



ICLG

The International Comparative Legal Guide to:

Project Finance 2018

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A practical cross-border insight into project finance

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Japan



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1 Overview

1.1 What are the main trends/significant developments in the project finance market in your jurisdiction?

After the introduction of a feed-in tariff for renewable energy in July 2012, photovoltaic (PV) power projects have been the main target for project finance in Japan. Since around the second half of 2014, however, the momentum for such projects has subsided, mainly due to the over-supply of PV power that led to decreased sales prices since 2012 and a newly enacted uncompensated and unlimited restriction on power supply. Recently, projects investing in renewable energy other than PV power, such as wind power and biomass power, have started to attract attention.

Since its introduction in 2011, the “concession right” scheme, in the field of public-private partnership (PPP) and private finance initiative (PFI) projects, has undergone further development. The concession right scheme is a scheme that enables a public entity to confer upon a private entity concession rights to operate and maintain existing facilities by financially relying on users’ fees. The leading examples of where concession rights have been granted are Sendai Airport and Kansai and Osaka International Airports, further detail of which is set out in question 1.2 below. Expectations are that in the coming years water supply services, sewage services, highways and other airports will also become subject to the concession right scheme.

1.2 What are the most significant project financings that have taken place in your jurisdiction in recent years?

As mentioned above in question 1.1 above, Kansai and Osaka International Airports were monumental transactions in terms of their scale. The concession right to operate Kansai and Osaka International Airports, for a term of approximately 44 years, was conferred on a special purpose company (SPC) established by a consortium consisting of ORIX Corporation and VINCI Airports S.A.S. in December 2015 for a consideration of approximately JPY 2,200 billion in total, paid over the 44-year term. The SPC commenced operation in April 2016.

2 Security

2.1 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

It is possible to create security interests by means of a general

security agreement, as long as each asset is clearly specified therein. However, the security interest in each type of asset must be perfected separately.

2.2 Can security be taken over real property (land), plant, machinery and equipment (e.g. pipeline, whether underground or overground)? Briefly, what is the procedure?

(1) Real property (land)

Under Japanese law, the typical security interest in real property is a mortgage (*teito-ken*). For a revolving facility with a maximum claim amount (*kyokudo-gaku*), a revolving mortgage (*ne-teito-ken*) is applicable.

A mortgage in respect of land or a building is created by an agreement between a mortgagor and a mortgagee. In order to perfect the mortgage against a third party, the mortgage must be registered with the Legal Affairs Bureau (LAB) having jurisdiction over the property. There are approximately 500 LABs throughout Japan.

It should be noted that the land and any building on the land are treated independently of each other. It is, therefore, important to separately create and perfect the mortgage as a first lien upon both the land and the building.

(2) Plant

A typical “plant” consists of land, a building, machinery and equipment. As mentioned above, land and a building can be collateralised by a mortgage (*teito-ken* or *ne-teito-ken*). Machinery and equipment are classified as movables, and can be collateralised by assignment as security (*joto-tanpo*) (discussed below).

In addition, Japanese law provides for two comprehensive security interests for property located in a factory. One is a factory mortgage (*kojo-teito-ken*), and the other is a factory estate mortgage (*kojo-zaidan-teito-ken*). A factory mortgage over land covers all machinery and equipment located in the factory. A factory estate mortgage is a particularly strong security interest that can actually eliminate pre-existing security interests over movables in the factory estate. Notice regarding the factory estate mortgage is published in the Japanese official gazette and if an existing security interest holder fails to object within a certain period (specified as being from one to three months), that party’s existing security interest is extinguished. Both a factory mortgage and a factory estate mortgage require each piece of machinery and equipment to be identified, and therefore require more burdensome procedures and costs than normal mortgages. The factory mortgage and factory estate mortgage are not very common and are used mostly for large factories.

