PricewaterhouseCoopers (Australia)
Greater scrutiny of government sales under foreign investment regime

PricewaterhouseCoopers Legal AG Rechtsanwaltsgesellschaft (Germany)
ECJ Kornhaas decision: a turnaround on the freedom of establishment?

PwC Legal (Vietnam) Co., Ltd
New regulations on foreign loans

PwC International Business Reorganisations Network – Monthly Legal Update

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Contents

Welcome

Welcome to the fifth edition of the PwC International Business Reorganisations (**IBR**) Network Monthly Legal Update for 2016.

The PwC IBR Network provides legal services to assist multinational organisations with their cross-border reorganisations. We focus on post-deal integration, pre-transaction separation and carve outs, single entity projects, and legal entity rationalisation and simplification as well as general business and corporate and commercial structuring.

Each month our global legal network brings you insights and updates on key legal issues and developments relevant to multinational organisations.

We hope that you will find this publication helpful, and we look forward to hearing from you.

In this issue

In our May 2016 issue:

- PricewaterhouseCoopers (Australia) reports on recent amendments to Australia's foreign investment laws and their impact on government sales of certain infrastructure assets;
- PricewaterhouseCoopers Legal AG Rechtsanwaltsgesellschaft (Germany) discusses the effects of a recent decision by the European Court of Justice on the law surrounding freedom of establishment; and
- PwC Legal (Vietnam) Co., Ltd provides an update on new regulations by the State Bank of Vietnam governing foreign loans.

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PricewaterhouseCoopers (Australia) – Greater scrutiny of government sales under foreign investment regime

At a glance

The sale of certain infrastructure assets by Australian governments will no longer be excluded from the ambit of Australia's foreign investment law, following amendments which came into force on 31 March 2016.

The changes means that acquisitions of land on which public infrastructure is situated may now be scrutinised by the Treasurer, subject to the standard thresholds and exemptions in the law.

The changes will impact the process and timing of asset sales conducted by State, Territory and Local governments and will likely result in greater involvement by Commonwealth agencies in these processes.

The changes further underline the need for an early assessment of the application of Australia's foreign investment law when structuring transactions, particularly when participating in government asset sales, where such considerations were previously unnecessary.

In detail

Background

Australia has a long-standing policy of welcoming foreign investment, with an assessment being made by the Commonwealth as to the congruence of an investment proposal with Australia's national interest.

As we have previously written, there has been a significant change in the process of assessment of investment proposals over the last 18 months, with the Commonwealth seeking to enhance the integrity of the system in order to strengthen public support for Australia's foreign investment policy. These changes have culminated in a wholesale re-write of the *Foreign Acquisitions and Takeovers Act 1975* (Cth) (the **Act**) and the *Foreign Acquisitions and Takeovers Regulations 1975* (Cth) (the **Regulations**).

Previous position in relation to review of government asset sales

The sale of assets by State, Territory and Local governments to private investors has previously been exempt from scrutiny under the Act under regulation 31 of the Regulations. The exemption was limited in scope and did not extend to sales to foreign government investors, who remained subject to the provisions of the Act and the Regulations. The proposal by the 'Power NSW' consortium, which included Chinese state-owned utility State Grid, to acquire the NSW electricity transmission network in 2015 was an example. In that case the Treasurer had no objection to the proposal.

The scope and application of the exemption was brought into focus following the recent grant of a long-term lease of the Port of Darwin by the Northern Territory government to China's Landbridge Group in late 2015, which generated significant public comment.

New rules on critical infrastructure assets

The Treasurer announced on 18 March 2016 that the scope of the exemption for government asset sales would be narrowed, with the stated intention being to ensure that potential national security risks can be addressed in government sale processes.

