabon has been able to defy the more calamitous predictions of the virus's impacts and avoid the situation faced in Europe and America. Two months after the first case of Coronavirus in the country, and at the time of writing, there were 1,004 infected people and nine dead in the country, with 162 recoveries. It seems clear that the measures implemented have helped contain the crisis from an early stage.

Nonetheless, a big challenge still lies ahead for the Gabonese economy as Gabon, an oil-exporting country, is facing a double blow from the impact of Covid-19 and from the drop in oil prices. Gabon must therefore simultaneously overcome these two challenges: one health-related and the other economic, with the latter being aggravated by the former.

In any event, the Covid-19 crisis has confirmed the need to rethink regional specialisation driven by globalisation. In fact, some countries have specialised in agricultural production, others in the export of natural resources, others in industrial production, or services, etc. Covid-19 demonstrates perfectly that this well-oiled approach could be jeopardised in the event of a pandemic as supply chains can be disrupted, potentially resulting in shortages of food supplies in some parts of the world and of equipment in others.

Should this approach change and economic diversity be prioritised at regional level, Gabon would certainly become a destination of choice for investment, insofar as it has set up free zones for industrialisation and still has under-exploited agricultural and fishing potential.

AFRICA MARKET MAKERS 2020

ANGOLA

Parallel battles

Tiago Marreiros Moreira of **VdA** and **Vanusa Gomes** of **ASP**, member of **VdA Legal Partners Network**, review Angola's battles with the double whammy of depressed oil prices and Covid-19, while steadfastly pursuing its privatisation programme

Compared with other African countries, Angola has managed to maintain political stability after the end of its 27-year civil war in 2002. Since the new government took office in September 2017, the country has faced several political changes and has become more assertive and shown a more steadfast commitment to compliance and anti-money laundering international best practice. However, the government's key challenge remains solving Angola's economic stagnation.

After the civil war, the country was able to achieve one of the highest economic growth rates in the world, thanks to its oil wealth. It became the second biggest oil producer in Africa and generated the third highest GDP in sub-Saharan Africa. However, in 2015 the economy was severely hit by the drop in oil prices and the fall in oil global demand and, since then, the economic situation has been critical. In fact, cuts to the state budget, currency devaluation and high inflation have slowed down imports and hindered economic growth in the past years.

It is well known that Angola has huge economic potential due to the abundance of important natural resources such as oil, gas, gold and diamonds. However, despite governmental reforms designed to stimulate the economy and create conditions for greater private sector participation in the economy, so far it has been challenging to attract foreign investment and leverage these resources, as well as to diversify the economy into other sectors.

This year is expected to be the fourth consecutive year of recession and the country battles through the worldwide crisis in the oil sector, which is now aggravated by the negative economic impacts of Covid-19. In just the past few weeks, at a time when the drop in oil prices and exports has put additional strain on the economy, the Angolan government has faced additional unique challenges.

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Lockdown measures put in place globally to contain the spread of Covid-19 represented an unprecedented shock to global oil demand, pushing oil prices down even further to their lowest historical levels. Oil companies suspended their production and the oil crisis will ultimately only be solved by a pick-up in global oil demand once lockdowns are lifted and the global economy is restarted.

Pandemic measures

To manage the Covid-19 outbreak, by the end of March 2020 the Angolan government had introduced a lockdown on the 28 million people living in the country, declaring the state of emergency for an initial period of 14 days, which has already been extended three times, between March 27 and May 25 2020.

Under Angolan law, the state of emergency can only be declared if a public disaster occurs or threatens to occur. In practical terms, the declaration of a state of emergency may involve the partial suspension of certain rights, freedoms and guarantees, such as a ban on travel or on certain personal or business activities. Presently, the following rights are suspended in full or partially: inviolability of the home; private property; private enterprise; freedom of belief, in its collective dimension; right of residency, circulation and migration; right of assembly and protest; right to inviolability of correspondence and communications; right to strike and other workers' rights; and freedom of worship, namely as regards religious events and gatherings. The authorities are further authorised to request detailed records of telephone calls, other support items and contact details from electronic communication operators, exclusively for purposes of tracing citizens suspected of being infected by, or confirmed cases of, Covid-19.

The lockdown measures implemented by the Angolan government include confinement measures and shelter-in-place orders, the closure of frontiers and the widespread establishment of handwashing stations in informal markets. These stringent measures implemented by the government to prevent the spread of Covid-19 have been deemed necessary and have been commended by the World Health Organisation (WHO). The Angolan response has been informed by an understanding of the magnitude of a pandemic and the need to take proactive steps, drawn from lessons from other countries, especially in Asia.

The government had to make difficult trade-offs by trying to find a proper balance between tackling the disease in a constrained health system and, simultaneously, addressing the negative impact of preventive measures on the economy, employment, incomes and food security of the population.

Additionally, the government also approved immediate measures to alleviate the negative economic and financial effects of the pandemic and to accelerate the process of economic diversification.

In this vein, the government adopted several measures for manufacturing companies that included extending deadlines on reporting obligations in respect of taxes and granting a tax credit to companies in respect of the amount of VAT payable on the imports of goods and raw materials used in the production of the 54 goods of the basic food basket. It also deferred the payment of social security contributions so that they may be paid in instalments and without interest.

The government implemented measures

to financially support minimum levels of activity for micro, small and medium-sized companies (MSME) in the manufacturing sector and to remove excessive bureaucracy affecting businesses, for example in the licensing of contracts relating to management, service provision and foreign technical or management assistance and the temporary suspension of all external tax audits by tax authorities.

Other measures were put in place for private individuals and for the protection of family welfare. For example, private sector employers must transfer to employees' salaries the amount of the discount to social security related to the months of April, May and June 2020; water and energy supply companies must not cut off supplies to customers who have difficulties paying their bills during the month of April; and campaigns were set up to distribute the basic food basket together with the provincial governments.

The government also implemented measures to promote the provision of credit to the real economy, while a set of measures were designed to boost the financing of projects of SMEs – with more favourable terms and conditions – for 2020. In addition, the government approved a financial package consisting of different credit lines with a view to help MSMEs in the services sector.

It is also worth mentioning other measures related to the obligations arising from bank loans. The recent regulations enacted by the government foresee that demands, delays and enforcement shall have no effect, by virtue of a delay in complying with obligations which may not be complied with as a result of the state of emergency. Also, bank customers may benefit from a 60-day moratorium to pay the instalments of their bank loans covering capital and interest. Banks are also prevented from modifying the amount of the instalments and must suspend all admonishments, constitution of customers in arrears and enforcement proceedings resulting from the delay in the compliance of the obligations to pay capital and interest, when such payments cannot be made as a result of the impact of the Covid-19 pandemic.

Privatisation and the pandemic

It is important to highlight the recent efforts made by the government to accelerate the privatisation program (Propriv). Propriv seeks to reduce the influence of state-owned companies in the economy and increase, diversify and ensure self-sustainability in terms of expected gains and liquidity for the Angolan National Treasury. The companies to be privatised include state-owned companies and companies in which the state has a direct or indirect holding, with majority or minority positions, in the following sectors:

- Mineral resources and petroleum
- Telecommunications and IT
- Financial sector: banking, insurance and capital market companies
- Transportation
- Companies in the Special Economic Zone (ZEE)
- Tourism and industry (including agribusiness)

Propriv's strategic companies include important telecom and IT companies, such as Unitel, Angola Telecom, Angola Cables and MSTelecom, major banks as Banco BAI, Banco de Comércio e Indústria (Banco BCI) and Banco Económico and insurance companies including Ensa, as well as the Bodiva stock exchange, mineral and oil companies such as Sonangol and Endiama, airline companies like TAAG and Sonair, industrial companies such as Nova Cimangola, Secil, Biocom, Cuca e EKA and construction companies as Mota-Engil Angola, among others. The privatisations will be implemented through open and limited public tenders, capital market offerings (initial public offerings) and auctions of indivisible blocks of shares offered to pre-selected investors (stock auctions) or, as contemplated in the Privatizations Framework Law, a mix of all the above.

Through Presidential Order No. 66/20 of May 5, Banco BCI's privatisation was recently launched and will be carried out under the Stock Exchange Auction regime, addressed to specially qualified candidates. According to a recent government announcement, some interested parties have already been identified, with expressions of interest received from certain domestic and foreign investors, all with experience in African markets. The timetable established for Banco BCI's privatisation is still expected to take place in 2020.

It is not difficult to anticipate what trajectory the Covid-19 outbreak will follow in Angola. The Covid-19 pandemic will undoubtedly depress the economy and the slowdown will trigger revenue declines for small businesses and larger companies operating in the country.

Corporate makeover

Nelson Raposo Bernardo, Joana Andrade Correia and Júlio Martins Júnior of Raposo Bernardo review Cape Verde's recently revamped and modernised corporate finance framework, which provides a swathe of new financial supports and aims to supercharge MSMEs

Cape Verde's government has recently put in place important institutional, legal and contractual instruments and mechanisms for investors with the aim of helping to promote and encourage the corporate finance sector.

At the institutional level, the government has created Pró Empresa (Decree Law No. 22/2017 of May 17), a public institution that aims to promote, facilitate and monitor investments into micro, small and medium-sized enterprises (MSME) across the country.

Pró Empresa's remit is to sponsor research into the private investment conditions that affect MSMEs and use the research in consultation with competent entities to propose beneficial measures for the sector. Its goal is to publicise and promote the opportunities and advantages private investment can bring to the production of goods and services and to facilitate, guide and support MSME investors by providing them with all the information they need relating to private investment in Cape Verde. The authority offers a one-stop-shop for client services and serves, more broadly, to coordinate client services by working in close cooperation with venture capital entities and credit guarantee institutions. Its overarching goal is to support and promote investment programmes for MSMEs.

In addition to Pró Empresa, companies can benefit from the Pró Capital mechanism (Decree Law No. 28/2017 of June 30), which facilitates investments into the share capital of any public and viable company which is in a difficult financial situation. The mechanism's goal is to promote the recovery of such companies as well as facilitate participation in the share capital of start-ups. Participation in the share capital of companies under this mechanism is capped at 10 years.

At the institutional level, the government has created the *Sociedade de Garantia Parcial de Crédito* (Pró Garante) (Decree Law No. 32/2018 of June 15). Pró Garante is a public financial

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Some of his recent transactions include advising BNP Paribas on an aircraft portfolio financing; Helios Investment Partners in the acquisition of Fertilizers and Inputs Holding, held by Louis Dreyfus; Mitsubishi Corporation Bank on international credit operations; Japan Bank for International Cooperation in operations regarding export loan agreements; Rabobank for financing operations of Ferry Boats; General Electric for a power wind farm project; and Barclays Bank and Caixa Bank in a banking syndicate with another 15 banks for the refinancing of an international construction group.

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Júlio has led and been involved in major international investment projects. His recent transactions include advising over 30 banks operating in the country on financing contracts for large infrastructure and equipment; acting as counsel to the largest private bank in Cape Verde; advising Iceland Air Group on the privatization of the national aviation company TACV, still the largest privatisation in the country;assisting on the financing process of the project to construct the second submarine cable connecting South Africa, Cape Verde and Portugal operated by CV Telecom; and advising China Construction Bank on a loan agreement for an international credit transaction.

He has been part of the teams drafting some of the most recent legislation packages for Cape Verde.

institution subject to the supervision of the Central Bank of Cabo Verde whose goal is to facilitate access to financing for MSMEs by offering credit guarantees, which will promote growth in each business sector and boost the sustainable development of the national economy.

Pró Garante has a range of tools at its disposal. It can grant guarantees to eligible credit institutions, regulated and supervised by Central Bank of Cabo Verde, to facilitate credit lines to companies. It can offer portfolio guarantees of special credit lines to ensure compliance with the obligations assumed by companies with entities that provide the special credit lines. Pró Garante can also offer counter-guarantees to the operations of other eligible financial institutions that are dedicated to providing credit guarantees to companies, as well as administer, on behalf of third parties, guaranteed funding aimed at improving access to corporate finance. A final key tool is that it can support the expansion and dissemination of other financial instruments that can further improve access to finance for companies.

These institutions and mechanisms have been created recently to promote business, facilitate risk capital and guarantee financing operations with credit institutions.

Another important legislative novelty introduced in Cape Verde that may have a strong impact on corporate finance developments is the new legal regime that governs crowdfunding or collaborative financing (Law No. 34/IX/2018 of 6 July). This is a very recent corporate finance alternative in Cape Verde and has already attracted investors' attention.

The framework provides a versatile corporate finance mechanism, which consists of:

- collaborative financing through a donation, whereby the financed entity receives a donation with or without the delivery of a non-pecuniary counterpart;
- collaborative financing with reward, whereby the financed entity is obliged to provide the financed product or service, against to the financing obtained
- collaborative capital financing, whereby the financed entity remunerates the obtained financing through participation in the respective share capital, distribution of dividends or profit-sharing; and
- collaborative finance, whereby the financed entity pays the financing obtained through the payment of interest fixed at the time of the fund raising.

Crowdfunding has proven to be especially useful in the financing of start-ups and SMEs, specifically those that are developing activities and projects in innovative areas. It is an instrument that also presents advantages that are not strictly financial, for instance it has a strong marketing effect by promoting businesses on its platform and by interacting on social networks.

Looking ahead

The implementation of these regulatory frameworks is expected to boost corporate finance activity over the short to medium term, especially in the period where markets begin to emerge from Covid-19. It should be noted that the Government of Cape Verde has also implemented other kinds of measures to inject more liquidity into the Cape Verdean economy (Decree Law No. 38/2020 of 31 March). These measures include the creation of credit lines to support corporate treasury, a bank financing moratorium, tax reductions and exemptions and a tax moratorium. Most companies have resorted to the bank financing moratorium. During the moratorium period, beneficiary entities may request to have capital repayments wholly or partially suspended.

If a company requests a moratorium this request cannot be treated, in any way, as a breach of any of the contractual obligations agreed with the banks, nor can it activate early maturity clauses or the suspension of interest due during the moratorium period – which will be capitalised in the loan amount with reference to the time when they are due at the current contract interest rate – or terminate any guarantees.

To inject liquidity into the economy, the government also opened up the possibility for companies to obtain bank financing with partial guarantee from the Cape Verdean state.

These sets of instruments will certainly provide companies with interesting investment opportunities and with the advantage that there are no restrictions in terms of the sector of activity, so they are available to companies operating in tourism, industry, services, agribusiness, energy, and every other sector. As a result of these developments, companies operating in Cape Verde have at their disposal important modern corporate finance instruments, namely venture capital, partial guarantee from the state or state-owned companies and crowdfunding in its most diverse modalities.

Traditional sources of corporate finance, including equity capital raising techniques, are provided for in the Cape Verde Companies Code, in addition to the financing possibilities mentioned above. In the first step of an equity financing, the partners of a company can subscribe to additional share capital in the primary market. In this instance, the shareholders will benefit from the distribution of dividends and the balance settlement. The shareholders can then also be called on to finance the company through a hybrid model, specifically by means ancillary payments and supplementary payments, which constitute financing through debt instruments.

To that extent, we conclude that Cape Verde has made available a wide range of corporate finance instruments to companies, which can be complementary and represent an important stimulus to entrepreneurship, innovation, and research and business development.

Companies have been attentive to these opportunities and the legal framework recently introduced in the area of corporate finance has contributed not only to a change mentalities, but modernised business practices, allowing Cape Verdean companies to have access for the first time to financial resources that have not previously been available.

AFRICA MARKET MAKERS 2020

MOZAMBIQUE

Natural wealth

Mozambique was well prepared for the Covid-19 pandemic. The country responded quickly and is now targeting growth for 2020, based largely on natural resource projects, write **Tiago Marreiros Moreira** of **Vieira de Almeida (VdA)** and **Guilherme Daniel** of **Guilherme Daniel & Associados**

It is difficult to remember the last time countries had to face, at the global scale, a threat that raised so much uncertainty regarding what to expect from the future and what the new normal will look like. Let us hope Covid-19 has alerted us all to the worlds' volatility and to the need of more collaboration between countries and people from all continents.

With a history of numerous crises following the end of the civil war, including repeated natural disasters – cyclones Idai and Kenneth in 2019, the floods of 2000, recurring droughts and floods, and repeated cholera outbreaks and pandemics – Mozambique has been well prepped to respond quickly and effectively to a health crisis such as the Covid-19 pandemic. It is a pandemic that required an immediate response and a mobilisation of means to provide medical and humanitarian assistance, even when available resources are limited. Mozambique could do this mainly because it has put in place a monitoring mechanism to respond and manage calamities, coordinated by the National Calamity Management Institute (*Instituto Nacional de Gestão de Calamidades*), an organisation that is present across the country and that is permanently vigilant and on call.

Mozambique announced its first Covid-19 case on March 22 and by May 12, it had a total of only 103 reported positive Covid-19 cases, most of them located in Maputo and in the Cabo Delgado province, and still with no human casualties.

Even if some construction works had to be suspended and several expatriate workers were forced to leave the country, the promising $20 billion LNG project in northern Mozambique, Africa's largest LNG project, seems to continue on track, focused on keeping its critical activity. The Mozambique LNG plant may start its operations by 2024, aiming to produce 12.9 million tonnes per annum (Mtpa) of LNG, most of it already sold to Asian and European buyers.

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The Mozambican government was quick to adopt a series of measures to prevent the spread of the virus. These included limiting the movement into and out of the country, restricting gatherings, reducing the number of workers in the public and private sectors, and declaring the mandatory use of masks in public spaces. The measures seem to have produced positive results up to this point in the fight against the coronavirus. However, like in all countries affected by this pandemic, the coming months will reveal the real impact of the measures on people's lives and on the economy of this resilient, beautiful and promising sub-Saharan African Lusophone country.

Although the impact is far from negligible, one could say that so far Mozambique's experience and prospects remain positive. Acting together with other countries in the region, Mozambique was able to ensure a relatively normal supply of food and other essential products despite restrictive measures that included a lockdown in South Africa, Mozambique's main supplier, which had a positive impact on social stability.

Horizons of promise

The government submitted a draft Plan and Budget for 2020 in April. The timing is explained by the fact that this government was elected in the October 2019 general election and took office in January 2020. The drafts were prepared taking account of Covid-19's potential impact and approved by parliament on April 16. Although the main economic indicators were adjusted downwards, the drafts are still optimistic regarding the country's economic performance during the Covid-19 year.

The government foresees a 2.2% GDP growth as opposed to the initial 4% forecast, a 6.6% increase of the inflation rate as opposed to the 4.4% increase in 2019 and a 6.5% drop in imports when compared to 2019.

Despite specific measures to diversify the economy, particularly in the agriculture, tourism and other sectors, the nature and role of the mining sector in the structure of the economy is indisputable: the Rovuma basin natural gas projects remain the greatest hope for Mozambique's socio-economic transformation in the coming years. While it is public knowledge that the final investment decision regarding the Rovuma Basin Area 4 onshore project led by Exxon and ENI has been pushed back, the preparatory work for the Total-led Rovuma Basin Area 1 project shows no signs of slowdown, apart from the limitations imposed by Covid-19, both as regards the start of the construction phase and the completion of the contractual package to close the financing.

Pursuant to Council of Ministers Decree 102/2019, of December 31 2019, the government approved the terms of the guarantee to be provided as part of the Golfinho-Atum LNG project and a debt offering issue by the Minister for Finance of a financial guarantee, capped at $2.25 billion, to cover the share of the risk inherent to the Empresa Nacional de Hidrocarbonetos's (ENH) participation in the financing that the lending parties will grant to the project.

Work also continues for the start of production on the (offshore) Coral project, set for 2021. This project is in the Rovuma Basin but is smaller in scale to the others. There is no evidence that the schedule will change significantly beyond the delays directly arising from the restrictions imposed by Covid-19.

The country's assorted resources will continue to play a significant role in attracting investment, in particular foreign direct investment (FDI) in the energy, agriculture and tourism sectors, but Mozambique needs to focus on strengthening its regulatory, legal and institutional competitiveness to facilitate such investment effectively.

Such optimism must be coupled with specific and significant impact measures to keep businesses operational in the short term and sustainable in the medium and long term, especially for small and medium-sized enterprises (SMEs) responsible for most jobs in the country. More than directly financing the economy (its budgetary constraints being well known), the government is expected to be quick in adopting legislative measures or in establishing derogations to mitigate the impacts of the crisis on SMEs. These will have to include easing the labour legislation to enable the adoption of temporary derogatory measures by agreement between employers and employees.

Although alleged terrorist groups have been perpetrating serious acts of violence in the Cabo Delgado province, the consolidation of peace and the use of political means to resolve conflicts, particularly in the relationship between the two major political parties, is remarkable. The consolidation of the peace process will be a great contribution to strengthen the country's competitiveness, which will go a long way to stimulating a few key sectors of Mozambique's economy, including national, regional and international tourism.