(3) Machinery and equipment

Machinery and equipment are movables. Movables can be collateralised by way of assignment as security (*joto-tanpo*). This security interest can be created by a security agreement between an assignor and an assignee. In order to perfect this security interest, the target movable must be “delivered” from the assignor to the assignee. Delivery can be made by (i) physical delivery, (ii) constructive delivery, or (iii) (where the assignor is a legal entity (including a company)) if a movable assignment registration (*dosan-joto-toki*) is filed with the LAB, the registration itself is deemed to be delivery from the assignor to the assignee. The LAB located in the Nakano Ward of Tokyo is the exclusive designated LAB for any movable assignment registration.

In creating a *joto-tanpo*, it is necessary to identify the target movable by whatever means is sufficient to specify it, such as the kind of movable, its location, number and so forth. This identification rule is also applicable to perfect the *joto-tanpo* by way of physical or constructive delivery. In perfection by movable assignment registration, there are two statutory ways to identify the target movable: (i) specification by both the kind of movable and by a definitive way to specify the target (such as a serial number); and (ii) specification by kind of movable and its location. The former is usually used for a fixed asset, and the latter is usually used for inventory (aggregate movables).

2.3 Can security be taken over receivables where the chargor is free to collect the receivables in the absence of a default and the debtors are not notified of the security? Briefly, what is the procedure?

A security interest in receivables (claim) may be taken by a pledge (*shichi-ken*) or assignment as security (*joto-tanpo*). These security interests can be created by a security agreement between the pledgor/assignor and pledgee/assignee.

In creating the security interest, it is necessary to sufficiently identify the target receivable to specify it (such as kind of movable, date of origination and other items to the extent applicable). If the target is a claim to be generated in the future (*shorai-saiken*, “future claim”), the period (the beginning and end dates of the period during which the claim will be generated) must be specified in the security agreement and in connection with perfection. If there is an agreement made between the debtor and the obligor of the target receivable which prohibits a pledge/assignment of the target receivable, the pledge/assignment is basically invalid, with two exceptions: (i) if the pledgee/assignee is unaware of the prohibition agreement without gross negligence on the part of the pledgee/assignee, the pledge/assignment shall be valid; and (ii) the pledge/assignment will become valid retroactively from the time of the pledge/assignment (to the extent not harmful to a third party) if the obligor of the target receivable consents to the pledge/assignment, even if there has been a prohibition agreement.

The pledgee/assignee can assert the security interest **against the obligor of the target receivable** upon (i) notice to the obligor from the pledgor/assignor, or (ii) the acknowledgment of the obligor. The pledgee/assignee can assert the security interest **against a third party** (such as a double pledgee/assignee or bankruptcy trustee of the pledgor/assignor) upon (i) notice to the obligor of the target receivable from the pledgor/assignor by a certificate with (a stamp of) a fixed date, (ii) the acknowledgment of the obligor of the target receivable by a certificate with (a stamp of) a fixed date, or (iii) (only where the pledger/assignor is a legal entity (including a company)) a claim pledge/assignment being registered with the special LAB located in Nakano Ward of Tokyo. The registration can be made with the LAB upon creation of the security interest without notice to the obligor. In such a case, practically, the notice to the obligor of the

target receivable will be sent upon the event of default of the pledgor/assignor, and the notice must be accompanied by a registration certificate (this notice can be sent by the pledgee/assignee).

2.4 Can security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Yes, a pledge over cash deposits is commonly used. A pledge over deposits is created by a pledge agreement between a depository bank and a depositor and perfected by a notice to, or acknowledgment by, a depository bank with a stamp of fixed date. The validity of a pledge over an ordinary deposit (*futsu-yokin*) has been debated but no Supreme Court decision addressing this issue exists. Despite this, such pledges are often used for project financing.

2.5 Can security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Briefly, what is the procedure?

Shares of stock companies (*kabushiki-kaisha*) incorporated in Japan can be pledged or assigned as security (*joto-tanpo*), and pledges are relatively common. The articles of incorporation of the company will specify whether the shares are represented by physical certificates. If the shares are “certificated” (i.e., if physical certificates representing the shares are issued or will be issued), then a pledge can be created by physical delivery of the certificates to the pledgee, and perfected by continuous possession of the certificates by the pledgee.