The *Foreign Acquisitions and Takeovers Amendment (Government Infrastructure) Regulation 2016* (Cth) was promulgated on 24 March and amends regulation 31 of the Regulation to add a number of exclusions from the exemption in regulation 31(1), namely sales to private investors of land, or a company which holds an interest in land, on which there is:

a ‘public infrastructure’, except in relation to public roads;

b infrastructure for existing or proposed roads, existing or proposed railways, or existing or proposed inter-modal transfer facilities, within the National Land Transport Network, as defined in the *National Land Transport Act 2014* (Cth);

c infrastructure for existing or proposed roads, existing or proposed railways, or existing or proposed inter-modal transfer facilities, that are designated under a law of a State or Territory as either significant or controlled by the State or Territory;

d the infrastructure (or part of the infrastructure) of a telecommunications network; or

e a nuclear facility.

It is likely that many types of asset sale that may be contemplated by a State, Territory or Local government will fall into one of these categories; in this regard we note the breadth of the definition of ‘public infrastructure’ in regulation 5 of the Regulations which, in summary, means:

a airports;

b maritime ports;

c infrastructure for public transport (regardless of whether it is publicly owned); and

d electricity, water, gas or sewerage infrastructure.

Impact of changes

We expect that State, Territory and Local governments have, in the past, routinely consulted with relevant Commonwealth agencies in relation to proposed asset sales, although the changes to the Regulation will mean that the Treasurer will, in many cases, now be able to prevent a particular transaction from proceeding, if the Treasurer considers that it would be contrary to Australia’s national interest.

It is conceivable that the Treasurer’s assessment of Australia’s national interest in respect of a particular sale may diverge from that of a State, Territory or Local government, whose interests may be more focused on financial considerations.

In a practical sense, foreign investment screening will result in scrutiny of proposals by Commonwealth regulators (e.g. environmental) who would not previously have had an opportunity to consider the merits of a particular transaction. Applicants will need to consider likely regulatory concerns as part of the application process and prepare for the possible need to engage with regulators on these.

The additional scrutiny that will now be applied to government sale proposals will add a degree of complexity to transaction execution and could, in theory, reduce the possible universe of bidders. These issues are, of course, routinely faced in private sector sale processes and may well be manged by a combination of engagement between selling governments and the Commonwealth as part of the pre-sale preparation, as well as early and diligent preparation by bidders of screening applications under the Act which demonstrate, in a comprehensive way, the alignment with Australia’s national interest.

The takeaway

The narrowing of the exemption for government asset sales in regulation 31(2) of the Regulations will lead to a greater scrutiny of infrastructure asset sales by Australian governments. We expect that the Commonwealth has always had some involvement in asset disposals conducted by other governments, although the Treasurer now has a right of veto in many cases, which is an important shift.

It will be critical for Australian governments to engage with the Foreign Investment Review Board early when preparing for major sale processes and for bidders to factor in this additional review step when planning their proposals. Where an application for screening is required, it will be important that bidders provide a comprehensive submission as to the alignment of the proposal with Australia's national interest.

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PricewaterhouseCoopers Legal AG Rechtsanwaltsgesellschaft (Germany) – ECJ Kornhaas decision: a turnaround on the freedom of establishment?

At a glance

In a series of prior judgements, the European Court of Justice (**ECJ**) defined the scope of the freedom of establishment. With its recent decision in "**Kornhaas**", the ECJ has taken position on the limits of this freedom.

In this decision, the ECJ considered whether a provision in the German Limited Liability Companies Act (**GmbHG**) protecting creditors of an insolvent company falls within the scope of the freedom of establishment.

The Kornhaas decision clarifies the earlier decisions of the ECJ and creates rules on the freedom of establishment which can be summarised into two points: (1) provisions preventing companies from other member states from moving into a member state violate freedom of establishment; and (2) provisions regulating the business after the movement do not infringe the freedom of establishment.

In detail

Situation prior to Kornhaas

With its "Überseering" and "Inspire Art" judgments the ECJ clarified that companies duly incorporated in one member state could move their operations into another member state by relocating their seat or establishing a branch. National provisions preventing foreign (EU) companies from relocating their business operations into a member state violate the freedom of establishment under Art. 49 (and Art. 54) of the Treaty on the Functioning of the European Union (**TFEU**). Provisions that prevent domestic companies from moving out of a member state are however not in violation of Art. 49 TFEU.