AFRICA MARKET MAKERS 2020

SÃO TOMÉ AND PRÍNCIPE

Sharpened focus

Joana Andrade Correia and Júlio Martins Júnior of Raposo Bernardo review São Tomé and Príncipe's recent efforts to overhaul and streamline its investment framework, including the establishment of a flagship One-Stop Office

RAPOSO BERNARDO

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São Tomé and Príncipe is strategically located in the Gulf of Guinea region, in close proximity and with easy access to the West Africa market. The Government of São Tomé and Príncipe is working to achieve sustainable economic development for the country, adopting policies to develop the free trade area and the circulation of people, goods and services and to resolve restrictions associated with non-trade barriers. São Tomé and Príncipe is entering a new epoch of its development, taking advantage from its natural, human and financial resources and also its political stability.

Foreign investment plays an important role in this process and is vital for the economic growth and development of São Tomé and Príncipe.

There are several potential sectors for investment and they include agriculture, livestock, industry, fisheries, infrastructure, services and energy.

To stimulate and develop the private sector, São Tomé and Príncipe has approved a set of legislative measures that establish favourable conditions for foreign investment and improve the country's business environment. One of the key pieces of legislation in this package to attract foreign investment was the implementation of a new São Tomé and Príncipe Investment Code (Decree-Law 19/2016 of November 17 2016) and the creation of a One-Stop Office (Decree-Law 37/2009 of October 13) for the incorporation of companies. There are also some other important new laws related to the protection of industrial property rights, tax benefits, foreign exchange and labour relations.

São Tomé and Príncipe's private investment policy is built on several general principles. These include a respect for private property, for the rules of the free market and healthy competition between economic agents and for free initiative, except in areas defined by law as being reserved for the state. The policy guarantees security and protects investments,

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Recent work includes advising Icelandair Airlines on the privatisation of the National Airline of Cape Verde; Iberostar Hotels and Resorts Group in its business incorporation in Portugal and opening of two hotels; Deutsche Bank in the negotiation and preparation of a bank financing agreement relating to the acquisition of commercial aircrafts; China Africa Development Bank on financing of investments in infrastructure and construction projects; Afreximbank on the financing of the construction of a Hilton hotel; and Elix Capital on transactions involving airlines and aircraft leasing companies, acquisitions and leveraged financings.

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Júlio has 15 years of experience in corporate law and finance related operations, namely in relation to sales and acquisitions of shares and assets, financing operations, licensing and regulation and M&A.

Júlio has led and been involved in major international investment projects. His recent transactions include advising over 30 banks operating in the country on financing contracts for large infrastructure and equipment; acting as counsel to the largest private bank in Cape Verde; advising the national aviation company TACV, still the largest privatisation in the country; assisting CV Telecom on a project to construct the second submarine cable connecting South Africa, Cape Verde and Portugal; and advising China Construction Bank on a loan agreement for an international credit transaction.

He has been part of the teams drafting some of the most recent legislation packages for Cape Verde.

guarantees equal treatment between national and foreigner investors and guarantees the promotion of the free movement of goods and capital, according to the law. It also pledges to respect and comply fully with international agreements and treaties.

Practical considerations

As a rule, São Tomé and Príncipe allows freedom of private investment, without it being subject to any authorisation or approval by the authorities. Nevertheless, for investments in economic activities that may contribute to the development of São Tomé and Príncipe and have a minimum value of €50,000, the investor and state may enter into an Administrative Investment Contract, regulated by the São Tomé and Príncipe Investment Code (Investment Code), which establishes the terms, conditions, forms, guarantees and incentives applicable to the investments made in the country.

The types of investments that will be subject to the Investment Code are broadly defined and may consist of several different activities. They include the transfer of financial resources from abroad or the application of own funds, and the application of foreign currency kept in bank accounts in São Tomé and Príncipe; the importing of machinery, equipment, accessories and other physical assets; the application of credit and other private investor funds that are intended to finance entrepreneurial activities; the application of technology and know-how; the creation of new companies exclusively belonging to the private investor; the development of real estate projects, tourist-focused or not, regardless of the legal nature they assume; and corporate finance, etc. These investments will also be eligible to incentives under the Tax Benefits Code.

The Investment Code offers three investment regimes:

- Simplified regime – for investments valued between €50,000 and €249,999
- General regime – for investments valued between €250,000 and up to but not including €5 million
- Special regime – for investments worth €5 million or more

The value of the investment determines the types of tax incentives and benefits available to the investors.

Private investment projects are subject to an investment agreement (Administrative Investment Contract) through which investors benefit from a unique package of perks, including: investment protection, particularly with regard to compulsory purchases; a guaranteed right to expatriate the proceeds of the investments abroad, such as royalties, profits and dividends; the right to import goods directly from abroad and to export the products produced; a guarantee of non-interference by the state in the management of privately-owned enterprises; the possibility of the provision of land necessary for the development of a project; and the abovementioned possibility of tax and customs concessions.

The Tax Benefits Code (Decree-Law 15/2016 of November 17 2016) grants investors general and special benefits and incentives. Certain incentives are granted automatically while others depend on further action by the investor and recognition by the authorities.

The general incentives include:

- An exemption from import duties for goods and equipment used for new activities or the expansion of existing activities (provided that the relevant goods and equipment cannot be sourced in São Tomé and Príncipe).
- A corporate income tax rate of 10%.
- Accelerated depreciation and amortisation for investments in the tourism, education, health, new technologies and export sectors (it consists of applying twice the normal rates, legally fixed for the calculation of depreciation and amortisation considered as costs attributable to the fiscal exercise in determining the taxable income).
- Tax deductions for investment in specialised equipment for the development of activities that are authorised under the Investment Code during the first five years of activity.
- Tax deductions for training costs of São Tomé and Príncipe staff.
- Tax deductions during the first five years of activity of costs relating to the construction and restoration of roads, water supply, electricity, energy, schools, hospitals and other public works. These deductions amount to 150%, if the activities are in the districts of Cantagalo, Lembá, Lobata, Caué or in Príncipe; and 100%, if the activities are in the other districts.
- Exemption of stamp duty during five years in case of amendment of articles of association.
- Exemption from SISA tax on acquisition of real estate.

In addition to general incentives there are also some special tax incentives for investments in agriculture, agro-industries, livestock and fisheries sectors. These include an exemption from import duties of goods and equipment; a 50% reduction of the corporate income tax rate for the first seven years of the project's implementation; and 0.2% stamp duty tax on banking operations in connection with the import of foreign capital.

The hospitality sector can also tap into special incentives, which target the restoration, construction, expansion or modernisation of hotels and related establishments and the development of rural and eco-tourism. Companies involved in international trading receive specific advantageous tax treatment and are subject to a flat income tax rate of 5%.

Furthermore, the Tax Benefits Code provides that additional incentives are available for high value projects exceeding $10 million.

Future hopes

Of all these legislative developments one the most relevant measures implemented in São Tomé and Príncipe is the creation of the One-Stop Office for the incorporation of companies, which simplifies the procedure of incorporating and registering a business. The One-Stop Office provides investors with the different legal forms for companies that can operate in São Tomé and Príncipe and which can be used as vehicles for investments, such as the limited liability company (SA) and the private (and single-member private) limited liability company.

São Tomé and Príncipe now has the minimum legal and institutional measures in place to welcome all investors intending to do business in this unique market, taking advantage of both its strategic location and natural resources.


China Outbound Investment
Special Focus 2020

CHINA OUTBOUND INVESTMENT SPECIAL FOCUS 2020

SWITZERLAND

Uncertain futures

Philippe Weber, Manuel Werder, Daniel Eisele and **Elga Reana Tozzi** of **Niederer Kraft Frey** review the Swiss investment framework and the foreign investment control law that Covid-19 has put on ice

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Switzerland implemented a broad range of measures for businesses in response to Covid-19, including restrictions on certain commercial, border crossings and gatherings exceeding a certain number of people. However, as the situation has stabilised, the Swiss government has adopted a step-by-step plan to lift many of these restrictions. Importantly, the Swiss government was quick to decide on a robust package of government aid (including government-backed credit, short-time work allowances, etc.) which thanks to characteristic Swiss efficiency reached businesses without delay and bureaucratic hurdles.

Swiss and foreign-owned Swiss domiciled companies with a turnover in 2019 of less than CHF500 million ($515 million) that have been significantly adversely affected by Covid-19 can obtain loans of up to a maximum of 10% of their revenue or a maximum of CHF20 million. Swiss commercial banks are required to pay out up to CHF500,000 per company upon request without any further requirements and the federal government will act as a guarantor for the full amount. Interest on these loans is 0.0% per annum. For loan amounts exceeding CHF500,000, the federal government will act as a guarantor for 85% of the principal amount of the loan. Interest on the 85% of the principal amount of these loans is 0.5% per annum. Interest on the remaining 15% is subject to negotiation with the bank. Further support packages involve financial support to start-ups and extended support to businesses in form of short-term work (i.e. part-time unemployment) compensation.

Regardless of this support, the environment makes any predictions about Chinese inbound investment into Switzerland very difficult to make. The increasingly uncertain business outlook in general may result in decreasing prices for targets. However, a less attractive seller market may also result in fewer targets being available.

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Manuel Werder's practice focuses on corporate law and domestic and cross-border M&A transactions, including corporate restructurings and private equity and venture capital transactions. His expertise also includes commercial, contract, securities and stock exchange law issues. He has considerable experience advising Chinese parties, in particular on cross-border M&A transactions. He has advised Chinese clients in a great number of acquisitions relating to Swiss target companies and other matters and Swiss and international clients in connection with investments in China.

Ease of investing

Switzerland's attitude to foreign investors, including Chinese investors, is generally open and favourable. Unlike in the EU, no investment control measures have yet been introduced. However, in March 2020 the Swiss parliament asked the government to draft a law on foreign investment controls. The content of the proposal is not yet known and given the current environment it is uncertain whether parliament will introduce a foreign investment controls act at all. In any event, the entry into force of such an act within the next 12 months is highly unlikely.

The following factors motivate Chinese companies to undertake M&A transactions with Swiss companies:

- Switzerland offers economic, legal and political stability and security and benefits from an efficient and reliable administration, which has been in evidence during the Covid-19 crisis where the Swiss government reacted quickly, efficiently and in a measured manner; Switzerland was among the first countries to approve and effectively roll-out state aid;
- the Swiss legal and regulatory framework is favourable for M&A transactions with Chinese buyers (as further described below, there is a double taxation agreement between China and Switzerland and, so far, the free trade agreement between China and Switzerland is one of only few such agreements that China has concluded with a continental European country);
- Switzerland is rich in human capital and offers reliable and well-educated employees;
- M&A transactions with Swiss companies allow for an efficient inroad to advanced technical know-how;
- the acquisition of companies in Switzerland offers Chinese groups relatively quick and easy access to the Swiss market;
- it is a good way to acquire recognised brands (for example in technology or luxury goods), which may provide legitimacy in the Swiss, European and even global markets;
- Chinese buyers have the potential to increase the value of acquired Swiss companies (for instance by using valuable access to the Chinese and other markets).

In transactions involving Swiss companies that are listed on a stock exchange or are regulated (for instance financial institutions), proper disclosure of the Chinese buyer's ownership structure and regulatory status is becoming increasingly important, as evidenced by recent public cases, including that of HNA.

Overall, however, there are no Swiss laws of general application prohibiting foreign investments in Switzerland or subjecting them to prior approval. Therefore, foreign investors generally do not need formal approval for their investments in Switzerland and no special governmental authority monitors foreign investments. Foreign investments in certain regulated industries might require governmental permission. The competent authority and the approval process and timings depend on the specific industry.

Regulatory considerations

Investment restrictions do exist in certain sectors, and while as a rule the government is not entitled to golden shares, it may make approvals or licensing subject to certain conditions.

Financial market laws mean that if foreign nationals have a controlling influence over a bank, a securities trader or certain other prudentially supervised entities active in the financial sector (finance companies), the granting of a licence by the Swiss Financial Market Supervisory Authority (Finma) is subject to additional requirements. Among other things, the corporate name of the legal entity must not suggest that the entity is controlled by Swiss persons. Further, the country – or countries – where the ultimate owner of the controlling interest is domiciled must grant reciprocity (which is the case if the relevant state is a member of the World Trade Organisation). Finma may impose additional conditions to the licence.

Acquisitions of residential, but not commercial, real estate in Switzerland by foreign or foreign-controlled persons is

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subject to strict limitations under the Lex Koller. Such properties can only be acquired if authorisation is granted by the competent cantonal and federal authority(ies). Authorisation is not easily obtained and may take several weeks, if not months, to obtain.

The relevant licensing authorities can also refuse to grant a licence to companies incorporated under foreign laws under the telecommunications act for radio communication licences, the nuclear act for nuclear power plants, the radio/TV act for broadcasting licences and the aviation act for the professional transport of passengers or goods, unless reciprocal rights are granted to Swiss persons by the respective foreign states. In the aviation sector, an aviation company headquartered in Switzerland must be under the actual control of Swiss citizens.

Further investment restrictions apply in the following fields: air transportation; public transport (railway, cable cars, shipping); TV and radio; post and telecommunications; energy (especially nuclear energy); specific professions such as university medical profession, lawyers etc.; minerals, raw materials and mining; health services and products; casinos and gaming; private security services; and weapons and war material (including dual-use goods).

Competition clearance is another key regulatory consideration. The authority is the Swiss Federal Competition Commission (Comco). In the event of a merger or takeover of a Swiss bank which is considered necessary for reasons of creditor protection, Finma will replace Comco as the competent authority.

In the merger or acquisition of a controlling stake, Comco needs to be notified prior to deal closing if, in the last accounting period before the transaction the enterprises concerned reported a joint turnover of at least CHF2 billion or a turnover in Switzerland of at least CHF500 million; and if at least two of the enterprises concerned reported an individual turnover in Switzerland of at least CHF100 million. Special thresholds apply for banks and insurance companies. Filing needs to be done after the signing of the relevant agreement but prior to closing. On receiving notice of a transaction, Comco must inform the parties within one month whether it will open a formal investigation. If Comco does not inform the parties within that period, the transaction can proceed without reservation. If an investigation is opened, the parties cannot close the transaction. Comco must then complete the investigation in four months.

As a rule, and unless a licence stipulates otherwise in its terms, an increase in an investment will not trigger additional approval requirements unless the foreign investor newly acquires a controlling interest through the increase. For banks, securities traders and certain other prudentially supervised financial institutions, any increase of a participation exceeding a threshold of 10%, 20%, 33% or 50% of the capital or voting rights must be notified to Finma. The same applies if a foreign investor decreases / exits its investments in such a company. As a rule, there are no exit obstacles and the repatriation of profits and capital is possible.

As for currency regulations, as a principle unrestricted amounts of liquid funds, for instance cash, foreign currency and securities (bonds and cheques etc.), can be imported into Switzerland, brought through Switzerland in transit or exported from Switzerland. In the context of combating money laundering, certain declaration obligations (purpose, beneficial owner etc.) may arise, for example when transferring higher sums of money in foreign currencies or in the case of cross-border cash movement exceeding CHF10,000. To date, Switzerland has taken a very liberal approach to cryptocurrencies. For example, stock companies have been incorporated using cryptocurrencies to pay the company's capital.

Investment structures

The most common legal entities for inbound investments are stock companies (AG) and limited liability companies (GmbH). Both have capital divided into shares and limited liability. They are both suitable for operational and holding purposes. Listed companies are usually constituted as AGs. In addition, certain special forms of investment company (the Sicaf and the Sicav) are subject to the Collective Investment Schemes Act (Cisa). Sicaf is an investment company with fixed capital (close-ended) with the sole purpose of collective investment. Sicav is an investment company with variable capital (open-ended) whose capital is divided into entrepreneurial and investor shares. Sicafs and Sicavs are regulated by Cisa and supervised by Finma. As a non-corporate vehicle under the scope of Cisa, limited partnerships (LPs) are often used for collective investment.

These entities must be domiciled in Switzerland, must have the required minimum capital (CHF100,000 for an AG, CHF20,000 for a GmbH) and must be represented by at least one individual domiciled in Switzerland. Additionally, publicly traded companies and companies that exceed certain thresholds with respect to total assets, turnover or number of employees must have an auditor. If changes occur – such as amendments to the articles of association, changes in the company's capital structure or changes in the authorised representative – the competent commercial registry must be kept up to date. For Cisa-governed entities, various financial market regulations must be observed.

Dispute resolution

Parties often include an arbitration provision in their contractual documents for international commercial agreements governed by Swiss law. Arbitration is generally seen as the most efficient dispute mechanism for large, cross-border disputes. Whereas the parties to commercial agreements may sometimes also agree on an arbitration clause of the International Chamber of Commerce (ICC) or another arbitration institution, the most commonly used arbitration rules are the Swiss International Arbitration Rules of the Swiss Chambers' Arbitration Institution.

Switzerland has also signed over 120 bilateral investment protection treaties (BITs). According to the United Nations Conference on Trade and Development (UNCTAD), Switzerland has the third largest network of these treaties after Germany and China. The current BIT between Switzerland and China was signed in 2009 and has been in force since April 13 2010.

Where parties wish to agree on state courts, it is important that the jurisdiction clause refers to the competent courts of a certain city or canton, and not simply to the "ordinary courts in Switzerland", which would not be considered a valid choice of jurisdiction.

The Swiss court system is relatively efficient and the quality of the state courts is normally high. Depending on whether a court case involves an evidence proceeding and/or is of a cross-border nature (and may even involve judicial assistance proceedings), the duration of a proceeding varies substantially. Normal first instance proceedings may take one to three years. There is then an appeal proceeding before the highest cantonal court which usually takes one to two years. A decision by the highest cantonal court is generally subject to appeal to the Swiss Federal Supreme Court. Such appeal to the Swiss Federal Supreme Court has only suspensive effect in exceptional cases.

Foreign claimants should note that they may be required to provide security for costs upon request of the counterparty in state court proceedings.

Apart from having an efficient court system, Switzerland also remains, as indicated above, one of the foremost jurisdictions for arbitration. This position is the result of its liberal legal framework as well as its extensive and arbitration-benevolent case law and doctrine. In this regard, foreign investors should be aware that Swiss BITs systematically contain diagonal arbitration clauses, allowing investors to initiate arbitration directly against Switzerland. Most of these clauses provide for ad-hoc or International Centre for Settlement of Investment (ICSID) arbitration, while many others provide for ICC arbitration.

Sports related arbitration is also very important, as over half of all international sports federations have their seat in Switzerland. The Court of Arbitration for Sports domiciled in Switzerland regularly deals with international sports cases, such as the recent case between the Chinese swimmer Sun Yang and the International Swimming Federation.

Swiss courts will generally respect foreign judgments by a competent court, including by a Chinese court, unless the foreign court violated due process requirements or rendered a decision that is contrary to Swiss public policy. One of the key objections that a defendant can make in such an enforcement proceeding is that the foreign court was not competent to decide the matter. The enforcement of judgments rendered in countries of the EU, Norway and Iceland is governed by the Lugano Convention, which harmonises the conditions for enforcement and applicable procedures.

Foreign international arbitral awards are recognised and enforced in Switzerland on the basis of the New York Convention, regardless of reciprocity. Foreign ICSID investment arbitration awards will be recognised and enforced pursuant to Article 54 (1) of the ICSID Convention, which stipulates that ICSID awards will be enforced as though they were the final judgments of a domestic court.

Enforcement of Swiss court judgments abroad can generally be expected in those jurisdictions with which Switzerland has an agreement for the reciprocal enforcement of judgments. Since Switzerland is a signatory state of the Lugano Convention, Swiss court judgments are generally enforceable in all EU countries, as well as in Norway and Iceland. Whether a Swiss judgment is also enforceable in a particular foreign jurisdiction in the absence of a bilateral or multilateral agreement will depend on the local laws of that jurisdiction.

Arbitral awards rendered in Switzerland can generally be expected to be enforced in those jurisdictions that are signatories to the New York Convention. ICSID investment arbitration awards rendered in Switzerland will generally also be enforceable in all states that are signatories to the ICSID Convention.

The tax factor

A withholding tax (WHT) of 35% is levied on dividend payments. The WHT is paid by the distributing company. The repayment of share capital and capital contribution reserves is exempt from dividend WHT (special repayment rules will apply for Swiss listed companies as of 1st January 2020).

There is a double taxation agreement in place between Switzerland and China (DTA-PRC) which follows the OECD Model Tax Convention. Based on the DTA-PRC, the residual WHT rate on dividends amounts to 10%, meaning that 25% could be refunded. Under the net remittance procedure, dividends distributed to a Chinese holding company on a substantial participation of 25% in the capital of the distributing Swiss company could be reduced to a residual treaty rate of 5% based on the DTA-PRC.