On the other hand, if the shares are not and will not be certificated, a pledge may be created by a security agreement between the pledgor and pledgee, and perfected by registration of the pledge on the issuer’s shareholders’ list.

It is not expected that a project company conducting project finance transactions would be a listed company. If it is listed, however, the shares of a listed stock company are managed in a book-entry system electronically and the pledge over the shares are created and perfected in the system.

In each case, the stock company’s approval is not necessarily required upon creation of the pledge, but will be needed when the pledge is to be enforced. For security assignments, the issuer company’s approval will be necessary at the time of its creation as well as its enforcement.

2.6 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets (in particular, shares, real estate, receivables and chattels)?

Registration taxes are imposed on (i) mortgage registrations (0.4% of the claim amount (or, for a revolving mortgage, 0.4% of the maximum claim amount)), (ii) movable assignment registrations (JPY 7,500 per filing (up to 1,000 movables)), and (iii) claim assignment registrations (JPY 7,500 per filing (up to 5,000 claims) and JPY 15,000 per filing (exceeding 5,000 claims)). Creation of assignment as security (*joto-tanpo*) over claims may be subject to a fixed stamp duty of JPY 200.

2.7 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

No, except for the factory estate mortgage, which requires the procedures discussed in question 2.3 above.

2.8 Are any regulatory or similar consents required with respect to the creation of security over real property (land), plant, machinery and equipment (e.g. pipeline, whether underground or overground), etc.?

No regulatory consents are required to grant security, except for general consents for transfers required by the terms of the asset itself (such as licences).

3 Security Trustee

3.1 Regardless of whether your jurisdiction recognises the concept of a “trust”, will it recognise the role of a security trustee or agent and allow the security trustee or agent (rather than each lender acting separately) to enforce the security and to apply the proceeds from the security to the claims of all the lenders?

A security trustee is recognised under the Trust Law of Japan. In practice, however, a security trust scheme is not commonly used, mainly due to a lack of precedents.

3.2 If a security trust is not recognised in your jurisdiction, is an alternative mechanism available (such as a parallel debt or joint and several creditor status) to achieve the effect referred to above which would allow one party (either the security trustee or the facility agent) to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

See question 3.1 above.

4 Enforcement of Security

4.1 Are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction or the availability of court blocking procedures to other creditors/the company (or its trustee in bankruptcy/ liquidator), or (b) (in respect of regulated assets) regulatory consents?

In principle, security shall be enforced through a court-supervised auction (*keibai*). However, it is possible and common to agree to enforce security without a court-supervised auction, such as by way of a private sale.

4.2 Do restrictions apply to foreign investors or creditors in the event of foreclosure on the project and related companies?

No, there are no such restrictions.

5 Bankruptcy and Restructuring Proceedings

5.1 How does a bankruptcy proceeding in respect of the project company affect the ability of a project lender to enforce its rights as a secured party over the security?

There are three types of bankruptcy proceedings: bankruptcy

(*hasan*); civil rehabilitation (*minji saisei*); and corporate reorganisation (*kaisha kosei*). Under both bankruptcy (*hasan*) and civil rehabilitation proceedings (*minji saisei*), secured creditors can enforce their own security interests outside the proceedings (*betsujo-ken*) unless the court orders the deletion of the security interest in response to the petition by a bankruptcy trustee under certain limited requirements. On the other hand, under corporate reorganisation proceedings (*kaisha kosei*), the enforcement of security interests is prohibited or suspended (*kosei-tanpo-ken*).

5.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g. tax debts, employees' claims) with respect to the security?

A bankruptcy trustee may exercise clawback rights (*hinin-ken*). With respect to the security, if a debtor repays its debts, or grants security to a specific creditor after becoming “unable to pay its debts” and being aware of such situation, or after a bankruptcy filing (or grants security without obligation or repays debts before maturity within 30 days prior thereto), then such act may be avoided by the bankruptcy trustees. Administrative expenses, pre-bankruptcy adjudication taxes, certain labour costs, etc. are treated as claims that have priority over general claims, but secured creditors have priority over the collateral irrespective of the existence of these claims.