No WHT is levied on interest payments on intra-group and shareholder loans. A

WHT of 35% is levied on bank and bond interest. Based on the DTA-PRC, the residual WHT rate amounts to 10% on such interest. Due to the beneficial DTA-PRC, there is no benefit in using intermediary tax jurisdictions.

Corporate income taxes have three levels: federal, cantonal and municipal/communal. The federal corporate effective tax rate equates to 7.83%. The applicable cantonal/communal tax rate depends on where the company is tax resident. Switzerland, as a confederation comprising 26 cantons, has no standard tax rate.

Following a substantial corporate tax reform that became effective on January 1 2020, the cantons have reduced or will reduce their corporate tax rates substantially. For the 2020 tax year, the Canton of Bern has the highest effective tax rate of about 21.61% (given the tax reform is not yet in place). On the other hand, the Canton of Geneva only has a tax rate of about 14.0%, when pre-tax reform it was about 24.16%. The most attractive cantons are the Canton of Zug, with an effective tax rate of 11.91% (especially if you take into account that the travel time between Zug and Zürich is only about 20 minutes) or the canton of Lucerne with an effective tax rate of approx. 12.32%. The Canton of Zürich has an effective tax rate of 21.15%, which will be reduced in the 2021 tax year to 19.71%. There is also an annual capital tax at a cantonal level due on the net equity of between 0.0717% and 0.4008% on net equity.

Since July 2016, Switzerland has applied revised regulations regarding the Swiss federal tax holiday scheme. The revised legislation provides for relief from federal corporate income tax for a maximum period of 10 years for industrial enterprises and production-related service providers. The federal tax incentives are linked to the number of newly created or maintained jobs by an enterprise domiciled in selected regional areas in Switzerland. It can lead to an annual tax credit of up to CHF95,000 for each newly created job and CHF47,500 for each maintained job. Depending on the number of newly created or maintained jobs, the effective tax rate may be substantially decreased to a low single-digit tax rate. There are also tax holiday schemes available at the cantonal level.

Renminbi crossroad

Marcus Peter and Kate Yu Rao of GSK Stockmann outline the benefits of Luxembourg as an investment destination and global investment springboard for Chinese investors

The Luxembourg government declared a three-month long state of emergency on March 18 in response to Covid-19. Using emergency powers, it enacted temporary measures to allow Luxembourg companies of any type to hold non-physical general meetings for shareholders and management bodies. These measures eased companies' decision-making processes. The government also established a financial support scheme for those in temporary financial difficulty, on top of companies being given the option to delay filing their annual accounts with the Luxembourg company register RCSL.

The government also announced a series of tax measures to support companies with regards to direct and indirect tax payments.

Notwithstanding these efforts, Covid-19 poses several challenges. The biggest concern for any investor in Luxembourg, Chinese or otherwise, is liquidity. Chinese investors can mitigate their financing risk by either having enough cash on hand or by having access to a revolving credit facility (RCF) to fund the purchase price of a target. Investors can also obtain commitment letters from debt and equity financing sources. Another obstacle to M&A transactions is that banks are concerned about their ability to syndicate while the Covid-19 situation develops, which means they are reluctant to commit financing. Buyers for their part are unwilling to risk being caught in a bridge debt limbo.

Chinese investors have also faced an issue with their workforce on the ground. As Covid-19 emerged some employees had just travelled back to China for the holidays and in many cases were unable to return to Europe. For employees in Europe, safety measures were put into place.

However, the outlook for Chinese investment into Luxembourg remains optimistic, despite the slowdown in Chinese foreign direct investment (FDI) into the European Union and the temporary change of investment conditions due to Covid-19.

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Ease of investing

Luxembourg has a forthcoming attitude to Chinese investment. This is characterised by a strong business and political exchange between both countries. Luxembourg continues to remain a core jurisdiction in the EU as a hub for guiding Chinese investment into other European jurisdictions, and because the Luxembourg government has kept an open mind towards Chinese investors. Over the last years, Luxembourg has experienced a growing interest from Chinese investors in carrying out their M&A transactions in the EU via Luxembourg investment structures.

Luxembourg is one of the most important hubs for the cross-border renminbi business in Europe. It already hosts the European headquarters of seven Chinese banks, which have been increasing their business activities, workforce and balance sheets year on year. These Luxembourg headquarters have been opening and continue to open branches in other EU jurisdictions, further underlining the importance of the Luxembourg banking sector. These Chinese banks are actively involved in financing M&A deals originated by Chinese investors.

As regards practical considerations for making investments, in general, Luxembourg has no specific pre-approval process, although M&A transactions may be subject to an *a posteriori* approval process by the competent Luxembourg authority.

Nevertheless, new EU regulations (Regulation (EU) 2019/452) on FDI entered into force in May 2019 and will be fully applicable in November 2020. Under these new regulations, EU member states are required to inform the European Commission and other member states of any FDI review. Even though Luxembourg itself does not conduct any FDI reviews, it will still be subject to this review process under the new regulations.

Generally, no restrictions on investment exist, although specific rules do apply in some sectors. For example, in acquisitions in the financial sector (banks or asset managers), an investor must notify its intention to acquire a certain threshold in a Luxembourg bank or financial sector entity to the regulator, the *Commission de Surveillance du Secteur Financier* (CSSF). The CSSF has the right to oppose the transaction based on reasonable grounds and certain legal criteria. Other restrictions apply in certain industries and on acquisitions of companies with securities admitted to trading on a regulated market in Luxembourg. The requirements are clearly established by the Takeover Law (the law May 19 2006 implementing Directive 2004/25/EU on takeover bids).

The Luxembourg law on competition (October 23 2011) designated the Competition Council as the competent authority to scrutinise and analyse mergers and acquisitions taking place in Luxembourg and involving Luxembourg entities. Although it is a post-closing merger clearance process, the Council has indicated its readiness to encourage market participants to run a pre-merger control check where feasible. This possibility therefore exists for investors looking to acquire a Luxembourg-based target.

Generally, there are no currency restrictions and no specific contractual provisions arise in relation to Chinese investment.

Investment structures

The most common legal entities used for Chinese investment into Luxembourg are private limited liability companies (*société à responsabilité limitée* – S.à r.l.) or public limited liability companies (*société anonyme* – S.A.). Both are commonly used as structures for acquisition companies. The

S.à r.l. has a lower minimum share capital and seems to be favoured over the S.A.

As regards to investment activities by funds established by Chinese investors in Luxembourg, the most common structure seems to be the new fund vehicle, the reserved alternative investment fund (RAIF), and also, to a certain extent, the specialised investment fund (SIF). Both are set up as limited partnerships (*société en commandite simple* or *société en commandite spéciale*). In addition, the Luxembourg investment fund market offers different investment vehicles that are used (including by Chinese investors) to pool money for investment. These vehicles are alternative investment fund vehicles that can be structured as a specialised investment fund (SIF), an investment company in risk capital (*société d'investissement en capital à risqué* – SICAR) or a reserved alternative investment fund (RAIF).

The key requirement for setting up and using any of these vehicles is the establishment of a certain entity in Luxembourg with sufficient substance. A minimum share capital needs to be provided to the Luxembourg vehicle and management procedures need to be put in place. In establishing investment funds that carry out M&A activities, investors must verify that these comply with the regime of alternative investment fund managers and obtain the applicable approvals from of the CSSF. While RAIFs are not subject to CSSF approval, the SIF and SICAR investment vehicles must be pre-approved by the CSSF before they can begin their business activities.

By 2020, Luxembourg was party to over 100 bilateral investment protection treaties including a treaty with China

Dispute resolution and tax

The most commonly used dispute resolution mechanisms are court litigation and arbitration. Arbitration is generally favoured by foreign investors because arbitral awards are easier to enforce than court judgments, more flexible and provide more privacy. By 2020, Luxembourg was party to over 100 bilateral investment protection treaties including a treaty with China, the latest version of which entered into force in 2009.

Luxembourg courts will review disputes in a neutral and independent manner. The courts typically review cases within a normal duration of time and issue titles for enforcement useable in Luxembourg and abroad – as far as other jurisdictions are covered under respective regulations and treaties. One of the most important pieces of regulation in this respect is the Recast Brussels Regulation: Regulation (EU) No 1215/2012 of the European Parliament and of the Council of December 12 2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters. Another is the Lugano Convention, the Convention on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters, signed in Lugano on 30 October 2007. Local civil procedure code and case law is also of important.

Dispute resolution proceedings through arbitration are also possible if arbitration in Luxembourg was agreed on using the abovementioned agreements. Luxembourg's arbitration courts are used to international agreements, given Luxembourg has been increasingly used as a platform for cross-border investments, joint-venture vehicles and investment funds carrying out M&A activities worldwide.

Typically, however, parties in Luxembourg try to solve their disputes outside arbitration and courts. This is to maintain confidentiality and enable a smooth continuation of business in Luxembourg.

As regards tax, Luxembourg benefits from an extended network of double taxation avoidance treaties which is advantageous for FDI into and out of Luxembourg. Due to the application of European legislation on the parent / subsidiary relationship, typically no withholding tax applies on dividends. Furthermore, the corporate income tax rate is 17%. No specific FDI tax incentive schemes are in place, nor are there any specific reciprocal tax arrangements between Luxembourg and China.

CHINA OUTBOUND INVESTMENT SPECIAL FOCUS 2020

FRANCE

Land of opportunities

Chinese investment into France held steady in 2019 while it dropped across the rest of Europe. **Raphaël Chantelot**, **Fanny Nguyen**, **Hubert Bazin** and **Nicolas Vanderchmitt** of **LPA-CGR avocats** review the jurisdiction's investment advantages

France remains one of the most popular destinations for foreign direct investment (FDI) in Europe, with targets ranging from luxury goods to high tech companies. Chinese FDI in France remained stable in 2019 while overall Chinese FDI in Europe decreased quite significantly.

The impact of the Covid-19 crisis is obviously hard to assess to assess at this stage but it is likely to result in a lot of restructuring and M&A activities. Some French companies will be on the verge of bankruptcy and others will have to refocus on their core business and divest non-core activities.

The 2019 decrease in the volume and number of transactions in Europe seems to be due both to the lasting restrictions imposed by the People's Republic of China (PRC) authorities on outbound capital flows and to the increased FDI controls put in place by European governments.

Chinese investment in France targets all kinds of sectors and types of businesses, from family businesses to listed groups (for example, Lanvin, Accor Hotels etc), in industries as diverse as tourism (Club Med), fashion brands (Baccarat), food and wine, football clubs, the automotive sector (listed car parts manufacturer Le Belier), among many others.

France traditionally welcomes foreign investment and has a positive and welcoming attitude towards Chinese investment, with various cooperation initiatives, both public and private, designed to promote Chinese investment in France. The recent visit by President Xi Jinping to France in March 2019, following President Emmanuel Macron's visit to China in 2017, illustrates the long-term and close relationships between China and France.

A series of political and legal measures have also recently been implemented to make France more attractive to foreign investors. For instance, President Macron's government decided to gradually lower the French corporate income tax

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(CIT) rate to 25% by 2022 (from 33.3% today) and to develop tax incentives for innovation (such as a strong research and development (R&D) tax credit system). Major changes have been agreed to make French labour law more flexible, with a simplification of the employees' representation system and amendments to the rules for dismissing employees (which will lead to reductions to both severance costs and the risks of litigation). Despite some social unrest, reflected by the "yellow jackets" movement, France remains an attractive market for Chinese investment.

France typically has no limitations on foreign investment. But as with all investment originating from outside the European Union, Chinese investment in France remain subject to certain limitations (which are further detailed below). The outlook for Chinese investment in France in the coming months is quite promising, as the positive trend observed in 2018 should continue into 2019. Indeed, France is benefitting from Brexit, as the UK was previously one of the preferred investment destinations in the EU, and from the rising trade tensions with the United States, which traditionally absorbed one of the largest chunks of Chinese FDI. These circumstances, combined with the positive effects of President Macron's reforms, make France a desirable entry point for Chinese investors looking to develop their operations in Europe.

Investment approval

As a principle, foreign investment in France is free and not subject to governmental approval. However, foreign investment in certain industries which are deemed sensitive or related to national defence may require prior authorisation from the French Ministry of Economy and Finance.

French law (section L.151-3 of the French Monetary and Financial Code) provides that foreign investments in activities relating to national security or which may disrupt public safety, or are in the research, production or sale of military weapons, are subject to prior approval from the French Ministry of Economy and Finance. Such restrictions apply to investments from investors registered in jurisdictions outside either the EU or the European Economic Area (EEA).

The list of industries impacted by these restrictions has been expanded to include industries deemed to be of national strategic interest, for instance telecoms, transportation or public health, or technologies with dual civil and military use, certain IT and telecoms areas (for example cryptology, communications and transportation networks and services). This extended list now includes key artificial intelligence technology, the aerospace industry, data storage and semiconductors. Other measures include the creation of golden shares, which would enable the French state to exercise specific rights in companies listed in these sensitive industries, in order to prevent their sale to foreign investors.

The authorisation process is quite straightforward. The request is submitted to the Ministry of Economy, which has two months to review the investment. If no opposition or request for further information is issued within this timeframe, the authorisation is deemed granted. It is

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worth noting that there was a recent regulation adopted by the EU at the beginning of 2019 designed to enhance cooperation between European countries with a focus both on FDI transaction that impact several jurisdictions and on subsequent changes in the investments made by foreign investors (if they increase their stake, if there is a change in their shareholding or if they use an EU acquired vehicle to subsequently carry-out acquisitions in the EU). It is likely that French rules will be adapted in the coming years to implement these new EU rules.

As for foreign currency or foreign exchange restrictions, there are none in France.

In terms of competition policy, the French authority that oversees competition clearance is the French Competition Authority (*Autorité de la Concurrence*), which is an independent administrative agency.

French merger control applies if the turnovers of the parties to a transaction (the acquirer, the target and their subsidiaries) exceeded, in the last financial year, certain (cumulative) thresholds provided in Article L. 430-2, I of the French Commercial Code. The thresholds include a worldwide turnover by all parties exceeding €150 million or a turnover in France exceeding €50 million for at least two of the parties. Transactions are not subject to notification in France if they are notified at the EU level.

Under Article L. 430-3 of the French Commercial Code, a notifiable merger cannot be finalised before it is cleared by the French Competition Authority. There is no filing fee. Failure to notify a reportable transaction is subject to daily penalties and fines.

The majority of notified transactions are cleared within 25 business days of their notification filing. However, certain transactions go through a more in-depth Phase II review which requires an additional 65 business days. Investment techniques French corporate law offers various forms of corporate vehicles that can be used for an acquisition or joint-venture, including the equivalent of a limited liability company and a company limited by shares. One of the most commonly used legal entities used by Chinese investors for large transactions is the simplified joint stock company (SAS), as it is a very flexible corporate form: it can be established with a single shareholder and with limited share capital, and the rules governing its functioning are very flexible and can be organised to a large extent freely in the by-laws.

In general, there are no specific requirements that impact a Chinese investor. It is worth noting that French law does not require the participation of a French citizen or entity in French commercial companies, either as shareholders or as directors or officers. Recent regulations requiring the disclosure of the ultimate beneficial owner of a French company however do sometimes raise disclosure issues with Chinese investors.

Dispute resolution

On November 28 2007, France and the PRC signed a bilateral investment treaty (BIT) which came into force in France in 2011. It is worth highlighting that French courts are independent and commercial matters are judged in courts composed of professional judges, with an appeal process in front of professional judges. There are also various summary proceedings that can allow an investor to efficiently enforce its rights.

French courts also duly deliver the exequatur allowing foreign judgments and international arbitration awards and deeds received by foreign officers when such judgments and awards have complied with basic principles designed to ensure the fairness of the trial and rights of the defendant.

Furthermore, France is party to multiple European and international conventions as well as bilateral treaties (including with the PRC) that provide simplified legal frameworks for the recognition and the enforcement of foreign judgments and judicial cooperation. French judgments and arbitration awards rendered in France (for instance under the ICC Arbitration Rules) are generally enforceable in other jurisdictions.

Tax

Traditionally, Chinese investors would establish holding companies in Luxembourg in order to benefit from lower corporate income tax (CIT) rates. However, these structures are now coming under scrutiny from French tax authorities and there is an increasingly common requirement to have "substance" in Luxembourg (for instance, actual staff and operations), which is quite costly and burdensome to meet. Since French CIT rates are being reduced and should match Luxembourg CIT rates by 2022, this type of tax structuring via Luxembourg will no longer be useful.

As of the financial year beginning on or after January 1 2020, a 28% CIT rate applies to the first €500,000 of taxable income, the part in excess of €500,000 being subject to a 31% rate (or 33.33% for MNEs whose turnover exceeds €250 million – article 219-I of the French Tax Code). This rate will be reduced progressively to 25% by 2022. Small companies (for example, enterprises at least 75% owned by individuals or by other small enterprises and with a turnover of €7.63 million or less) are taxed at a reduced rate of 15% on the first €38,120 of profits and at the standard CIT rate on any excess (article 219-I-b of the French Tax Code).

Gross dividends distributed to corporate shareholders outside France are subject to a final withholding tax of 30%, unless there is a tax treaty between France and the foreign country that provides for reduced withholding tax rates (as described below, China and France have signed a treaty providing for a favourable tax treatment). However, no withholding tax is levied on dividends paid by a French company to a qualifying parent company resident in the EEA if certain conditions are met.

Foreign companies established in France enjoy the same government aid and incentives as French companies (such as support for productive investment, R&D, professional training and job creation, among other activities). France also offers some tax and non-tax incentives to French and foreign businesses that are creating new, or expanding existing, businesses in certain French regions, acquiring declining industries or decentralising their activities out of the Paris and Lyon regions.

In addition, taxpayers in France (including foreign investors who have established a business in France) may benefit from the attractive R&D tax credit system. The R&D credit, which takes into account the annual volume of expenditure, amounts to 30% of the expenses related to R&D operations up to a value of €100 million, and 5% for anything above that. Higher rates apply to companies that never benefited from the credit and those that did not benefit from the credit for a five-year period. Certain conditions must be met.

France and China signed a revised double taxation agreement (DTA) on November 26 2013. This agreement reduces the withholding tax rates applicable to dividends, royalties and interests. A Chinese investor will be taxed only 5% on the repatriation of dividends from France if the investor holds 25% of the shares or voting rights in the French company (the withholding tax rate will be at 10% in all other cases). Withholding taxes on royalties and interests paid to investors resident in China are also reduced to 10%.

The DTA also helps to eliminate any double taxation arising from cross-border transactions and to secure the tax position of Chinese investors.

LMG Analytics 2019 DCM League Table Report

Welcome to the 2019 DCM League Table Report from LMG Analytics.

Despite a slowdown in the overall number of bonds issued, 2019 was a busy year for law firms in the debt capital markets. Over 950 unique law firms are represented in the data, which covers 14,318 DCM transactions from last year. LMG Analytics' 2019 data includes 6,121 unique issuers and 821 underwriters, accounting for $6.074 trillion in bond sales. The products' full coverage includes transactions from January 1 2018 through to Q1 2020.

LMG Analytics' primary focus is on the relationships between issuers, underwriters and the law firms that advise them. In addition to volume and value, the underlying data – over 33,000 transactions – powers an analytics machine that measures the durability of firm/company relationships, the complexity of each deal in the database, and the market share for each company across multiple filters.

14,318
NUMBER OF DEALS

897
NUMBER OF LAW FIRMS REPRESENTING ISSUERS

280
NUMBER OF LAW FIRMS REPRESENTING UNDERWRITERS

820
NUMBER OF UNDERWRITERS

6,121
NUMBER OF ISSUERS

1,306
NUMBER OF ELITE DEALS

5,598
NUMBER OF INFLUENTIAL DEALS

7,414
NUMBER OF RECOGNIZED DEALS

Methodology
Transactions with a total deal value equal to or more than US$1 million are eligible. The league tables included in this report include all transaction types. Subscribers have the option to generate league tables that do not include MTN issues online. All submitted data is vetted and sources remain strictly confidential and will not be disclosed. LMG Analytics rankings are broken down into three types: legal adviser, issuer and underwriter, with the legal adviser table further broken down into issuer and underwriter instructions.

LMG Analytics does not contain the following debt issues in our league tables:

- CLOs/CBOs
- Federal Credit Agencies/Government/State/Municipality/Trust issuers
- Private placements
- Fund Vehicle Issues

Please visit our website or contact Liam Sharkey on lsharkey@lmganalytics.com for more information on our league tables, methodology and subscriptions.