5.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

No, there are no such exclusions.

5.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of the project company in an enforcement?

As set out in question 5.1 above, secured creditors can enforce their own security interests outside bankruptcy (*hasan*) or civil rehabilitation proceedings (*minji saisei*).

5.5 Are there any processes other than formal insolvency proceedings that are available to a project company to achieve a restructuring of its debts and/or cramdown of dissenting creditors?

Turnaround alternative dispute resolution (ADR) proceedings (or business turnaround ADR) are a method overseen by the Japanese Association of Turnaround Professionals that can be used to restructure an insolvent business without involving courts. The process works by forming an agreement between the insolvent business and its creditors that includes debt write-offs and the rescheduling of debt payments.

5.6 Please briefly describe the liabilities of directors (if any) for continuing to trade whilst a company is in financial difficulties in your jurisdiction.

Directors are liable against the company if they breach their duty of care as a good manager; however, this can be tempered by the application of the business judgment rule to directors' decisions. Also, directors are liable against third parties for any loss or damages incurred by a third party due to a director's wilful misconduct or gross negligence. Criminal liability would arise in certain limited cases where directors intentionally breach their duty and cause damages to the company.

6 Foreign Investment and Ownership Restrictions

6.1 Are there any restrictions, controls, fees and/or taxes on foreign ownership of a project company?

A foreign investor is required to lodge a filing if it obtains shares in a non-listed company, obtains more than 10% of shares in a listed company, or conducts certain other activities under the Foreign Exchange and Foreign Trade Act. Investment in certain types of businesses (such as electricity, mining, oil, gas, water supply, transportation, telecommunication and shipbuilding) requires prior filing with the Japanese government. Investment in certain industries (such as telecommunications, airlines and broadcasting) is subject to maximum shareholding restrictions.

6.2 Are there any bilateral investment treaties (or other international treaties) that would provide protection from such restrictions?

While Japan has executed bilateral investment treaties with certain countries, these treaties do not provide protection from the restrictions noted above.

6.3 What laws exist regarding the nationalisation or expropriation of project companies and assets? Are any forms of investment specially protected?

Expropriation may be permitted for a limited public interest (such as transportation, electricity facilities and airlines) under the Compulsory Purchase of Land Act, with compensation provided. No form of investment is specially protected.

7 Government Approvals/Restrictions

7.1 What are the relevant government agencies or departments with authority over projects in the typical project sectors?

The relevant government agencies or departments will vary depending on the types of projects over which regulatory bodies in the state or local government have authority. Among the agencies and departments, the Ministry of Economy, Trade and Industry (METI) is the responsible authority in relation to matters such as energy, natural resources and other industries, and the Ministry of Land, Infrastructure, Transportation and Tourism (MLIT) is the responsible authority in relation to matters such as construction, transportation and ports.

7.2 Must any of the financing or project documents be registered or filed with any government authority or otherwise comply with legal formalities to be valid or enforceable?

Financing or project documents do not generally require registration or filing with any governmental authority. However, a guarantee agreement must be executed in writing, and perfection of security rights may require registration with the relevant authority. Stamp duty may be imposed depending on the type of financing or project documents if they are executed in Japan.

7.3 Does ownership of land, natural resources or a pipeline, or undertaking the business of ownership or operation of such assets, require a licence (and if so, can such a licence be held by a foreign entity)?

Ownership of land or a pipeline does not require a licence. However, development or, in some situations, the acquisition of land, as well as the instalment or operation of pipelines, are subject to various regulations such as agricultural land regulations and pipeline business regulations. While these matters are regulated by various acts, a licence is generally required for the extraction of natural resources and the operation of pipelines. A licence under the Mining Act is given only to Japanese nationals. On the other hand, activities for quarrying and/or gravel gathering, subject to local regulations, can be performed by a registered foreign entity. Acquisition of an oil pipeline or gas pipeline business is subject to a pre-notice filing requirement under the general restrictions of the Foreign Exchange and Foreign Trade Act and may also be subject to a suspension order in case it disturbs public order.

7.4 Are there any royalties, restrictions, fees and/or taxes payable on the extraction or export of natural resources?

Fees apply depending on the mining activities. Certain prefectural and municipal mining taxes are payable on the extraction of natural resources, as applicable. The rates for these taxes may vary depending on the location and the resource, but in general, a prefectural tax is imposed on the area of the allotted mining area, and a municipal tax, the standard rate of which is 1% of the relevant mineral price, is also imposed.

There are no general export restrictions relating to natural resources, provided that they do not fall into the exceptional categories regulated under the Export Trade Control Ordinance. No tax is imposed on the export of natural resources.

7.5 Are there any restrictions, controls, fees and/or taxes on foreign currency exchange?

No, other than a *post facto* filing under the Foreign Exchange and Foreign Trade Act.

7.6 Are there any restrictions, controls, fees and/or taxes on the remittance and repatriation of investment returns or loan payments to parties in other jurisdictions?

Generally no, but a *post facto* filing is required under the Foreign Exchange and Foreign Trade Act if the remittance exceeds JPY 30 million. Withholding of Japanese income tax at the rate of 20.42% (including special reconstruction income tax) will be taxed for dividends and interest paid to foreign lenders, unless a double tax treaty applies.

7.7 Can project companies establish and maintain onshore foreign currency accounts and/or offshore accounts in other jurisdictions?

Yes, they can, but a report is required to be filed with the tax authority if the offshore assets exceed JPY 50 million.

7.8 Is there any restriction (under corporate law, exchange control, other law or binding governmental practice or binding contract) on the payment of dividends from a project company to its parent company where the parent is incorporated in your jurisdiction or abroad?

No, there is no such restriction.

7.9 Are there any material environmental, health and safety laws or regulations that would impact upon a project financing and which governmental authorities administer those laws or regulations?

There are various regulations including local prefectural or municipal regulations that handle environment, health and safety issues. The necessity of an environmental impact assessment under state or local regulations would have a big impact on the costs and schedule of a project financing. Regulations on certain areas (such as forest areas and agricultural land) would also affect the project financing. Environmental matters are generally handled by the Ministry of the Environment (MOE) and/or similar environmental division at the local government level, and health and safety matters are generally handled by the Ministry of Health, Labour and Welfare and similar divisions at the local government level.

7.10 Is there any specific legal/statutory framework for procurement by project companies?

No, privately owned project companies are not subject to such procurement regulations.

8 Foreign Insurance

8.1 Are there any restrictions, controls, fees and/or taxes on insurance policies over project assets provided or guaranteed by foreign insurance companies?

Except for certain exceptions, foreign insurers are, in principle, required to obtain insurance business licences as a condition to underwriting insurance relating to project assets located in Japan.

8.2 Are insurance policies over project assets payable to foreign (secured) creditors?

Insurance policies over project assets can be generally payable to foreign creditors.

9 Foreign Employee Restrictions

9.1 Are there any restrictions on foreign workers, technicians, engineers or executives being employed by a project company?

Foreign workers, technicians, engineers or executives may be employed by a project company as long as it obtains an appropriate visa (certificate of eligibility). The visa requirements vary depending on the type of visa.

10 Equipment Import Restrictions

10.1 Are there any restrictions, controls, fees and/or taxes on importing project equipment or equipment used by construction contractors?

Construction contractors may generally import project equipment, except for limited restrictions such as goods that are deleterious to health and safety under the Foreign Exchange and Foreign Trade Act. A licence is not generally required in order to import equipment. Contractors may be subject to customs duties and VAT (consumption tax).

10.2 If so, what import duties are payable and are exceptions available?

Import duties may differ depending on product type, origin and other relevant conditions.