TOP 20 FIRMS (ALL DEALS, GLOBAL)

COMPANY	TOTAL USD (M)	# OF TRANSACTIONS	ESTIMATED MARKETS SHARE BY VALUE	BY VOLUME
Linklaters	574,238	1,424	7.48%	9.01%
Allen & Overy	550,875	1,400	7.18%	8.85%
Clifford Chance	497,784	1,083	6.49%	6.85%
Sullivan & Cromwell	267,151	565	3.48%	3.57%
Davis Polk & Wardwell	470,652	523	6.13%	3.31%
Sidley Austin	182,122	484	2.37%	3.06%
King & Wood Mallesons	207,656	324	2.71%	2.05%
White & Case	173,879	305	2.27%	1.93%
Cleary Gottlieb Steen & Hamilton	208,925	280	2.72%	1.77%
Latham & Watkins	219,639	276	2.86%	1.75%
Dentons	76,330	249	0.99%	1.57%
Simpson Thacher & Bartlett	273,118	203	3.56%	1.28%
Simmons & Simmons	38,216	179	0.50%	1.13%
Zhong Lun Law Firm	86,324	179	1.12%	1.13%
Hogan Lovells	84,820	173	1.11%	1.09%
Hengeler Mueller	81,182	160	1.06%	1.01%
Commerce & Finance Law Offices	62,135	154	0.81%	0.97%
AllBright Law Offices	41,280	146	0.54%	0.92%
Freshfields Bruckhaus Deringer	62,353	141	0.81%	0.89%
Mannheimer Swartling	10,937	141	0.14%	0.89%

LEAGUE TABLES

LMG Analytics allows customers to create custom league tables with filters for geography, deal types, industry sectors, value, volume, and complexity of work, among others. Firms, issuers and underwriters can be ranked by various key performance indicators to evaluate the nature of their DCM work.

The top 20 DCM law firms in 2019 combined accounted for 52% of the market share by volume and over 57% by aggregate value. At the very top, Linklaters narrowly edged Allen & Overy by a mere 24 transactions in 2019, with 1,424 to A&O's 1,400. Together, those two firms stand out for the volume and breadth of their DCM work, accounting for a third of the transactions from the entire top 20 combined. Clifford Chance, Sullivan & Cromwell, and Davis Polk & Wardwell occupy the next three slots.

Three firms headquartered in mainland China represent the Asia-Pacific region in the top 20: Zhong Lun Law Firm (#14), Commerce & Finance Law (#17) and AllBright Law Offices (#18).

Occupying the #12 slot with 203 transactions, Simpson Thacher & Bartlett moves up to #5 position when measured by aggregate deal value and is second only to Cravath Swaine & Moore when measured by the average deal value in 2019. The firm sits at #8 in deal volume when looking at the top 10 underwriter representations only.

Swedish giant Mannhiemer Swartling comes in #20 position when looking at all deals in the research period. Highlights include working on the first EMTN programme to be governed by Swedish law and listed in Stockholm, and assisting on the issuance of the country's largest green bond to date.

German powerhouse Hengeler Mueller occupies the #8 position on underwriter transactions, driven by work for clients such as DZ Bank, HSBC and RBS.

When analysing law firms' work on behalf of issuers only, Allen & Overy and Clifford Chance occupy first and second spot with 461 and 449 transactions. Clifford Chance leads the pack when judged by aggregate value for the year, driven by large bond issuances by Anheuser-Busch InBev and the European Financial Stability Facility's (EFSF) issuing vehicle. A&O advised on a series of deals for Swedish real estate giant Vasakronan and French bank Banque Fédérative du Crédit Mutuel (BFCM).

UNDERWRITER LEAGUE TABLES

The Top 10 Underwriters league table assesses investment bank activity for any transaction where they played a bookrunner or manager role of any kind. JP Morgan, Citigroup, BofA Merrill Lynch, HSBC and Goldman Sachs sit in the top five spots respectively, together accounting for over 16% of the entire market share by volume.

ELITE DEALS

LMG Analytics produces a score for each transaction, using a proprietary algorithm to quantify the complexity of the work involved. The points for each **Complexity Score** are weighted for deal value, jurisdiction, multiplicity of currencies and tranches, and whether it is a debut or repeat transaction.

There was a small drop in the average complexity of transactions in 2019 – less than 2% – but the volume of deals that fall into our 1st (**Elite**) and 2nd (**Influential**) tiers of complexity dropped from 54% of all transactions to 48% in 2018. The bottom, **Recognised** tier, saw 52% of all 2019 transactions compared with 46% in 2018.

As might be expected, the Elite transactions are heavily dominated by familiar names from the law firm and underwriter league tables. In fact, 45% of all 2019 Elite transactions had representation from firms in the top 10 Elite league table. Linklaters led the pack globally, acting on 94 Elite deals: 41 on behalf of issuers and 53 on behalf of underwriters. Clifford Chance, Davis Polk & Wardwell, Allen & Overy and Latham & Watkins filled the other top five positions. Davis Polk moves up to the #1 spot for Elite transactions acting for the issuer and Dentons, #7 for all legal work, moves to #2 on issuer instructions only.

JP Morgan continues to lead global underwriters when measured by the number of Elite deals in 2019, with Bank of America Merrill Lynch, Citigroup, Goldman Sachs and Barclays taking the next four slots. While Deutsche Bank and Credit Suisse do not appear in the Top 10 Underwriters table for deal volume, both banks move into the Top 10 Elite Underwriters table for 2019.

TOP 10 FIRMS (ELITE DEALS, GLOBAL)

COMPANY	TOTAL USD (M)	# OF TRANSACTIONS	ESTIMATED MARKETS SHARE	
			BY VALUE	BY VOLUME
Linklaters	95,133	95	4.91%	6.28%
Clifford Chance	129,744	74	6.70%	4.89%
Davis Polk & Wardwell	201,009	70	10.38%	4.63%
Allen & Overy	85,103	68	4.40%	4.49%
Latham & Watkins	100,501	53	5.19%	3.50%
Simpson Thacher & Bartlett	99,295	43	5.13%	2.84%
Dentons	25,665	38	1.33%	2.51%
Cleary Gottlieb Steen & Hamilton	62,640	37	3.24%	2.45%
Sidley Austin	37,537	37	1.94%	2.45%
Cravath Swaine & Moore	95,162	34	4.92%	2.25%

TOP 10 FIRMS ADVISING UNDERWRITERS (GLOBAL)

COMPANY	TOTAL USD (M)	# OF TRANSACTIONS	ESTIMATED MARKETS SHARE	
			BY VALUE	BY VOLUME
Allen & Overy	210,588	461	4.80%	4.94%
Clifford Chance	222,391	449	5.07%	4.81%
Linklaters	206,312	385	4.70%	4.12%
Sidley Austin	81,998	307	1.87%	3.29%
King & Wood Mallesons	185,740	270	4.23%	2.89%
Dentons	66,213	235	1.51%	2.52%
Davis Polk & Wardwell	120,549	185	2.75%	1.98%
White & Case	86,202	167	1.96%	1.79%
Zhong Lun Law Firm	82,168	167	1.87%	1.79%
Latham & Watkins	108,737	161	2.48%	1.72%

TOP 10 FIRMS ADVISING ISSUERS (GLOBAL)

COMPANY	TOTAL USD (M)	# OF TRANSACTIONS	ESTIMATED MARKETS SHARE	
			BY VALUE	BY VOLUME
Linklaters	369,872	1041	11.19%	15.92%
Allen & Overy	345,820	972	10.46%	14.87%
Clifford Chance	276,791	637	8.38%	9.74%
Sullivan & Cromwell	129,627	432	3.92%	6.61%
Davis Polk & Wardwell	350,106	339	10.59%	5.19%
Sidley Austin	100,134	179	3.03%	2.74%
Cleary Gottlieb Steen & Hamilton	90,701	155	2.74%	2.37%
Hengeler Mueller	75,873	144	2.30%	2.20%
Simpson Thacher & Bartlett	195,432	139	5.91%	2.13%
White & Case	87,767	139	2.66%	2.13%

TOP 10 UNDERWRITERS (GLOBAL)

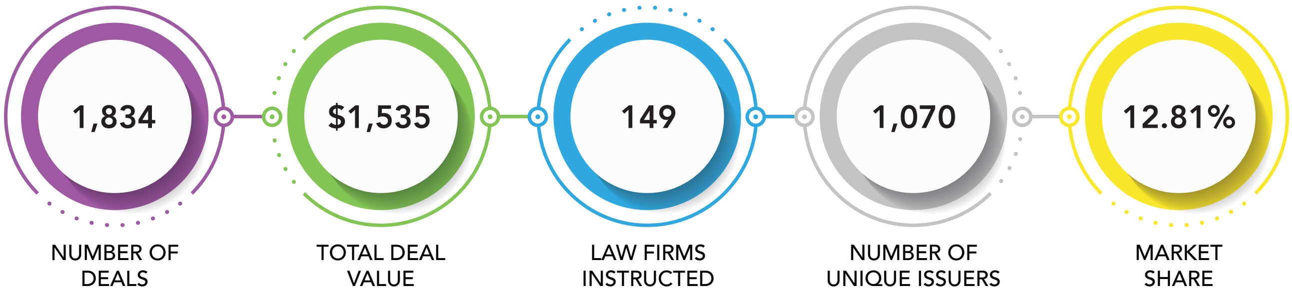
COMPANY	TOTAL USD (M)	# OF TRANSACTIONS	ESTIMATED MARKETS SHARE	
			BY VALUE	BY VOLUME
JP Morgan Chase	1,535,311	1,834	4.07%	3.83%
Citigroup	1,465,004	1,637	3.88%	3.42%
Bank of America Merrill Lynch	1,449,998	1,597	3.84%	3.34%
HSBC	1,204,312	1,466	3.19%	3.06%
Goldman Sachs	1,083,841	1,275	2.87%	2.66%
BNP Paribas	1,049,955	1,273	2.78%	2.66%
Barclays	1,237,613	1,154	3.28%	2.41%
Mizuho Bank	1,037,908	1,124	2.75%	2.35%
Morgan Stanley	998,618	1,073	2.65%	2.24%
Mitsubishi Corp	942,358	1,068	2.50%	2.23%

ELITE DEALMAKER
LMG ANALYTICS IFLR1000

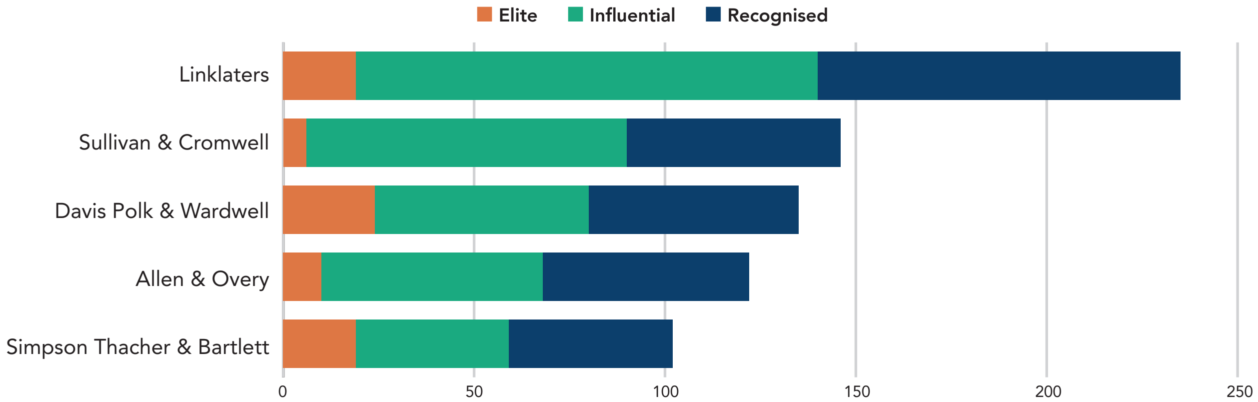
JP Morgan Chase

AS UNDERWRITER

JP Morgan has been identified as an underwriter on over 1,800 transactions in LMG Analytics' 2019 DCM data. Nearly 15% of those transactions met the threshold for Elite complexity status, with 47% falling into the Influential tier. Linklaters was the dominant law firm on JP Morgan's 2019 transactions, while Davis Polk & Wardwell advised on the largest proportion of Elite deals.



LEGAL ADVISER TO THE UNDERWRITER: NUMBER OF DEALS



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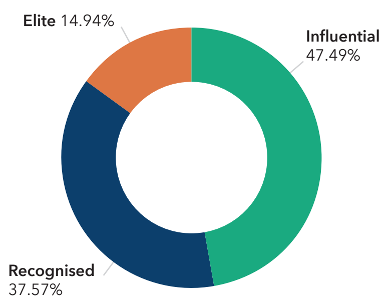


GEOGRAPHICAL SPREAD OF DEALS

ELITE DEALMAKER
LMG ANALYTICS IFLR1000

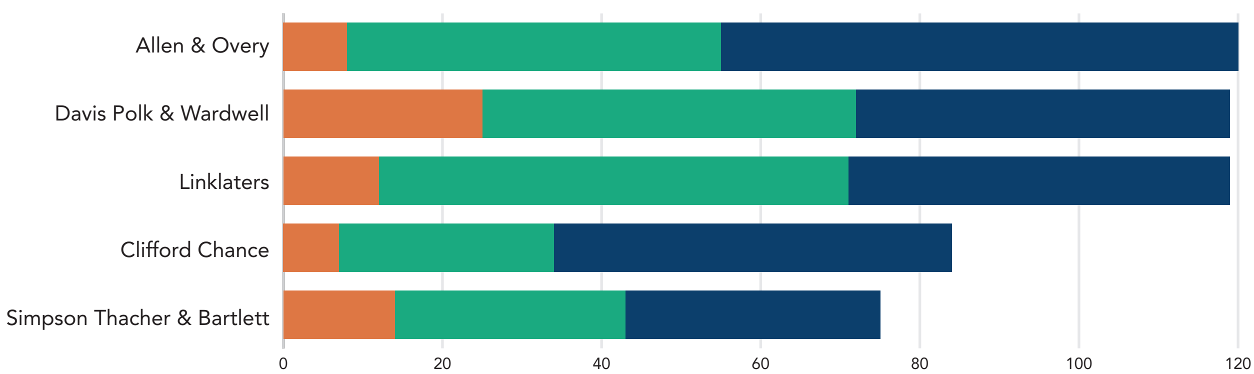
Citigroup

AS UNDERWRITER

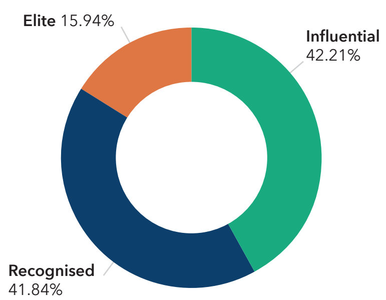
LMG Analytics logged over 1,600 transactions, on behalf of 1,017 issuers, where Citigroup was listed as an underwriter in 2019. Allen & Overy, Davis Polk & Wardwell and Linklaters had a very similar share of wallet for those deals, while Clifford Chance and Simpson Thacher & Bartlett were #4 and #5. Davis Polk appears to be a go-to firm for the most complex work in 2019, with the largest number of Elite transactions. Proportionally, Simpson Thacher also advised on an impressive number of Elite deals when compared to their totals against Citigroup.

1,637	$1,465bn	152	1,017	11.43%
NUMBER OF DEALS	TOTAL DEAL VALUE	LAW FIRMS INSTRUCTED	NUMBER OF UNIQUE ISSUERS	MARKET SHARE

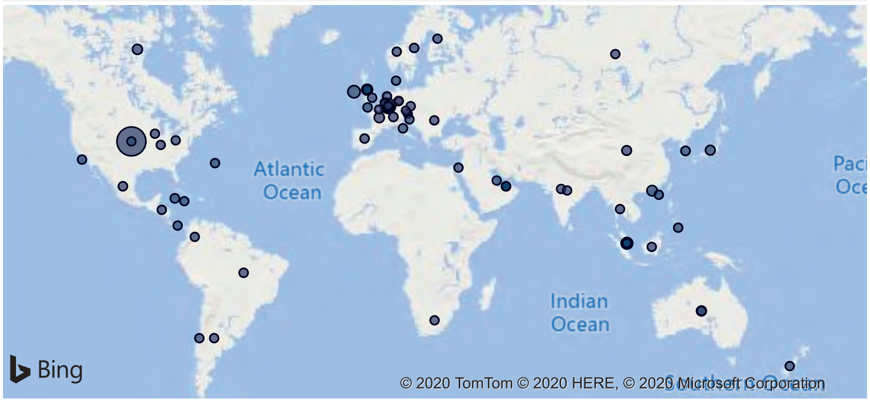
LEGAL ADVISER TO THE UNDERWRITER: NUMBER OF DEALS



DEAL COMPLEXITY



GEOGRAPHICAL SPREAD OF DEALS



Bank of America Merrill Lynch

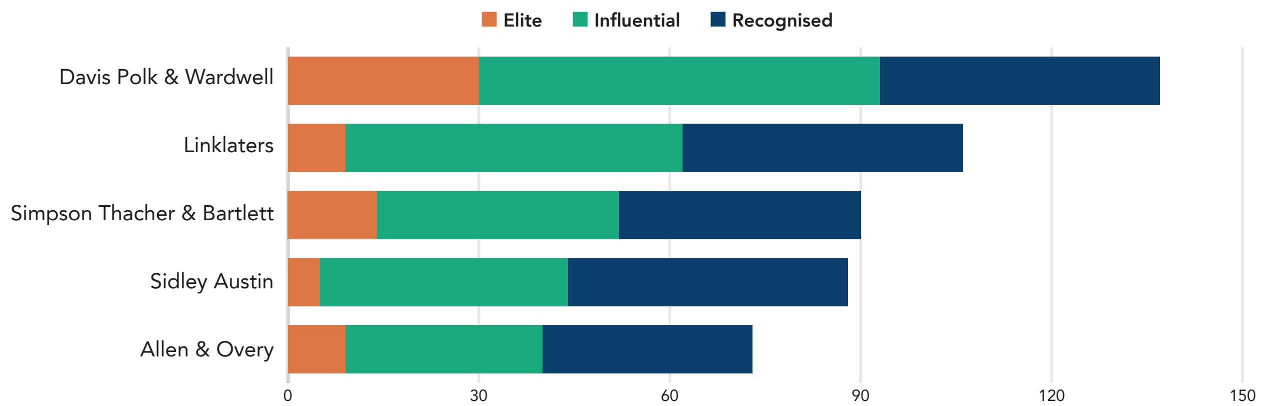
ELITE DEALMAKER
LMG ANALYTICS IFLR1000

AS UNDERWRITER

David Polk & Wardwell led the way as external counsel on BofA's underwriter activity in 2019 and logged an impressive 30 deals at Elite status. Linklaters, Simpson Thacher & Bartlett, Sidley Austin and Allen & Overy rounded the top five. Nearly 17% of transactions with BofA listed as an underwriter in 2019 met the threshold for Elite status. The investment bank ranks first in North America for Elite transactions, with 152.

1,597	$1,450 bn	130	988	11.15%
NUMBER OF DEALS	TOTAL DEAL VALUE	LAW FIRMS INSTRUCTED	NUMBER OF UNIQUE ISSUERS	MARKET SHARE

LEGAL ADVISER TO THE UNDERWRITER: NUMBER OF DEALS



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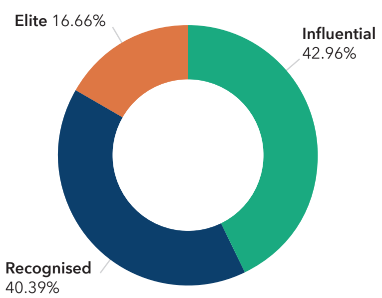


GEOGRAPHICAL SPREAD OF DEALS

ELITE DEALMAKER

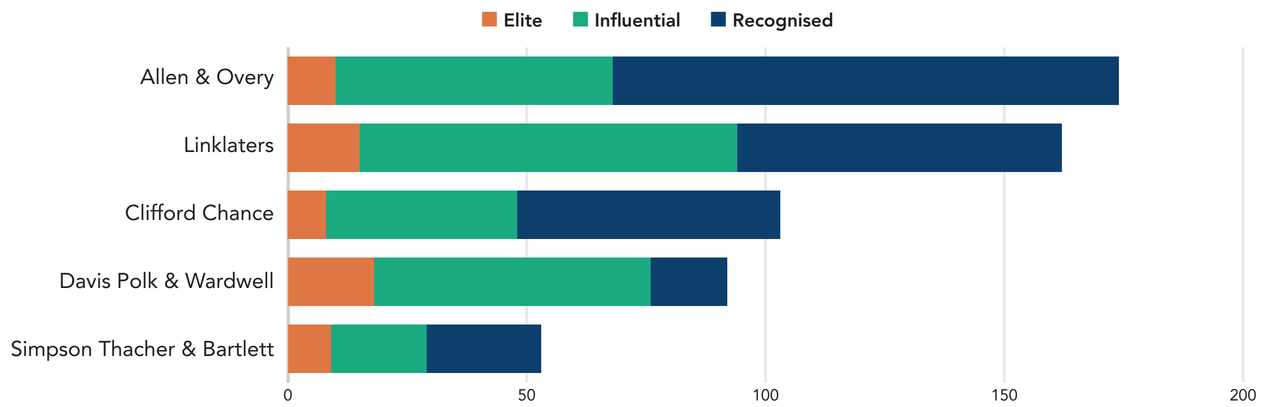
HSBC

AS UNDERWRITER

Allen & Overy and Linklaters dominate the top five firms acting on HSBC-underwriter transactions. While fourth in terms of overall share of wallet, Davis Polk & Wardwell again shines through with the most Elite transactions for the investment bank. HSBC's Elite deals comprise 11% of its total activity, a slightly lower proportion than its peers in the top five of the underwriter league tables.