11 Force Majeure

11.1 Are force majeure exclusions available and enforceable?

Force majeure provisions are set out in many project agreements. Generally, exclusions based on such provisions are enforceable as long as they are clearly defined in such agreements. Normally, *force majeure* exclusions do not apply to payment obligations.

12 Corrupt Practices

12.1 Are there any rules prohibiting corrupt business practices and bribery (particularly any rules targeting the projects sector)? What are the applicable civil or criminal penalties?

Bribery is a criminal offence under the Criminal Code, with a penalty of imprisonment for up to three years or a fine of up to JPY 2.5 million. Conducting corrupt business practices with foreign government officials is a criminal offence under the anti-bribery provisions of the Unfair Competition Prevention Act, with a penalty of imprisonment for up to five years and/or a fine of up to JPY 5 million (for the offender) and fine up to JPY 300 million (for the corporate body).

13 Applicable Law

13.1 What law typically governs project agreements?

Project agreements are typically governed by the laws of Japan.

13.2 What law typically governs financing agreements?

Financing agreements are typically governed by the laws of Japan. However, securities documents may be legally required to be governed by the laws of the state in which the collateral is located.

13.3 What matters are typically governed by domestic law?

The parties may generally choose the governing law. However,

securities documents for collateral located in Japan are typically governed by the laws of Japan. In addition, enforcement, insolvency, consumer protection and employment matters will be subject to mandatory provisions of Japanese law.

14 Jurisdiction and Waiver of Immunity

14.1 Is a party's submission to a foreign jurisdiction and waiver of immunity legally binding and enforceable?

A waiver of sovereign immunity is legally valid and enforceable subject to the conditions in the Immunity Act. The Immunity Act is based on the United Nations Convention on Jurisdictional Immunities of States and Their Property (2004) and became effective from April 1, 2010.

15 International Arbitration

15.1 Are contractual provisions requiring submission of disputes to international arbitration and arbitral awards recognised by local courts?

Generally, yes. Japan is a signatory to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards.

15.2 Is your jurisdiction a contracting state to the New York Convention or other prominent dispute resolution conventions?

Yes, the Convention became effective from 1961 with a reservation of reciprocity. Japan is also a party to the Washington Convention on the Settlement of Investment Disputes Between States and Nationals of Other States (1965) (otherwise known as ICSID).

15.3 Are any types of disputes not arbitrable under local law?

Unless otherwise provided by law, civil and commercial disputes that may be resolved by settlement between the parties (excluding that of divorce or separation) are arbitrable (Art. 13.1 of the Arbitration Act). Examples of matters which are generally considered to not be "arbitrable" include: (i) the validity of intellectual property rights granted by the government; (ii) shareholders' actions seeking revocation of a resolution of the shareholders' meeting; (iii) administrative decisions of government agencies; and (iv) insolvency and civil enforcement procedural decisions.

15.4 Are any types of disputes subject to mandatory domestic arbitration proceedings?

No, they are not.

16 Change of Law / Political Risk

16.1 Has there been any call for political risk protections such as direct agreements with central government or political risk guarantees?

There has been no call for political risk guarantees. Lenders will typically require direct agreements with governmental authorities

if the project is a PPP or PFI project. Lenders usually seek criteria to approve the potential transferee of shares in the project company or concession right since a transfer thereof requires a consent of the relevant governmental authority under the PFI Act and its relevant regulations.

17 Tax

17.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Withholding of Japanese income tax is required on interest paid to foreign lenders at the rate of 20.42% (including special reconstruction income tax). This is subject to a double tax treaty between Japan and the country where the foreign lender resides, which in many cases will reduce withholding of such tax.

The proceeds of enforcing security may be subject to income tax if it is categorised as Japanese-sourced income.

17.2 What tax incentives or other incentives are provided preferentially to foreign investors or creditors? What taxes apply to foreign investments, loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

Various tax or other incentives are available to foreign investors to attract more foreign investment; however, such incentives are not intended specifically for project financing.