1,466	$1,204 bn	137	864	10.24%
NUMBER OF DEALS	TOTAL DEAL VALUE	LAW FIRMS INSTRUCTED	NUMBER OF UNIQUE ISSUERS	MARKET SHARE

LEGAL ADVISER TO THE UNDERWRITER: NUMBER OF DEALS



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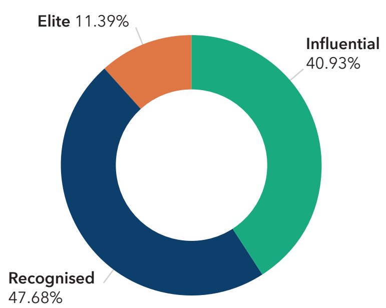


GEOGRAPHICAL SPREAD OF DEALS

ELITE DEALMAKER
LMG ANALYTICS IFLR1000

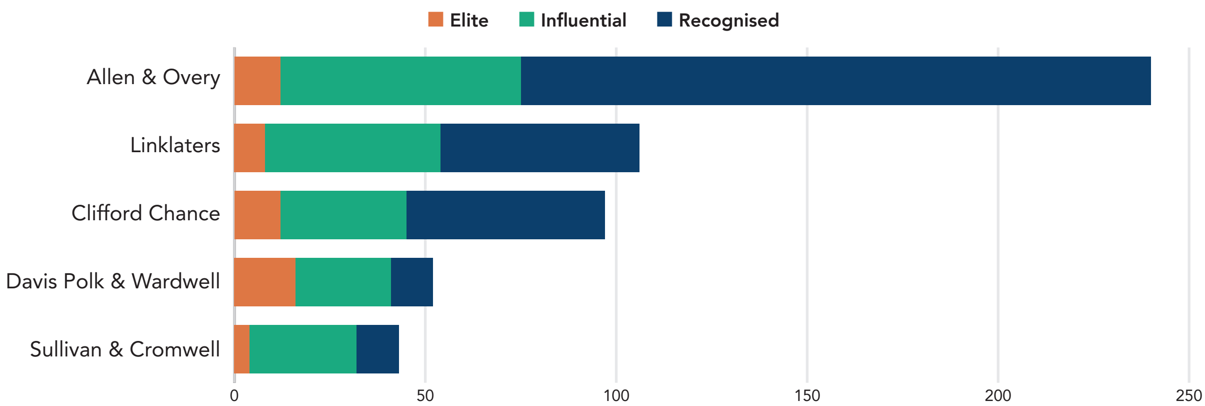
BNP Paribas

AS UNDERWRITER

Allen & Overy advised on double the number of BNP Paribas transactions as the next nearest firm, Linklaters, in 2019. The investment bank's Elite deals amount to nearly 13% of their total, with David Polk & Wardwell advising on a higher proportion of those matters, compared to its peers.

NUMBER OF DEALS	TOTAL DEAL VALUE	LAW FIRMS INSTRUCTED	NUMBER OF UNIQUE ISSUERS	MARKET SHARE
1,273	$1,050 bn	120	683	8.89%

LEGAL ADVISER TO THE UNDERWRITER: NUMBER OF DEALS



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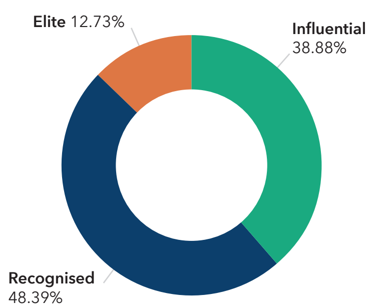


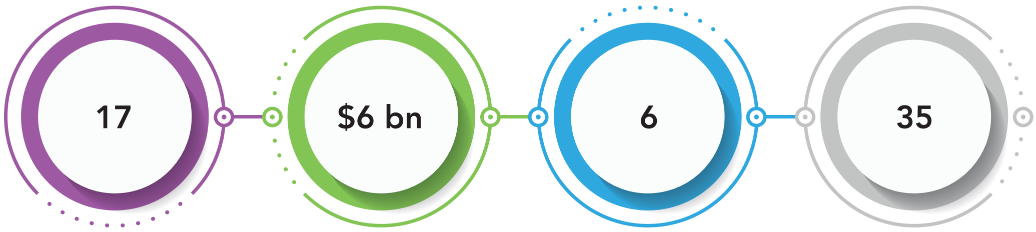
GEOGRAPHICAL SPREAD OF DEALS

General Motors Financial Company

ELITE DEALMAKER
LMG ANALYTICS IFLR1000

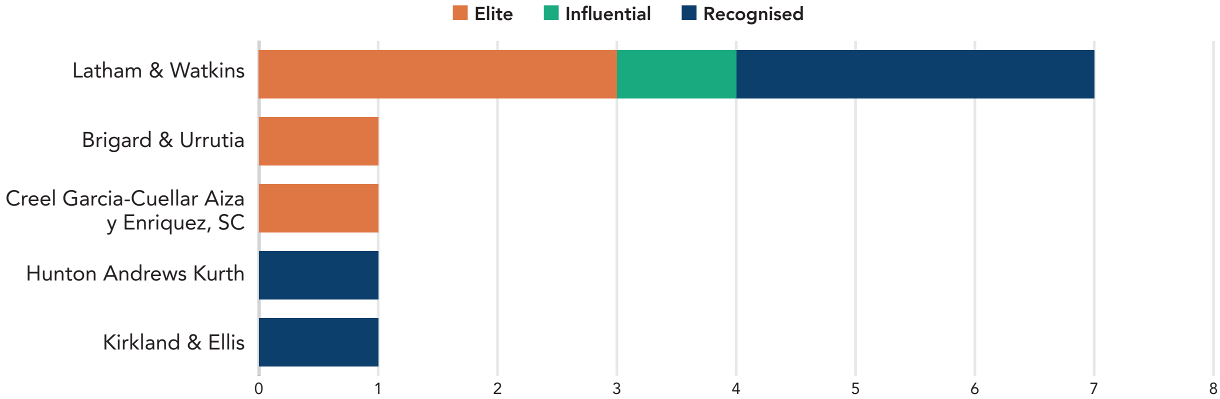
AS ISSUER

LMG Analytics logged 17 transactions from General Motors in 2019, with Latham & Watkins advising on the vast majority where counsel was identified. Hunton Andrews Kurth and Kirkland & Ellis each advised on a single transaction in the United States, while Brigard & Urrutia (Colombia) and Creel García-Cuéllar Aiza y Enríquez (Mexico) each acted on the automaker's two issuances in Latin America. The volume of work by Latham & Watkins is notable compared to 2018 when Hunton Andrews Kurth (formerly Hunton & Williams) acted on at least 10 deals.



NUMBER OF DEALS | TOTAL DEAL VALUE | LAW FIRMS USED | NUMBER OF UNDERWRITERS USED

LEGAL ADVISER TO THE ISSUER: NUMBER OF DEALS



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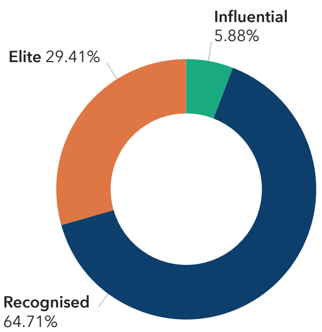
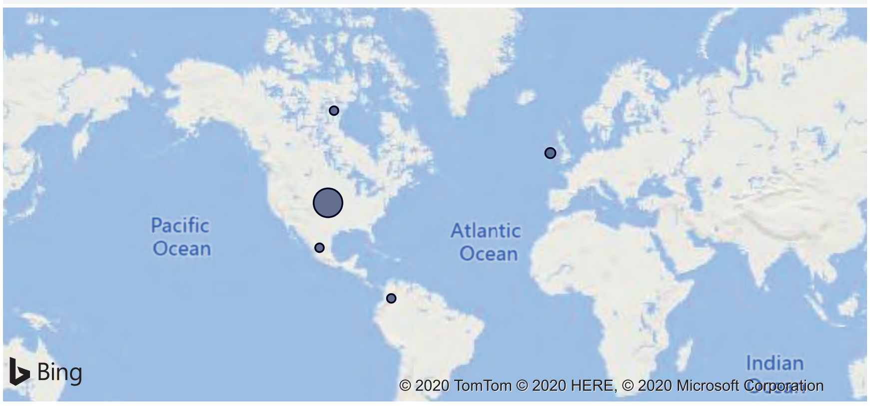


GEOGRAPHICAL SPREAD OF DEALS



ELITE DEALMAKER
LMG ANALYTICS IFLR1000

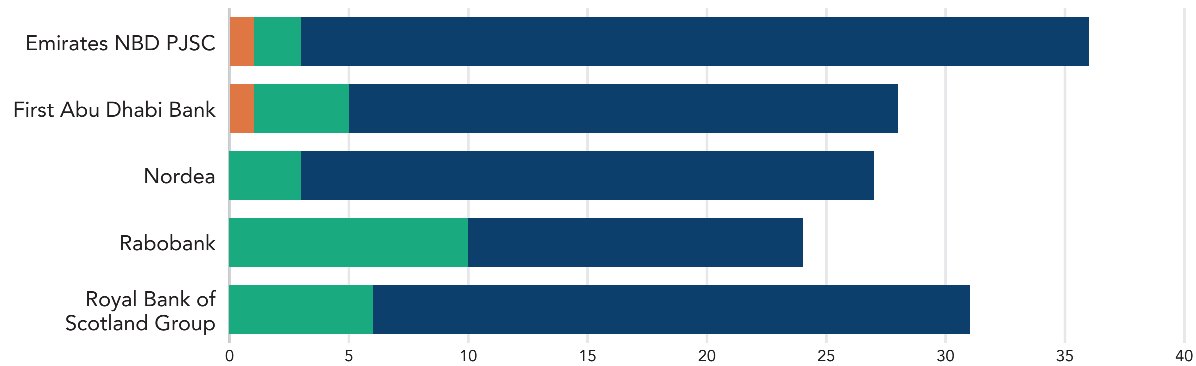
Clifford Chance

ADVISING ISSUERS

Elite Dealmaker Clifford Chance advised 135 separate issuers on 416 transactions in 2019. The firm is joint top of the 2019 rankings for transactions advising the issuer globally with their magic circle compatriots at Allen & Overy. Globally, the firm had 4.65% of the market share by volume of transactions and 4.86% when looking at the value of the transactions worked on. Given the strength of the firm's Middle East capital markets team, a region in which the firm dominates the market, it is unsurprising to see First Abu Dhabi Bank and Emirates NBD as major clients.

416	31	$210 bn	135	4.65%
NUMBER OF DEALS	NUMBER OF ELITE DEALS	TOTAL DEAL VALUE	ISSUERS REPRESENTED	MARKET SHARE

LEGAL ADVISER TO THE ISSUER: NUMBER OF DEALS



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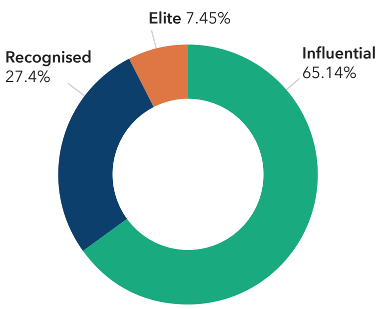


GEOGRAPHICAL SPREAD OF DEALS

ELITE DEALMAKER
LMG ANALYTICS IFLR1000

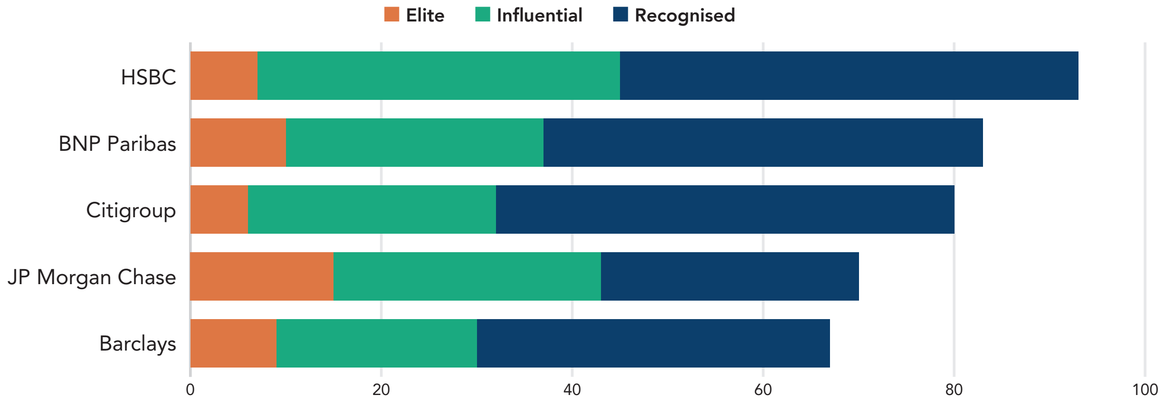
Clifford Chance

ADVISING UNDERWRITERS

As a powerhouse across the financial and corporate sphere, the firm's experience in advising banks and financial institutions means it is no surprise that it comes third in the global league firm league table for underwriter counsel work, having worked on 561 transactions in the research period. The firm also comes third in the global league tables for legally complex work, having worked on 38 Elite deals in 2019. The firm works with HSBC more than any other bank, with only Linklaters and Allen & Overy connected to more HSBC deals globally.

561	38	$259 bn	171	9.35%
NUMBER OF DEALS	NUMBER OF ELITE DEALS	TOTAL DEAL VALUE	UNIGUE UNDERWRITERS	MARKET SHARE

LEGAL ADVISER TO THE UNDERWRITER: NUMBER OF DEALS



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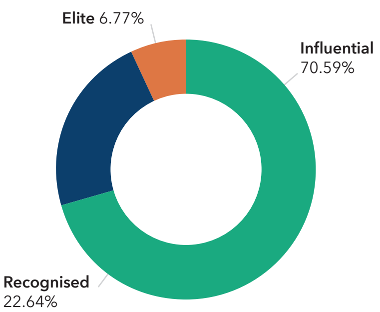


GEOGRAPHICAL SPREAD OF DEALS

Simpson Thacher & Bartlett

ELITE DEALMAKER
LMG ANALYTICS IFLR1000

ADVISING ISSUERS

White shoe firm Simpson Thacher's work is understandably focused in the US, with over half of the transactions logged by LMG Analytics listed there. The firm is focused on high-value, legally complex transactions, with 23.81% of its work classified as Elite. Only Latham & Watkins worked on more Elite deals in the US in the research period. Simpson Thacher's main client was JP Morgan Chase, which it advised on 11 issuances in the research period.

63
NUMBER OF DEALS

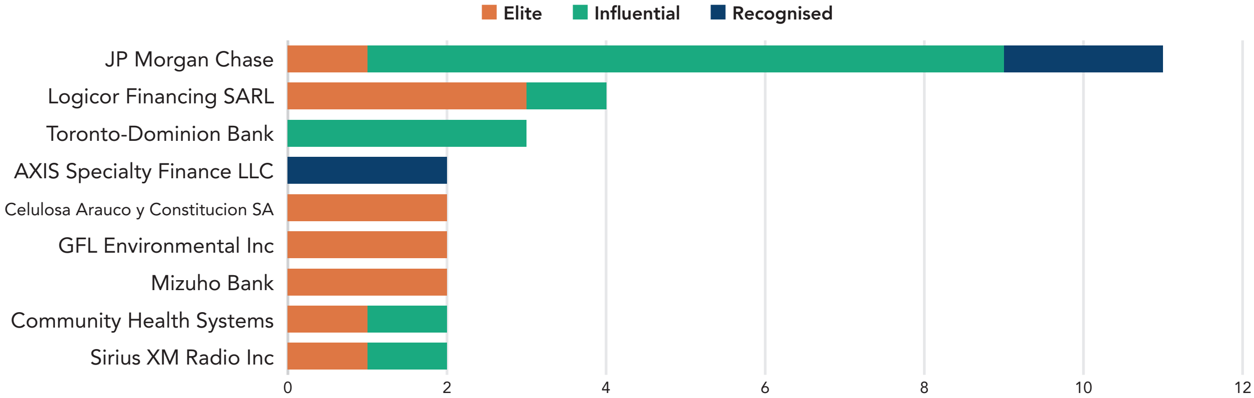
21
NUMBER OF ELITE DEALS

$78 bn
TOTAL DEAL VALUE

42
ISSUERS REPRESENTED

0.88%
MARKET SHARE

LEGAL ADVISER TO THE ISSUER: NUMBER OF DEALS



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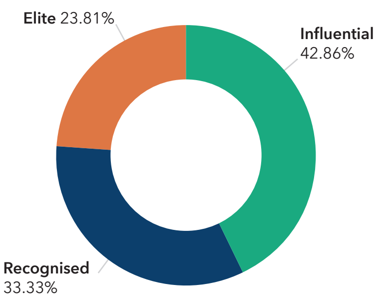


GEOGRAPHICAL SPREAD OF DEALS

Simpson Thacher & Bartlett

ELITE DEALMAKER

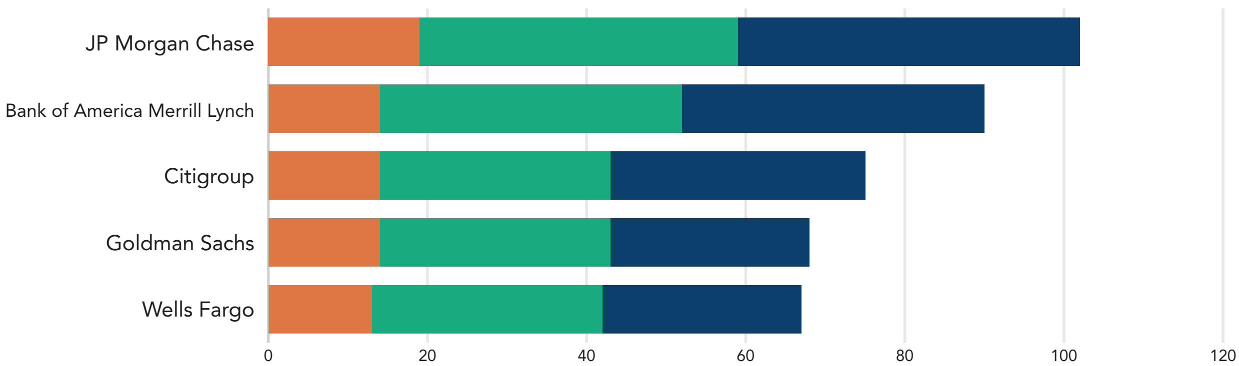
LMG ANALYTICS IFLR1000

ADVISING UNDERWRITERS

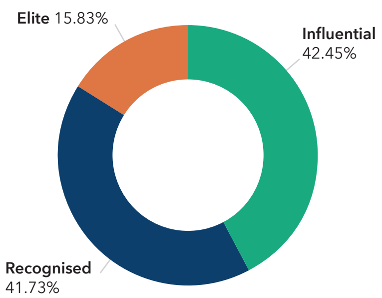
Simpson Thacher's work is focused on the large American banks. The firm is third in the United States league table for underwriter work, with 95 of its 139 deals listed there. Given their work on the issuer side it is not surprising that Simpson Thacher worked with JP Morgan Chase on 105 deals in the research period.

139	22	$195 bn	96	2.62%
NUMBER OF DEALS	NUMBER OF ELITE DEALS	TOTAL DEAL VALUE	UNIGUE UNDERWRITERS	MARKET SHARE

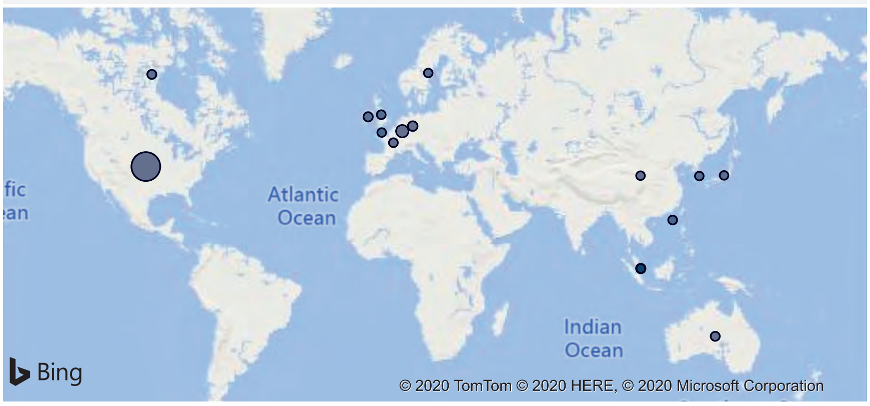
LEGAL ADVISER TO THE UNDERWRITER: NUMBER OF DEALS



DEAL COMPLEXITY



GEOGRAPHICAL SPREAD OF DEALS



ELITE DEALMAKER
LMG ANALYTICS IFLR1000

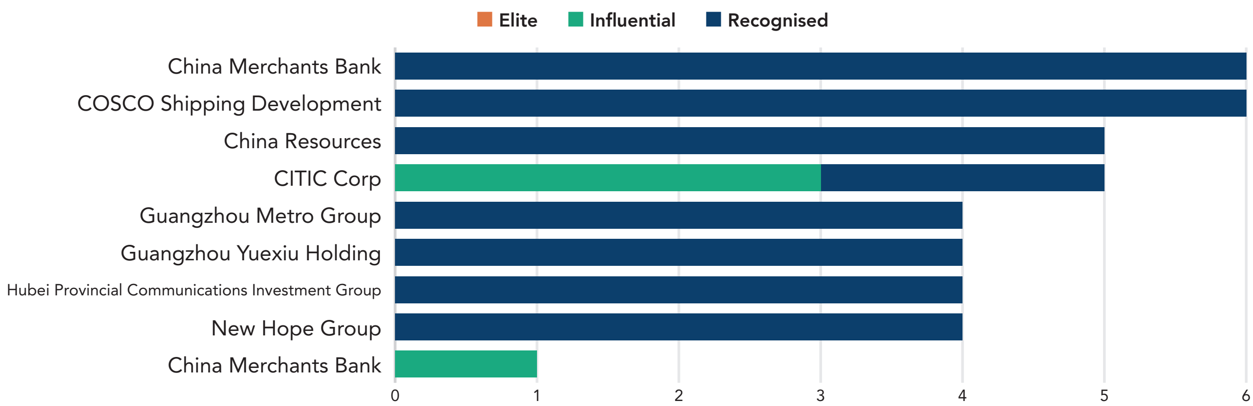
Zhong Lun Law Firm

ADVISING ISSUERS

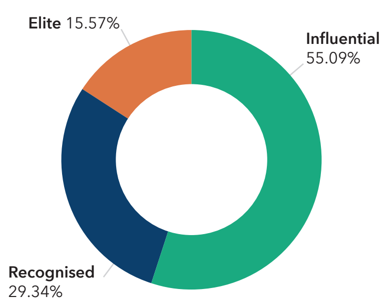
A colossus of the Chinese legal market, Zhong Lun appears in #12 place on the international deal league tables advising issuers, easily the highest position of any non-global law firm. The firm worked for China-domiciled issuers on 92 transactions in the research period, more than any other firm. It worked on 26 Elite deals on the issuer side, accounting for 10% of the total Elite deals in China.

167	26	$82 bn	120	2.29%
NUMBER OF DEALS	NUMBER OF ELITE DEALS	TOTAL DEAL VALUE	ISSUERS REPRESENTED	MARKET SHARE

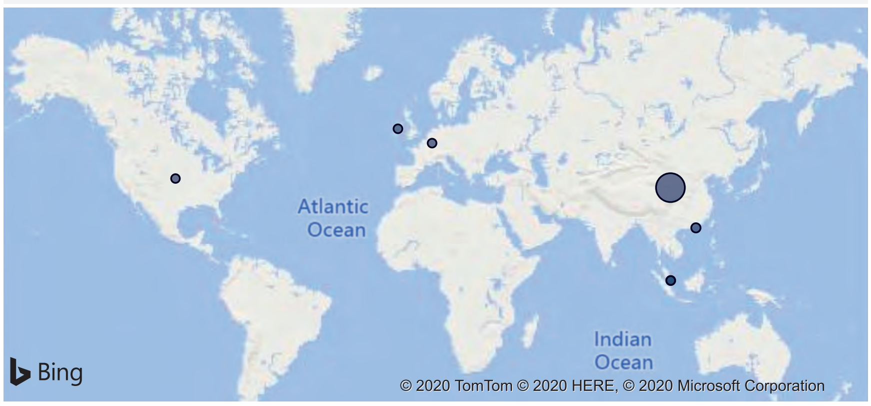
LEGAL ADVISER TO THE ISSUER: NUMBER OF DEALS



DEAL COMPLEXITY



GEOGRAPHICAL SPREAD OF DEALS



PEOPLE & CULTURE
BIGLAW IN SINGAPORE

Tech expansion continues in Singapore BigLaw

Recruitment firm **Jowers Vargas** co-founder **Evan Jowers** and partner **Alexis Lamb** review the tech legal landscape in Singapore and consider the potential impact of coronavirus

Singapore, a city-state of just 5.7 million people, sits at the tip of the Malay Peninsula. It has stood as one of the world's most important financial gateways since the days of Sir Stamford Raffles and the East India Company. In much more recent times, the Lion City has transformed itself into an attractive destination for major tech companies, founders, VC [venture capital] funds, and investors alike – much like a regional version of Silicon Valley.

According to David Kuo, partner in DLA Piper's Singapore office, Singapore is "a natural choice for the technological hub of Asia, given the stability of its legal system and rule of law, strong intellectual property protection, geographical proximity to the fastest-growing economies in Asia and access to a deep talent pool".

Many – if not most – of Southeast Asia's unicorn startups call Singapore home. In 2018, five of the top 10 most-funded digital startups in Southeast Asia were based in Singapore, including the top two – ride-hailing app Grab, and NYSE-traded digital entertainment, e-commerce, and e-payments company Sea Limited. A number of Indian startups, including e-commerce giant Flipkart, have likewise set up shop in Singapore.

Yanjun Wang, group chief corporate officer and general counsel of Sea Limited, describes Singapore's business advantages as such:

> "As an international hub for business, Singapore has evolved a highly sophisticated and efficient regulatory regime that promotes the long-term development of companies based here and attracts top talent from around the world. Tech companies here can benefit from having strategic operations and governance anchored in Singapore's mature ecosystem while simultaneously having a presence in the highly dynamic regional markets."

Foreign tech behemoths such as Facebook, Google, Amazon, Alibaba, ANT Financial, Tencent, Xiaomi, Go-

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Evan Jowers is based in Hong Kong SAR and is a co-founder of our Jowers Vargas. His focus is moving US associates, counsel and partners to and within Asia. He has made or helped make over 400 US lawyer placements in Asia since 2006. He has also made numerous placements in the US markets, including at the partner level.

He has been interviewed by numerous major media outlets for his insights on Asia BigLaw, such as the New York Times, LegalWeek, American Lawyer, Asia Counsel, California Lawyer, and CNBC, among many others. Jowers also created the Asia Chronicles blog featured at abovethelaw.com which, from 2008 to 2012, was regularly read by US-to-Asia associate movers.

Prior to his recruiting career, Evan was an associate at Cadwalader Wickersham & Taft's New York offices and had an in-house role at a Miami-based company.

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Alexis Lamb is extremely knowledgeable about the BigLaw legal markets in Asia as well as in the US. Prior to recruiting, she practiced as an M&A/private equity associate in the New York office of O'Melveny & Myers and a US capital markets associate in the Hong Kong SAR office of Linklaters, focusing primarily on pan-Asia work.

She successfully took her BigLaw experience to transition into a role as a trusted career adviser, counseling associates looking to make a move from the US into Asia or within the Asia markets, as she herself was placed by Evan Jowers from OMM into Linklaters.

Prior to joining Jowers Vargas, Alexis served as director of talent at Bliss Lawyers, a US-based alternative legal model, and as a senior recruiter for two New York-based recruiting agencies.

Jek, and Baidu all have significant operations in Singapore. "Singapore is an important hub for Ant Financial's globalisation and innovation efforts," says Leiming Chen, senior vice president and general counsel of Ant Financial Services Group. "We have significantly increased our headcount in legal and compliance in the city over the past three years and will continue to enhance our team there in the coming years to support our business expansions globally."

How will Covid-19 affect Singapore's status as a tech hub?

It's too early to predict Covid-19's lasting effects on tech meccas, including both Silicon Valley and Singapore. Several high-profile startups, from home-sharing behemoth AirBnB to clothing rental pioneer Rent the Runway, are shelving IPO plans, conducting layoffs, and facing overall uncertain futures.

Fortunately for Singapore (and much of Asia), the industries in its tech ecosystem could be poised to take advantage of the challenges of Covid-19. One unique trait of the tech landscape in Asia is the proliferation of 'superapps' and other all-everything tech companies. Do-it-all companies such as Grab, Go-Jek, SEA Group, and, of course, the Alibaba Group are diversified between a number of industries that will be vital in rebuilding the post-Covid business and leisure landscape, such as fintech, e-commerce, and online gaming. A 2019 report by the US-based project Startup Genome has named Singapore as the fourth-best global ecosystem for blockchain and the fifth-best global ecosystem for fintech; with some lauding Singapore as the eventual "fintech capital of the world".

According to Kuo, "while the current coronavirus pandemic has affected the economy in general, it has also created a unique opportunity for tech companies to prosper, given the growing need for e-commerce, telecommuting and other related services". Wang agrees, noting that "as the coronavirus crisis further accelerates the shift from offline to online, the tech sector is presented with new opportunities as well as challenges that come with potentially a much steeper growth curve".

Kuo has also observed "increased investor interest in deal activities in areas such as cloud-based platforms, data centres, and digital tool developers".

Fintech

As the pandemic lingers, many expect the volume of contactless payments to markedly rise and for branchless banking services to gain in popularity. A March 30 study by a Swiss-based financial services company shows a 72% rise in fintech app usage in Europe, and it's not a stretch to anticipate similar results in other markets. One Philippines-based bank saw digital banking transactions explode in March after three weeks of quarantine.

Covid-19 could also be an opportunity for insurtech companies to innovate and show their potential. While the virus has reminded us all of the fragility of our lives and livelihoods, it has underscored the importance of various types of insurance coverage – and the necessity of insurers and companies to be able to transact digitally.

As Covid-19 thrust supply chains into chaos, blockchain could be primed for a big moment. Blockchain tech has been used in Asia to speed insurance claims payouts, track donations, and trace the supply chains of medical materials. IBM and EY are even developing their own blockchain projects to deal with pandemic-related issues.

E-commerce and food delivery

E-commerce and food delivery have reaped the benefits of a stay-at-home society. YouTrip, Singapore's first multi-currency mobile wallet, has seen a 20% growth in consumer online spending. While YouTrip was initially conceived as a travel card, many are using its prepaid MasterCard for local e-commerce purposes. Within e-commerce, the online grocery sector could experience significant Covid-related growth.

Grab CEO Anthony Tan calls Covid-19 the "single biggest crisis" in his company's history, yet Southeast Asia's most valuable unicorn is already starting to pivot into fintech and food delivery. In February, Grab raised US$856 million to facilitate its expansion into financial services – namely SME lending, mobile payments, and micro-insurance – as demand for ride-hailing services has cratered.

Rival Go-Jek – another one-stop 'superapp' offering ride-hailing, food delivery, and mobile payments services – is seeing a rise in demand for its delivery services across Southeast Asian markets.

Across Singapore, demand for food delivery services has increased by 20-30% since the circuit breaker began on April 7.

Online gaming

As lockdowns keep people inside, many online gaming companies are seeing a surge in new subscribers despite decreased production of new products. In March, e-commerce retailer Lazada experienced an "unusually huge rise in the sales of games" in Singapore. Sales of console games and gaming chairs rose by 200% and 130%, respectively, from February 23 to March 7 to the following two-week period.

Homegrown companies that touch one or more of the above-mentioned industries will be well-poised for global growth. "Looking longer term," notes Wang, "we believe that the next wave of growth for Singapore's tech sector will see more local companies expand beyond the country to regional and even global markets. That is the growth trajectory that our company has been on. Founded and based in Singapore, Sea has been building a global footprint for our diverse offerings in digital entertainment, e-commerce and digital financial services under Garena, Shopee and SeaMoney respectively, which cover some of the largest sectors in the consumer internet industry."

The future of Singapore's legal market

Covid-19 may have chilled many forms of transactions, including strategic M&A and VC financings, but there is still the potential for considerable long-term growth in Singapore's legal markets.

In the past few years, some of Silicon Valley's top law firms have already seized the opportunity to take advantage of Singapore's growth in the tech sector. Gunderson Dettmer opened a Singapore office in 2016, citing the island nation's status as a critical global innovation hub. In 2019, Cooley followed suit; their 16th location worldwide. Silicon Valley's first mover into Singapore was MoFo, which opened its Singapore office in 2013.

Even despite the pandemic, we continue to advise US firms' global management on their long-term strategies to open up in Singapore. Firms with an EC/VC client base have been particularly interested in opening up Singapore offices. The coronavirus may defer their expansion plans in the short to medium term, but firms are not abandoning their strategic objectives. In the current climate, firms will take a cautious tack and will likely wait to pull the trigger on an office opening until (1) they find the right partner or team to serve as a cornerstone, and (2) some semblance of a post-Covid normal is achieved. This could involve a lateral external hire, an internal transfer, or, most likely, a combination of both.

For BigLaw associates attracted to Singapore's innovation-driven tech landscape, expect smaller offices and a greater chance to make more of a meaningful impact on deals and get closer to clients than one might get in New York or Silicon Valley. Singapore has not yet achieved the prominence of the world's two largest tech hubs, but this means that each associate who joins a tech-focused practice in Singapore has greater exposure to Southeast Asia and South Asia's up-and-coming companies. Taking a role in a firm's Singapore office could open up business-side and GC-level exit opportunities that might elude an associate should they choose to stay in more traditional tech havens.

Further, with the number of firms with Silicon Valley-type practices likely to more than double over the next 10 years, there is a lot of opportunity for associates entering the market on the ground floor to have solid partnership opportunities down the road. There will likely not be enough senior legal talent in Singapore to accommodate the BigLaw expansion of tech, startup, emerging companies, PE and VC practices as new firms seek to enter the market. We are working with two tech-focused law firms about to enter Singapore, and it's challenging to find the partner-level candidates needed to open new offices.

As Prime Minister Lee Hsien Loong said in a dialogue with VC firm Sequoia Capital, "the ferment, the effervescence, the ingenuity and brilliance which has gone into the tech scene has already made a big change in the world". Singapore's culture of innovation has both nurtured homegrown unicorns and 'soonicorns', as well as attracted some of the world's largest tech giants. While Covid-19 will undoubtedly change both personal spending habits and VC trends for the foreseeable future, unexpected crises have a way of accelerating innovation. Corporate lawyers with a passion for tech should still watch this island nation between the Indian Ocean and South China Sea.

Our team at Jowers/Vargas has placed the vast majority of new-to-Singapore US-trained lawyers in the Silicon Valley-type transactional space in Singapore over the past five years. This includes the associate and partner level. Feel free to reach out to us at alexis@evanjowers.com if you would like to discuss the Singapore market.

> ***"One Philippines-based bank saw digital banking transactions explode in March after three weeks of quarantine"***

CHINA

JunHe

Joey Lu

New official guidance for foreign debt filings

In 2015, the National Development and Reform Commission (NDRC) issued the Circular on Promoting the Reform of the Filing and Registration Regime for Issuance of Foreign Debt by Enterprises, under which, both issuance of bonds and borrowing of mid-and-long term commercial loans overseas by PRC enterprises and/or their offshore subsidiaries and branches (collectively, the debtors) are subject to a prior filing and registration with NDRC (foreign debt filing). Over the past five years, the debtors as applicants encountered a lot of issues with regard to the foreign debt filing due to the ambiguity in definitions, scope and standards thereof. As a result, the NDRC issued detailed application guidance including 25 FAQs and respective answers in February 2020, aiming to make these issues clear.

The new official guidance represents NDRC's prevailing regulatory views and may be regarded as practical guidance on the foreign debt filing. Some of the major changes are as follows:

- **The spectrum of debtors has been expanded.** NDRC confirms that the foreign debts to be issued by the offshore entities (e.g. entities incorporated in the Cayman Islands or Hong Kong SAR), which are controlled by a domestic individual under a red-chip structure relating to PRC entities, shall be subject to the foreign debt filing.
- **Two kinds of loan transactions are included.** Despite several uncertainties before, NDRC clarifies that (i) a revolving loan with a loan period of more than one year and (ii) an intra-company loan with a term of more than one year by a domestic enterprise from its offshore shareholder shall be filed as well.
- **The filing procedures are clearer.** For example, NDRC requires that the foreign debt filing shall be completed prior to the utilisation of the relevant facilities.

The new official guidance is much clearer about how to prepare and submit application documents

Although there are still some ambiguities surrounding the application process, the new official guidance is much clearer about how to prepare and submit application documents, and helps debtors completing foreign debt filings. Moreover, with the issuance of the new official guidance, an online application system for foreign debt filings is launched.

In addition to the new official guidance, the People's Bank of China and the State Administration of Foreign Exchange decided to raise the cross-border financing upper limit of PRC enterprises in February 2020. These recent optimisations reflect Chinese regulatory authorities' increasing willingness to utilise international financing channels for the financing of PRC enterprises. More positive changes and effects can be anticipated in Chinese foreign debt markets, and we expect that PRC enterprises will become more and more active in the international financing market in the near future.

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Challenges replacing Libor

Libor [London interbank offered rate] is the primary benchmark, along with Euribor, for short-term interest rates around the world. Libor rates are calculated for five currencies and seven borrowing periods, ranging from overnight to one year, and are published each business day. Libor is based on submissions provided by a selection of large international panel banks. These submissions are intended to reflect the interest rate at which banks could lend one another unsecured funds. Many financial institutions, mortgage lenders, and credit card agencies set their own rates based on this. However, in 2017, the UK's Financial Conduct Authority (FCA) announced that after 2021 it would no longer require the panel banks to submit the rates needed to calculate Libor. Libor will no longer be published after the end of 2021, and market participants are urged to transition to alternative reference rates (ARRs).

The reason for this change of policy is the fact that the number of deposits held between banks in the London market have been reduced significantly. A result of the financial crisis has been that the interbank deposit market stalled, and the quoted rates were to a great degree guessed, that is, based on an assumed rate that would be in place if the transactions were taking place. There have also been allegations of manipulation. In June 2012, multiple criminal settlements revealed significant fraud and collusion by member banks connected to the rate submissions, leading to the Libor scandal. This resulted in fines being imposed on some banks and prosecutions of individual traders.

Since the financial crisis, fewer market participants are willing to lend on an unsecured basis, particularly for a term longer than overnight (e.g., three-month). Liquidity in the interbank market has been reduced since the 1990s and disappeared entirely during the financial crisis. Banks have moved away from this market.

In light of the above, the EU introduced the 2016 Benchmarks Regulation, which secured control over benchmarks and their providers. It entered into effect on January 1 2018. This new regulation refers to indices used as benchmarks in financial instruments and financial contracts or to measure the performance of investment funds. It introduces a framework to ensure the integrity of benchmarks referenced in

If not well prepared, banks may face material risks

financial instruments, financial contracts or investment funds in the EU. The aim of this framework is to contribute to the improved functioning of the internal market. A high level of consumer and investor protection is an additional aim of this legislative effort. The relevant ARR concept in the EU is the euro short-term rate (€STR).

Moreover, there has been preparation for the operational substitution of Libor in various jurisdictions. In the US, the secured overnight financing rate (SOFR) launched in mid-2018, following the growing trend in trading in derivatives such as futures and swaps. A problem with SOFR is that the issuance of its notes is made mainly by state-linked entities and financial institutions, thus resulting in it having a rather exclusive nature.

In the UK, the replacement rate is called the sterling overnight index average (Sonia). The Bank of England administers this rate. In Switzerland, the relevant ARR is called Swiss average rate overnight (Saron) and it is a secured rate that reflects interest paid on the interbank overnight repo rate. In Japan, there is the Tokyo overnight average rate (Tonar), which is an unsecured rate that captures the overnight call market rate.