Registration tax is imposed on the registration of certain rights and securities. Rates vary depending on the type of rights and securities (e.g., 0.4% of the claim for mortgage). Stamp duty is imposed on the execution of certain documents. The amount of stamp duty for a loan agreement ranges from JPY 200 to JPY 600,000.

18 Other Matters

18.1 Are there any other material considerations which should be taken into account by either equity investors or lenders when participating in project financings in your jurisdiction?

Foreign investors should take into account currency exchange risk, since revenues generated by a project are generally paid in Japanese yen.

A wide variety of regulations will generally need to be considered for the development of a project. Generally, applicable permits and/or licences may differ depending on the site or facilities, and they are handled by the competent government and/or local government having regulatory oversight of the subject matter. Administrative officers sometimes have broad discretion on permits and/or licence application procedures, and this may result in a certain degree of unpredictability.

If lenders to a project are not banks, loans for project financings will generally be subject to the Money Lending Business Act, which requires registration with the authority and compliance with other obligations.

18.2 Are there any legal impositions to project companies issuing bonds or similar capital market instruments? Please briefly describe the local legal and regulatory requirements for the issuance of capital market instruments.

Project bonds are considered securities and are therefore subject to the Financial Instruments and Exchange Act. Offering securities to the public will require filing securities registration statements and following certain continuous disclosure obligations, unless exempt under certain exceptions.

19 Islamic Finance

19.1 Explain how *Istina'a*, *Ijarah*, *Wakala* and *Murabaha* instruments might be used in the structuring of an Islamic project financing in your jurisdiction.

To the extent of our knowledge, Islamic project finance has not been used in Japan. However, Japanese law has a similar legal framework corresponding to the Islamic finance concept. While compliance with *Shari'ah* is required to be reviewed separately, Japanese law would likely recognise: *Istina'a* as a procurement and construction agreement (*seizou itaku*); *Ijarah* as a lease agreement (*chintaishaku*); *Wakala* as an agency agreement (*dairi* or *toiya*); and *Murabaha* as a sales agreement with an instalment payment (*kappu hanbai*). Therefore, in a possible structure for a project financing, (i) an *Istina'a* arrangement may be used in order to provide funds

for the construction of the plant during the construction period, and (ii) an *Ijarah* arrangement may be used in such a manner that the financier leases the plant to a project company and receives the rent during the operation period. In addition, (iii) a *Wakala* arrangement may be used for syndication fund providers to provide funds to the project company through a financing special purpose vehicle. Also, (iv) *Murabaha* financing would in theory be permissible to make a working capital facility or equity bridge finance available to the project company. Note that in such cases, project participants may also be subject to their applicable regulatory restrictions (e.g., the Banking Act of Japan).

19.2 In what circumstances may *Shari'ah* law become the governing law of a contract or a dispute? Have there been any recent notable cases on jurisdictional issues, the applicability of *Shari'ah* or the conflict of *Shari'ah* and local law relevant to the finance sector?

We doubt that a Japanese court would recognise *Shari'ah* law as the governing law of a contract or dispute. No notable cases have been determined in this area.

19.3 Could the inclusion of an interest payment obligation in a loan agreement affect its validity and/or enforceability in your jurisdiction? If so, what steps could be taken to mitigate this risk?

In general, inclusion of an interest payment obligation does not affect the validity or enforceability of a loan agreement, although usury laws will apply.

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The Project Finance practice at Anderson Mōri & Tomotsune frequently advises all parties involved in projects, including sponsors, project companies, domestic and international commercial lenders, export credit agencies, suppliers, contractors and governments. We provide comprehensive and practical legal advice on the successful structuring and implementation of major infrastructure projects in all sectors, including electricity, oil and gas, transport, water and telecommunications. We are able to draw on our firm's expertise in complementary areas, such as Japanese corporate law and regulation, tax-effective structured financing and capital markets. In addition to our commitment throughout the entire duration of a project, we are able to exploit our international experience to recognise specific cultural, political or environmental issues, enabling the successful implementation of major cross-border and transnational projects.

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