To summarise, on the one hand these initiatives, the function of which will be controlled by the authorities, will represent relatively risk-free overnight interest rates for lending to banks overnight and will be quoted daily early in the morning. On the other hand, however, all replacement efforts seem to suffer from a perceived lack of a forward-looking term rate.

The disruption in funding markets over the past few months has highlighted the importance of shifting from Libor to a new benchmark rate. The spreading Covid-19 pandemic can be seen as a potential obstacle to reform. However, in our view, this disruption has drawn some of Libor's flaws to the attention of analysts. It is expected that, in the context of the US government's rescue package for the US economy, the US Treasury will launch its first SOFR-linked floating rate notes this year to help fund increasing deficits.

Banks have been somewhat reluctant to submit quotes in the framework of a mostly inactive market, due to the risk of exposure to litigation. However, currently, the banks' ability to make the transition away from Libor by the end of 2021 is not clear, while the risks arising from the transition are increasing. If not well prepared, banks may face material risks, including unanticipated operational and conduct risks. The result of this could be reputational damage, fines, and lawsuits.

Banks are not the only ones that should be alerted to the dangers entailed of the upcoming transition. Market players should be cautious, in general, of the risks of the shift. One such risk is an excessive reliance on fallback clauses.

Fallback language consists of three key components: fallback trigger event, benchmark replacement, and benchmark replacement adjustment. Market participants may face increased operational risk if they finally rely on updated fallback clauses for their transition from Libor when Libor becomes unavailable. New interest payments, valuations, and collateral requirements calculations will be required, which means changes for thousands of contracts. Moreover, there are doubts about the level of consistency in fallback terms and triggers. New fallback language being drafted by industry bodies like ISDA [International Swaps and Derivatives Association] and the LMA [Loan Market Association] is an encouraging initiative; however, there might be discrepancies in fallback language for subsets of transactions, which could induce increased basis risk.

In addition to the fallback language, firms will also need to be cautious of other critical contractual matters that may have an impact on the shift, such as maturity dates, the firm's role in the contract, governing law and jurisdiction, and *force majeure* provisions. There will be broader needs for transitional documentation, which would permit a smoother succession from Libor.

Another aspect that should be highlighted is that the process of repapering will most probably be threatened by conduct risk and data complexity. Banks will require a full review of their exposures to each counterparty and the estimated economic impact of transition on all products and currencies. This may be particularly burdensome in cases of products related to different businesses and sectors of the economy.

The trading volume of products linked to Libor is expected to decrease as we approach 2021. Disengaging from these current positions may become more difficult as market activity will be reduced. Moreover, this reduction of liquidity will inevitably induce various changes to risks in corporate portfolios between now and the end of 2021. Market players should undertake initiatives to make the Libor transition faster, safer, and more efficient. Regulators should remove disincentives for market participants to switch from Libor-linked to ARR-linked derivatives.

The common view is that banks should develop loan products based on ARRs. For example, adjustments to interest observation periods may be necessary to achieve advance visibility on cashflows. At the time when ARRs are established, products utilising these rates could be added to allow customers (and banks) to make their choices. In the meantime, banks should avoid procrastination and complacency, as well as the assumption that there is plenty of time left to proceed with the transitions.

Currently, in Cyprus, the majority of credit positions utilise LMA standard wording, which is linked to Libor. Unfortunately, many corporate market participants in our country may not be that sophisticated, and may not appreciate the impact and plans for the shift.

It is estimated that the shift will have an impact of different kinds on transactions, across different products. This may engender the need for potentially costly changes to models, data, analytics and technology. Companies will need to apply inventory models across all departments that rely on Libor for updates. The appropriate approvals of any model changes should be obtained, while there should also be an improvement of current systems that may not be equipped to support contracts referencing ARRs. Such efforts will certainly be time-consuming to develop due to the complexity of bank systems and organisations.

Moreover, consistent methodology for renegotiation and appropriate programme governance structures with prudent board oversight, including stakeholders from all businesses that are expected to be impacted, will be necessary. The interested entities should develop a communication strategy for regulators, investors, and company personnel, that describes the company's transition plan and strategy. Companies that offer Libor-related finance to clients should develop plans to handle the way clients are approached on these matters, and to handle contract remediation so that clients are treated equitably.

Notwithstanding the progress that has been made, Libor-related products are still being sold across all currencies and jurisdictions. It seems unlikely that all Libor exposures will have been converted to the new reference rates by the end of 2021, or even that firms will have ceased engaging in Libor transactions. The industry will face considerable problems in transitioning legacy positions if meaningful volumes and liquidity have not developed in the alternative rate markets. This will significantly increase the risk caused by the probability of Libor discontinuation after 2021. Parties to Libor-based contracts may face unpredictable transfers of value, even with the adoption of new fallback clauses, which aim to – but cannot guarantee to – mitigate value transfer upon Libor discontinuation.

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Countermeasures against money laundering in trust agreements

On July 24 2019, based on a request from the Financial Services Agency (FSA), the Trust Companies Association of Japan – a financial association whose members comprise of financial institutions engaged in trust businesses – proposed sample provisions to deal with the risk of money laundering etc. in trust agreements. The outline of these sample provisions is as follows:

(a) In cases where the trust under the agreement is likely to be used for transactions that violate money laundering regulations, etc., if it is inappropriate to continue this transaction, the trustee may terminate the agreement.
(b) The trustee may make various inquiries and the submission of materials in order to collect information on the settlor, the beneficiary, etc. In the case where no response is provided by the settlor or the beneficiary without a justifiable reason, the trustee may terminate all or part of the agreement, or restrict part of the transaction.
(c) In the case where the trustee considers that there is a possibility of a violation of money laundering regulations, etc. in light of the responses of the settlor or the beneficiary to the various inquiries, etc. under paragraph (b), the trustee may terminate all or part of the agreement, or restrict part of the transaction.

In response to the proposal, some trust banks in Japan have already added these provisions to their template trust agreements. They are expected to become general market practice.

From the perspective of settlors and beneficiaries, the treatment of documents that are subject to obligations of confidentiality or decision-making documents (minutes of meetings of board of directors, etc.) will be an issue. Since (1) there is no restriction on the scope of materials that the trustee may request the settlor or the beneficiary to submit under paragraph (b) above, and (2) it is unclear in what circumstances the settlor or the beneficiary has a 'justifiable reason' to refuse to submit such materials, there is a possibility that the trustee may terminate the trust agreement or restrict part of the transaction if the settlor or the beneficiary refuses to submit such documents even if the settlor or the beneficiary believes that it has a justifiable reason. Accordingly, the operation of these provisions in actual practice (particular in relation to materials requested by the trustee) should be carefully monitored in order to establish and refine good market practice.

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Impact of the coronavirus in ongoing public contracts

Contractual relations between governments and the private sector are usually dictated by a strict set of rules and regulations, that are set in place as an assurance that the public interest is protected and that the public procedures are transparent and subject to the necessary advertising and competitive tendering requirements. In this context, the exceptional public health situation we are living in represents a true game changer, posing challenges to the existing legal frameworks and imposing upon governments the task to quickly adapt the regulatory system to provide answers to the ever evolving pandemic situation.

Therefore, and generally speaking, governments were quick to issue regulation on exceptional public procurement frameworks, mostly intended to simplify and therefore accelerate public procurement procedures required to respond to the SARS-CoV-2 or coronavirus epidemic, as a necessary measure to protect health and human life. This effort includes even supranational entities, like the European Commission, that on April 1 2020 publish welcome guidance clarifying the application of the public procurement framework during the pandemic.

Under the broad scope of the prevention, containment, mitigation and treatment of the epidemic, public procurement exceptional procedures were adopted in conjunction with several other measures that

The exceptional public health crisis we are living in represents a true game changer

included quarantine measures, limitation to travel, circulation, and social gatherings or the mandatory closure of existing establishments.

The issue at hand relates to the execution of ongoing public contracts, that was not addressed by the exceptional legal framework, but was affected or prevented by the current exceptional circumstances, namely but not limited to, by measures issued by the governments to respond to the pandemic.

Therefore, the current analysis is especially relevant in jurisdictions like Macau or Portugal, in which the legislative authority did not set a specific legal framework to regulate the performance of non-coronavirus-related public contracts during this crisis period, as well as its more long-lasting impacts.

The question we are facing is, to what legal constructions can the parties of public agreements resort, when confronted with an event that disturbs the performance of such agreement, and that is rooted, in any way, in the vicissitudes deriving from the extraordinary the measures undertaken by the government? We believe the main issues in this field relate to the potential modification, suspension of performance or termination of the agreements, as a result of such events.

In order to address the situation, we need to begin by analysing the nature of the event the parties face, namely to determine if the current pandemic – with all the measures and limitation imposed by the governments to counter it, can be deemed as a *force majeure* event.

It is broadly accepted that an event of force majeure is composed by a number of cumulative elements – it is an unforeseeable (on the day the contract is concluded), irresistible (both in its occurrence – unavoidable and in its effects – insurmountable) and external (to the parties) event.

It is not our intention to advocate that the mere existence of the virus could constitute an event *force majeure*. However, we believe that the current pandemic, combined with the administrative decisions implemented by the different jurisdictions to avoid its propagation, have indeed affected the daily lives of companies and citizens, and have likewise significantly hindered the world´s economy and the financial systems. Therefore, due to the exceptional – and thus unforeseeable, and imperative – nature of the different elements that compose the existing situation, we can indeed establish the occurrence of a *force majeure* event.

Following this conclusion, in the event we are faced with a breach of the contract by private contractor due to the impossibility of performance of the contract, the next step is to determine whether or not the event is causing the performance of the contract to be temporarily or definitively impossible, including situations of full or partial. As a general rule, in order to demonstrate that the full or partial non-performance is caused by the force majeure event, a causal link should exist between the failure to perform and the overall measures adopted in response to the epidemic and that hinder the performance of the contract.

In case the private contractor is able to prove the existence of the above mention link between the force majeure event and the default, it is exonerated from any potential liability deriving out of the non-perform of the relevant obligation.

Furthermore and, faced with a temporary impossibility to perform the contract, the suspension of performance of the contractual provisions may be agreed. In this event, the performance of the contract should be resumed as soon as the grounds for suspension terminate and typically the new deadline for the performance of the defaulted obligation should not be superior to the period initially agreed for the performance of such obligation added by any preparatory works necessary for the performance.

In line with what has been said about the measures undertaken by different jurisdictions to respond to the pandemic, we can however, identify situations whereby either by a unilateral decision of the governmental authority, such as the mandatory closure of existing establishments or, by an external an unpredictable event related to the current crisis, the performance of the agreement under the exceptional situation may cause an unexpected and significant increase in costs that the private contractor is required to bear, therefore increasing the burden of the execution of the agreement to this party. In these situations the equitable modification of the contract may be in order, as a means to restore the financial balance of the agreement.

The decision to modify a public agreement generally has three potential causes: an agreement between the parties, a judicial or arbitration decision, or by decision of the public contractor, in this case by reasons related to the public interest.

Moreover, and unlike private contracts, the fundamental principle that guides all procedures regarding public agreements is the pursuance of public interest: the whole regime imposing different procedures in procurement of different goods or services aims to assure the compliance and preservation of the public interest. Furthermore, the principle of competition constitutes an important guideline in the entire legal regime: as a general rule, the public administration has to adopt open tender as to better guarantee fairness as well as the better pursue of public interest. Therefore, any amendment to a public agreement must comply with severe guidelines; otherwise it may jeopardise the aforementioned principle.

Nevertheless, it is undeniable that part of the recognition of the mandatory force of a contract does not result exclusively from the will of the parties nor does it concern only the linked individuals. In fact, the legal value of contracts arises from the law and is conferred deriving out of their social utility, thus the agreement cannot dissociate itself from the general conditions in which it is celebrated and executed. Therefore, in the event there is an alteration on the circumstances of the agreement in such a manner the base of justice the parties agreed upon to execute the agreement is affected, the applicable legal regimen must intervene.

Subsequently, the validity of any modification of a public agreement must comply with both general principles, relating to the specific legal structure of the public agreement and specific requisites that concern the situation *in casu.*

Regarding the general principle, we must conciliate a double dimension: on the one hand, the principles of commutative justice and good faith, which must govern any contractual relationship; on the other it is also justified in the light of specific principles of administrative law, such as the principle of continuity of public services.

The key element for determining the possibility to modify a public agreement is not the subjective element linked to the common intention of the parties, but rather an objective element of commutative justice and contractual good faith, which constitutes the *raison d'être* of the legal mandatory force of any contract.

Furthermore, and to what concerns another dimension of the public interest, the possibility of modification serves an additional purpose: the purpose of the public contracts, i.e., the need for the agreements to be performed in a continuous and regular manner and in the most adequate way to satisfy the general interest. The amendment of the agreement must, therefore, serve the principle of pursuance of public interest – translated into the requirement for regular and continuous functioning of public services and the fulfilling of the collective needs.

In the event the modification of the agreement is duly substantiated by reasons of public interest, we must then verify the specific framework of the situation to ensure that it complies with the requisites for the modification of the agreement. Firstly, it must be determined if the event derives from the occurrence of an unforeseeable circumstance on the date of the conclusion of the contract, which determines an additional burden to be undertaken by private contractor to perform the agreement. Secondly, the event must be extraordinary in a matter that, as the French put it, causes a *bouleversement du contrat*, this is to say, profound disruption of the contractual economy.

Another element that must be weighed to determine whether the performance of the benefits has become or not excessively burdensome for the private contractor is that of the event does not fall under normal business risk, taking into account the type of contract (v.g., longer agreement are, in thesis, more subject to new circumstances), and any special conditions the parties have agreed to include in the agreement. Finally, the contract must still be susceptible of performance, i.e., the contract cannot have been rendered impossible to be performed.

Taking into account all of the above, regarding the conditions for the valid modification of public agreements in force previously to the pandemic, that have seen the balance of their respective obligations affected, we believe the current situation, previously qualified as an event of *force majeure*, may also be considered as the grounds for their modification. In this event, the private contractor must proceed with the performance of the contract and, concomitantly, the public contractor has an obligation to assist the co-contractor with the difficulties that such compliance presumes.

Regarding the public contractor´s duty to assist the contractor, it can take two forms: a readjustment of the contract, taking into account the economic difficulties affecting its performance, namely by means of an extension of a deadline for the compliance of the relevant obligations, an extension of the agreement itself, or a review of contract prices, or consist of the payment of a compensatory compensation for the excessive cost of compliance with the performance of the agreement.

Regarding the determination of the quantum of the applicable measure, first we must determine the exact moment from which the contractor is entitled to demand this compensation and then observe the specific characteristics of the event. As an example, and considering that the extension of public contract could be served as one of the possible ways to reestablish the economical-financial equilibrium of a specific agreement, there could be different approaches contingent to the specific situation. However, we believe two principles shall orientate this decision. On a positive stipulation, the measure shall allow for the necessary time for the private contractor to restore the financial proportion on which the contract was initially based; on a negative limit the restoring the financial balance of the agreement cannot place any of the parties in a more favorable situation than that resulting from the financial balance initially established.

To conclude, we are indeed undergoing extraordinary times. However the legal framework we have been analysing is designed to deal with situations that exceed the limit of what should be considered proportional and balanced in a contractual relationship. They are effectively composed by strict requirements, as they should be, and naturally contingent to the specifics of the situations, we believe there are legal grounds to effective subsume these legal concepts to public contracts affected by events related to the coronavirus pandemic.

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PANAMA

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Manufacturing services for multinational companies

Since its inception, Panama has positioned itself as a world-leading logistic services provider. This has been in part due to its privileged geographical location and connectivity, as well as to a solid pro-market and dollarised economy. A robust banking system and a responsible territorial fiscal regime have qualified Panama as an investment-grade country since 2010 – and it has since been upgraded by Moody's, Fitch Ratings and Standard & Poor's.

Panama has focused on supplementing its natural advantages with a variety of attractive and competitive special economic regimes aimed at promoting investments, such as the Colon Free Zone, The Panama Pacifico Special Economic Zone, The City of Knowledge, Free Trade Zones and Multinational Companies Headquarters (SEM). What makes them especially competitive is that each regime is tailored to suit different economic activities and offer

The MSM regime will provide an opportunity for qualifying companies to be a part of Panama's logistic services ecosystem

benefits that are adaptable to each sector. Some are ideal for research and development, others for logistics and distribution, and others for shared services' regional operations.

Recently the Panamanian government proposed a new regime focused on attracting multinational companies involved in manufacturing, assembly, maintenance, remanufacturing and conditioning of products, R&D and logistics services to companies from within the same business group. This regime, called Manufacturing Services for Multinational Companies (MSM), or *Régimen Especial para el Establecimiento y la Operación de Empresas Multinacionales para la Prestación de Servicios Relacionados con la Manufactura (EMMA)* in Spanish, seeks to emulate the Multinational Companies Headquarters (SEM) regime, which has been praised for its pro-business characteristics.

The MSM regime will provide an opportunity for qualifying companies to be a part of Panama's logistic services ecosystem and take advantage of a wide variety of incentives, such as:

- During the first five years, full exemption on the income tax. Thereafter, a five percent income tax rate applies;
- Exemption on dividend tax or complementary tax;
- Exemption on ITBMS (equivalent to VAT) on services rendered to recipients outside of Panama;
- Foreign executives holding an MSM visa will not count for the purposes of local limits on hiring of foreign and local employees;
- The ability for MSMs to physically establish their operations in other special economic zones and take advantage of the control and infrastructure benefits they offer;
- Automatic legal stability.

The MSM regime is still pending congressional approval but the government has expressed its confidence that such approval will be obtained soon. Once approved, the unique conceptualisation of this regime will boost Panama as a formidable competitor in the international trading and logistics playing field.

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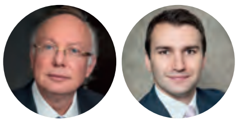

Daniel Futej and Daniel Grigel

Interim protection of business operators from Covid-related bankruptcies

Another set of measures came into force in Slovakia on May 12 to protect business operators from the fallout caused by Covid-19. These measures implement interim bankruptcy protections for business operators. These measures are temporary and as it stands, will expire on October 1 2020, with an option for the government to extend them through December 31 2020.

The primary purpose is to prevent a potential wave of creditor petitions for bankruptcy over business operators, and to that end the measure mandates that any bankruptcy proceedings initiated by creditors after March 12 will be suspended by law. In addition, a protected business operator will not be forced to file for bankruptcy. Existing law requires a business operator to file for bankruptcy within 30 days after becoming aware it is over-indebted, or after it could have become aware of that fact with the exercise of professional diligence. Creditors will not be able to exercise liens or pledges against a protected business operator and all enforcement proceedings commenced after March 12 against a protected business operator will be suspended; enforcement agents will also be required to unblock the bank accounts of the business operator. Creditors and experts alike have already voiced concern that this interim protection is disproportionate and significantly reduces the protection of creditors from non-paying debtors. The counter-arguments note that it is necessary to protect otherwise viable businesses whose problems objectively arose solely due to the coronavirus health crisis.

The interim protection is designed as an opt-in model, meaning that business operators will be required to apply for the protection at one of the four designated district courts using the form made available on the website of the justice ministry. If the application for interim protection meets all the lawful requirements, the court will provide the interim protection without delay (although no specific time period has been laid down) by issuing a confirmation of interim protection to the business operator and publishing the information in the Official Gazette.

The requirements for eligibility have been drafted broadly – for instance, the business operator is not required to attach any additional material to the application, such as a list of obligations or assets, that could be reviewed prior to approval of the interim protection in an effort to prevent abuse of the protection. Businesses will not be required to offer any evidence to the court in advance when applying for the protection. Potential abuse of the interim protection will be reviewed after it has been provided.

The court approving the interim protection will have the right, of its own initiative or on the suggestion of any third person, to decide on the early termination of the interim protection in cases where the requirements of the application were not met or if the protected business operator violates the obligations arising out of that protection. While under the interim protection, a business operator will be required to always give priority to creditors over the operator's own interests, and during the interim protection will not be permitted to take profit payouts, modify the structure of assets, or substantially reduce assets.

Creditors are concerned that the law does not specifically set out these obligations and/or criteria for termination of interim protection, and the decision is strictly in the court's discretion. The law also does not provide for a time period in which the court must decide on termination of interim protection or, what is likely an even greater danger, any specific penalties for debtors who abuse the interim protection or violate the lawful requirements during the protection.

All legal entities and sole traders who were not insolvent as of March 12 are eligible to apply for interim protection. Interim protection will not be available to business operators who were in financial difficulties and insolvent prior to the Covid-19 health crisis. Banks, insurance companies, pension fund management companies, and other financial market participants are barred from applying for interim protection.

The definition of insolvency provided in the Act on Bankruptcy and Restructuring will be applicable for matters concerning interim protection. This act defines two insolvency situations: inability to repay debts as they come due, and over-indebtedness. A legal entity is unable to repay debts if it is 30 days or more past due on its obligations to at least two creditors. A sole trader is unable to repay debts if they are 180 days or more past due on obligations to at least one creditor. Over-indebtedness is where a business operator has at least two creditors and the value of its obligations exceeds the value of its assets. However, total obligations do not include obligations owed to members, directors, and other related parties.

The rules of interim protection allow protected business operators to financially support their business through resources from related parties during the period of protection. In fact, if a business operator, despite interim protection, enters bankruptcy after the protection ends, the debts owed to related parties will not be considered subordinated debts but instead will be automatically satisfied in bankruptcy proceedings along with other normal creditor claims. The only limitation will be that in bankruptcy proceedings that follow the end of interim protection, any use of the business operator's assets to collateralise the claims of related parties will not be taken into account.

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Swiss withholding tax reform: move to a paying agent system?

Switzerland is generally an attractive business location from a tax perspective, however not when it comes to interest withholding tax on notes and bonds. The Swiss 35% withholding tax on interest payment is imposed not only on notes and bonds issued by Swiss borrowers, but can also, in certain circumstances, apply to notes and bonds issued by foreign group companies guaranteed by Swiss group companies.

In practice, the latter can generally be managed in case of upstream guarantees and – after a recent change in the withholding tax ordinance and the practice of the Swiss Federal Tax Administration – also in case of downstream guarantees by Swiss headquartered groups. However, notes by a Swiss issuer cannot be issued without triggering Swiss withholding tax on interest. The regime does not allow for a reduction / exemption of the 35% withholding tax at source. Swiss investors may normally either set off the withholding tax liability against their ordinary tax liability or request a refund. The position of international investors depends on the provisions of the applicable double tax treaty. Most of the Swiss double tax treaties provide for a full refund of the withholding tax on interest. However, the administrative procedure and costs for the refund process, as well as the liquidity disadvantage make Swiss bonds less interesting even for investors entitled to a full refund of the withholding tax, not to mention foreign and institutional investors.

This regime has long been criticised by Swiss multinationals, in particular because of the implementation of specific – temporary - withholding tax exemptions for bonds (CoCos/Tier 1 notes) issued by Swiss banks. The request to change the withholding tax regime was also clearly supported by the Swiss banks. In response to this critique, in June 2019, the Swiss Federal Council decided to resume the suspended reform of the Swiss withholding tax. The new proposal was published and submitted to the legislative consultation procedure by the Swiss Federal Council on April 3. The consultation procedure runs until July 10.

The main concept of the reform is that the withholding tax will no longer be deducted and paid by the borrower making the interest payment and instead by the paying agent of the investor, for example, a bank holding notes in depository accounts. No changes to the dividend withholding tax regime are contemplated. The 35% dividend withholding tax still has to be paid by the distributing Swiss entity (with the possibility to benefit from a reduction or exemption at source for distributions to significant Swiss or foreign corporate shareholders, the latter based on a double tax treaty).

Paying agent withholding tax regime

The basic principle of the new regime is as follows: a Swiss-based paying agent will be responsible for withholding and transferring to the tax authorities the withholding tax on interest payments made to individuals based in Switzerland.

The proposal suggests two essential changes to the scope of the withholding tax. First, only interest income of individuals based in Switzerland is subject to Swiss withholding tax. No withholding tax is due on payments to foreign-based investors (corporate or individual) and Swiss-based corporate investors. Secondly, the Swiss withholding tax will newly apply to domestic and foreign bonds and notes likewise, irrespective of whether such foreign bonds and notes are guaranteed by a Swiss parent or not.

The tax is due and must be deducted

Over the past few years, there have been movements towards the liberalisation the Swiss interest withholding tax regime

only by Switzerland-based paying agents. The reason for this rule is that the withholding tax in principle does not have a fiscal purpose and, instead, should provide an additional guarantee that Swiss residents comply with their ordinary income tax obligations. Hence, the full refund rights of Swiss residents, provided they declare the underlying income. The position is, of course, different in respect of foreign investors, who may not be entitled to a full refund. With the new proposal, the non-fiscal purpose of the Swiss withholding tax, at least in respect of interest payments, will remain in the foreground. In respect of the bonds/notes held with a non-Swiss based paying agents, it is assumed that the international automatic exchange of information on financial accounts (based on the multilateral convention on mutual administrative assistance in tax matters) would have sufficient preventive effect on possible tax evasion.

Typically, Switzerland-based financial institutions holding notes in depository accounts would qualify as paying agents. However, Switzerland-based issuers (provided no financial institution holds the notes), Switzerland-based portfolio managers, trustees and other Switzerland-based payors may also qualify as a paying agent.

In most cases, a paying agent acting for the holder of notes/bonds - i.e. as a rule a financial institution holding notes in depository accounts for its client - will qualify as a taxable person and will be obliged to withhold the tax. An exception to this rule applies in case of substitute payments (see below).

Trustee as a paying agent

The reform proposal explicitly indicates that a trustee would qualify as a paying agent. Therefore, payments made by issuers, banking institutions and other paying agents to a trustee are not subject to the Swiss withholding tax. Instead, the trustee as a paying agent becomes a taxable person and has to withhold and transfer the tax, provided it transfers, refunds, credits or pays out interest income to an individual based in Switzerland. The trustee must also withhold and pay the Swiss withholding tax in case interest income is transferred to the trust, and, although not distributed, is subject to income tax for a Swiss-resident settlor or beneficiary. This could be the case, for example, for the settlor of a revocable trust.

Investment funds and indirect interest income

Under the current regime, Swiss withholding tax is due only in respect of certain Swiss investment funds and some foreign funds; normally foreign contractual investment funds with fund management in Switzerland.

Under the new proposal, the regime for investment funds will become more complicated. First, income from all types of domestic investment funds will be subject to Swiss withholding tax. Excluded are capital gains and income from real estate (also excluded under the present regime) and interest income in accordance with a paying agent regime (i.e. provided that the paying agent is a taxable person and the income is paid to corporate or foreign investors). Secondly, indirect interest income received through domestic or foreign investment funds will also be subject to Swiss withholding tax, provided that such income is paid through a Switzerland-based paying agent to an individual based in Switzerland.

Further, the reform proposal requests that the indirect interest income subject to the withholding tax from structured products and investment funds is separately identified in order to enable the paying agent to deduct the withholding tax based on the residence of the investor. If the necessary identification data on the fund or structured product is not available, the full amount of income will be subject to Swiss withholding tax. The same rules apply to accumulated profits in case of accumulation funds. In this case, the withholding tax must be paid by a paying agent, even in the absence of the corresponding cash flow to the paying agent.

Substitute payments

The scope of the Swiss withholding tax will further be extended to include the substitute payments, i.e. payments that replicate capital assets subject to Swiss withholding tax, provided that the income is paid through a Switzerland-based paying agent. This concerns, for example, payments under securities lending and repo transactions, which replicate interest payments or Swiss-source dividends. Withholding tax on substitute payments for Swiss-source dividends under a security lending is already currently paid, however, based on practice applied by Swiss financial institutions. This practice will be implemented in the Withholding Tax Act in course of the reform. Substitute payments will be subject to the paying-agent regime. However, substitute payments, which replicate Swiss-source dividends cannot profit from the usual exemption, i.e. payments to foreign and corporate investors remain subject to Swiss withholding tax.

Further, as an exception to the general rule, the paying agent of the debtor and not the holder qualifies as a taxable person in case of substitute payments.

Voluntary application of the paying agent regime

For Switzerland-based issuers of notes and collective investment schemes, the change to a paying agent-based regime is voluntary. These parties can choose whether they will continue to apply the currently existing debtor-based regime or will switch to the paying agent regime. No such choice is provided to foreign issuers, foreign collective investment schemes or in respect of structured products and substitute payment – in all these cases the application of the paying agent regime is mandatory.

Position of the paying agents

One of the more problematic provisions of the reform is the position of the paying agents. Under the new regime, the paying agent becomes a taxpayer and bears the ultimate liability, including criminal liability, for the correct withholding and transfer of the withholding tax. The issuer, on the other hand, is discharged from any liability in the event of non-compliance. In that respect, the new paying agent regime is fundamentally different from the existing arrangements where a paying agent, normally an agent of an issuer, performs withholding and reporting under a service agreement.

The reform seeks to alleviate the position of the paying agent with a number of measures. First of all, the paying agent will only be subject to criminal liability in case of non-compliance for intentional violations. Under the normal rules, taxpayers are subject to criminal liability also in case of negligent violations. This relief seeks to address in the first instance the situation of incorrect interpretation of law or facts, e.g. when a paying agent erroneously determines that a particular product or payment is not subject to the withholding tax. This, however, does not release the paying agent from its obligation to deliver the withholding tax due.

Further, the proposal provides for a time-limited compensation to the paying agents at the cost of the federal budget. For a certain period, which is yet to be determined, after the new law comes into force, paying agents will be entitled to retain a portion of the withholding tax as a compensation for the implementation costs of the regime. The exact percentage of such compensation is yet to be determined.

After the expiry of this grace period, paying agents will be expected to shift the costs to the clients or carry them themselves.

Future outlook

Over the past few years, there have been movements towards the liberalisation of the Swiss interest withholding tax regime. For example, in 2019 the Swiss Federal Tax Administration introduced a new beneficial practice on the use of proceeds in Switzerland with respect to foreign bonds, guaranteed by a Swiss parent company. This was already a move in the right direction and facilitated to a certain extent the external financing for Swiss headquartered groups. However, the long discussed abolition of the Swiss withholding tax on interest with respect to foreign or Swiss corporate lenders/noteholders and change to a paying agent system for Swiss individuals is still required to enable Swiss companies to directly issue notes through Swiss vehicles. The April 2020 proposal tries to find a viable solution, and, if introduced, it will become more attractive for Swiss companies to raise financing out of Switzerland.

Nevertheless, the reform also contain a number of issues, which need to be fixed or clarified. For example, the funding of withholding tax in case of accumulating funds and in case of trusts may be practically problematic, especially taking into account that Swiss withholding tax amounts to 35%. The rules in respect of liability of the paying agents and the provisions concerning indirect interest income, structured products and foreign investment funds should definitely be discussed in the current consultation process and be subject to further clarifications – hopefully without jeopardising the long-awaited reform project itself, but by finding viable and practical compromises and solutions for the involved stakeholders.

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VIETNAM

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Kazuhide Ohya, Michael Douglas and Cao Bao Tran

New merger filing regulations

On March 24, the Vietnamese government issued Decree 35/2020/ND-CP (Decree 35), which took effect on May 15 and contains detailed guidelines on the implementation of the Law on Competition No. 23/2018/QH14 (2018 Law on Competition). This article gives a brief overview of some key features of merger filings addressed in Decree 35, as well as some practical observations.

New notification thresholds

Decree 35 establishes new thresholds for transactions – primarily in the form of mergers, consolidations, acquisitions and joint ventures – that, if met, must be notified to the soon-to-be-established National Competition Commission (NCC), which will be tasked with overseeing economic concentration in Vietnam, prior to implementation. Notably, a distinction is made between financial thresholds for credit institutions, insurers and securities companies on one hand, and all other enterprises on the other. For parties participating in the transaction that are *not* credit institutions, insurers or securities companies, notification is required if:

- the party's total assets in the Vietnamese market – or that of its affiliated group – was VND 3 trillion (US$130 million) or more in the financial year preceding the year in which the transaction is proposed to take place;
- the party's total turnover of sales or purchases in the Vietnamese market – or that of its affiliated group – was VND 3 trillion (US$130 million) or more in the financial year preceding the year in which the transaction is proposed to take place; or
- the value of the transaction is VND 1 trillion (US$43 million) or more.

For insurers and securities companies, however, the relevant financial thresholds for total assets, total turnover, and transaction value are higher.

For credit institutions, these thresholds are expressed as a percentage of the relevant figure for the entire credit institution system in Vietnam, rather than as a standalone absolute value as described above. Accordingly, the asset and turnover thresholds applicable to credit institutions are 20% or more of the total asset or turnover of the credit institution system in the Vietnamese market for the financial year preceding the year of the transaction; and the transaction value threshold applicable to credit institutions is 20% or more of the total charter capital of the credit institution system in the Vietnamese market for the financial year preceding the year of the transaction.

For all parties, whether credit institutions, insurers, securities companies or others, notifications to the NCC are also required if the combined market share of the participating parties was 20% or more of the relevant market for the financial year immediately preceding the year of the transaction.

Other than transaction value, the foregoing notification thresholds are also applicable to transactions conducted outside

Decree 35...provides welcome guidance on the 2018 Law on Competition

Vietnam. For example, a transaction between two non-Vietnamese entities that have no physical presence in Vietnam may still be required to make a merger filing in Vietnam if one of the involved entities (or its affiliated group) has a nexus to Vietnam. This could be in the form of sales conducted in Vietnam that generate a turnover exceeding the applicable threshold for merger filing under Decree 35. However, the decree does not provide any guidance on the type of nexuses that would require a merger filing.

Unlike in other jurisdictions, in Vietnam, notification thresholds reflect multiple metrics. As such, parties are required to examine sales amounts, asset values, transaction value, and market share information, which may be burdensome.

Two-phase review process

Transactions requiring notification to the NCC must now go through a review process, which begins with a preliminary 30-day review. The NCC has seven working days upon receiving the merger filing dossier to make a request for information (RFI) in case it is incomplete. The parties then have another 30 days to amend or supplement it. If they fail to do so, the NCC will reject the merger filing. The preliminary 30-day review period can only begin once the NCC is satisfied that the dossier is valid and complete.

If no decision is issued by the NCC within the 30-day period, the transaction may proceed. However, if the NCC issues a notice of non-approval, this will trigger an official 90-day review period. This occurs when the proposed transaction does not meet at least one of the following four criteria:

- the combined market share of the participating parties is less than 20% in the relevant market;
- the combined market share of the participating parties is 20% or more in the relevant market but the Herfindahl–Hirschman index (i.e., the total market share squares of the parties) in the relevant market following the transaction is less than 1,800;
- the combined market share of the participating parties is 20% or more in the relevant market, the Herfindahl–Hirschman as a result is higher than 1,800, but the increase in the Herfindahl–Hirschman index is less than 100; or
- the market share of the participating parties that have a vertical relationship with each other in the chain of production, distribution and supply of a specified type of good or service, or whose business lines provide mutual inputs or provide ancillary support to each other, is less than 20% in each relevant market.

The NCC has the power to stop the clock during the official 90-day review process by requesting additional information and materials. Unlike in some other jurisdictions, such as the US, the NCC is able to make such a request twice.

Decree 35 does not state for how long the 90-day period may be tolled or give any indication as to how burdensome the requests might be. Since the enactment of the 2018 Law on Competition (July 1 2019), only a small number of merger filing dossiers have been submitted, but it is unclear whether any of these submissions have undergone an official review.

Decree 35 also fails to indicate what sources of statistics are approved by the NCC for the identification of market share in the review process.

Although the 2018 Law on Competition and Decree 35 do not provide for preliminary consultations and draft checks, it is common practice in Vietnam to unofficially consult with the competition authority before submitting a merger filing dossier. Officials from the Vietnam Competition Authority, the predecessor to the NCC, have been helpful during the unofficial consultation process.

Definition of controlling or governing

Prior to Decree 35, it was unclear to what extent the acquisition of capital contributions or assets of a target company could be deemed to give the acquirer the ability to 'control or govern' the target for the purposes of determining economic concentration. Decree 35 now defines "controlling or governing" as the acquisition of:

(i) more than 50% of the charter capital or voting shares of the target;
(ii) more than 50% of the assets of the target in all or one of its business lines;
(iii) the right to directly or indirectly appoint, remove, or dismiss the majority of the board of management, the chairperson of the members' council, or the director or general director of the target; or
(vi) the right to decide any amendment to the charter of the target or certain enumerated matters in the course of business activities of the target.

This new definition of "controlling or governing" is now clearer but broader. For instance, the decision-making rights mentioned in items (iii) and (iv) do not hinge on any particular equity threshold as defined in Decree 35. A literal reading of the decree suggests that a person could be deemed to control or govern a target company with a minority investment if such person has any of such decision-making rights.

In addition, while Decree 35 does not specify whether veto rights fall within the legal definition of 'controlling or governing', anecdotal evidence strongly suggests that they will. Parties contemplating a minority investment in a target company that involves veto rights should therefore officially consult with the competition authority to get confirmation as to whether the contemplated minority acquisition will be deemed to be an acquisition that triggers a merger filing.

Decree 35 is now effective and applicable to transactions conducted both in Vietnam and abroad. While numerous points require further clarification, it provides welcome guidance on the 2018 Law on Competition. Further guidance is expected to be issued as it begins to be implemented.

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Back on the road again?

In the last edition of IFLR, published in early March, we wrote about how the world was reaching peak hysteria as the effects of the coronavirus began to take hold. Concerns at the time were of office closures and restrictions on travel to and from China and Hong Kong SAR.

How naïve that now feels. Yet things do appear to slowly (or quickly if you live in Florida) be returning to normal. Inevitably, some things will come back in different forms; some will not come back at all.

One potential casualty of the virus that probably won't be mourned for too long is the initial public offering (IPO) roadshow. Investopedia's definition of a roadshow is "a series of presentations made in various locations leading up to an IPO" which acts "as a sales pitch to potential investors by the underwriting firm and executive management team of the company about to go public" – which breaks just about every social distancing rule there is.

With CEOs and their teams unable to traverse the globe to find investors and pitch their companies in remote conference centres, the industry has taken the entire process online. The plethora of online seminars and conferences may be getting tiring as the months go on, but one can imagine it beats giving the same presentation over and over again, fresh off a flight, likely on just a few hours' sleep.

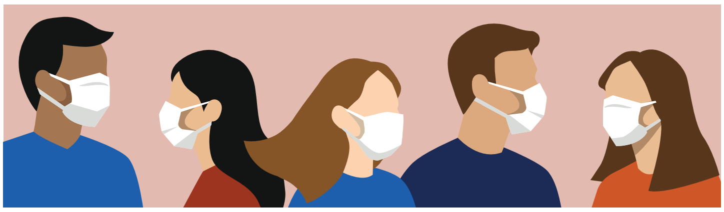
The virtual roadshow concept has of course had its issues, like every other virtual meeting, but overall the sentiment has been positive. As Abhimanyu Bhattacharya, partner at Khaitan & Co in India wrote on LinkedIn: "Despite the hiccups, it has been reported that some issuers are relieved that they do not have to participate in a 'choreographed pandemonium' in which you conduct 50 meetings in about 10 days flying in and out of cities. The traditional IPO roadshow is under an existential threat." The question is whether that would be such a bad thing.

A New York cover-up

Anyone with a vested interest in New York, or indeed the United States, will be familiar with governor Andrew Cuomo's daily address to the people of New York from state capital Albany over the last few months.

However, one step taken by the governor very nearly caused the most unlikely of legal conflicts. On April 15 Cuomo issued an executive order requiring all people in the state to wear masks or face coverings in public: a necessary step in the battle against the invisible enemy.

Unfortunately, NY Penal Law 240.35(4), a nearly two-century-old statute that deems it a criminal violation for groups of individuals to wear masks in public – with the risk of a 15-day prison sentence – directly contradicted this.



"Wearing masks in public remains necessary for the health and safety of New Yorkers. But there was a clear conflict of law, and repealing this outdated provision is commonsense policy," wrote attorney-general Letitia James in a letter to Cuomo. "Even if it is difficult to imagine a police department enforcing, a prosecutor charging, or a judge upholding such a charge during the Covid-19 crisis, we should not tolerate a situation where following the law is dangerous."

Towards the end of May, New York state senator Jamaal Bailey took steps to remedy the problem by passing legislation expressly repealing that part of the existing statute. "This is a disaster waiting to happen," said assembly member Dan Quart. "Not only is the continued criminalisation of face coverings confusing for all New Yorkers, it exposes men of colour to police harassment. If we are to stop the spread of Covid-19, we must ensure that everyone feels safe wearing a mask in public, without the threat of arrest, prosecution, or worse."

This is just one of countless ways in which the pandemic is shaping the world we live in: rewriting social norms, business practices, and now legislation itself.

The quarter in numbers

99%	fall in UK deal value from March 2020, the lowest in 35 years
2 million	number of confirmed cases in the US at time of writing
3.3%	contraction in global GDP for 2020 as predicted by BNP Paribas
$2.4 trillion	extent of US government virus related stimulus in mid-May
2	coronavirus cases in New Zealand at the time of writing
13.5%	forecasted growth of Brazilian credit card debt following Covid-19

Heard something that deserves a mention in Closing Conditions? Let us know at elizabeth.meager@legalmediagroup.com

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