This led to some discussion and quite some confusion as to which provisions were applicable to companies that had relocated their business operations into another member state. Any provision obliging a company to anything could be a deterrent for moving and thus infringe Art. 49 TFEU.

On company law the consensus was that the law of the country of incorporation continues to be applicable in the event business operations are relocated to another member state. This is different for insolvency law. According to Art. 3 and 4 of the European Insolvency Regulation (**EIR**) the applicable law under insolvency proceedings is the debtor's centre of main interests (**COMI**).

It follows that companies established and registered in one member state that moved business operations into another member state are subject to the company law of their state of incorporation and subject to insolvency law of the member state their operations were moved to.

ECJ rules on Kornhaas

In its judgement of 10 December 2015, C 594/14 the ECJ held the director of a private company limited by shares incorporated under UK law (the **Ltd.**), Ms. Kornhaas, to be liable under Section 64 GmbHG. The Ltd. had moved its administrative seat and thus its COMI to Germany.

Sec. 64 GmbHG states, among others, that the managing director of a German GmbH making payments after he/she should have filed for insolvency is personally liable for the repayment. Although this provision is formally part of German company law it could be argued that in substance it is either part of company law (creditor protection) or of insolvency law or of both.

Ms. Kornhaas had made payments after the financial situation of the Ltd. had deteriorated and insolvency proceedings should have been initiated in Germany. The liquidator of the Ltd. sued Ms. Kornhaas for repayment under Sec. 64 GmbHG. A German court submitted two inquiries to the ECJ for preliminary decision: (1) could Sec. 64 GmbHG be considered insolvency law and if so, (2) does its application in the case of Ms. Kornhaas violate the freedom of establishment?

The ECJ ruled that Sec. 64 GmbHG is, in substance, insolvency law, as it regulates the "conditions for the opening of [insolvency] proceedings", see Art. 4 subsec. 2 EIR. Sec. 64 GmbHG is applicable to all private limited companies in Germany (including those incorporated in other member states), regardless of the fact that it is a part of an act on company law.

On the violation of the freedom of movement the judgement reads:

"*[A] provision of national law [that] is applicable only after that company has been formed, in connection with its business, […] does not, therefore, affect freedom of establishment*" - lit. 28

In consequence, Ms. Kornhaas could be held liable under Sec. 64 GmbHG.

Impact of the decision

The immediate impact of the decision is that any provision relating to insolvency proceedings will have to be carefully evaluated, regardless of the act it is a part of in. If the provision is to be considered to be insolvency law in substance, it is applicable to all companies with a domestic COMI.

This has a considerable impact in member states with creditor protection rules traditionally located in company law or civil law, like Germany. For corporate advisors this should be taken into account, e.g. when giving advice to a director of a British Ltd. on the risks and obligations in connection with a potential move to Germany.

New rule for the freedom of establishment

There is a more fundamental fact to be derived from the reasoning of the ECJ. An unprecedented rule on how to assess whether a provision violates the freedom of establishment has been established.

The ECJ argues that its prior judgements "Überseering" and "Inspire Art" had a limited scope. Only provisions actually preventing a company from moving into another jurisdiction, e.g. requiring a certain capital structure, are in violation of Art. 49 TFEU. On the other hand provisions that regulate the day-to-day business of both domestic and foreign companies alike cannot infringe the freedom of establishment.

The restrictions this judgement puts on the freedom of establishment are a reflection of what the "Keck" decision has done for the free movement of goods (Art. 34 TFEU): After having expanded the range of the freedom to basically prohibit any national provision that regulates foreign goods, the ECJ had to step in to prevent the freedom from eroding all national provisions and protections. Through the "Keck"-decision the ECJ introduced rules to test a provision for compliance with the free movement of goods that are still in place today.

In light of the judgement in Kornhaas, the rule of thumb for testing a provision against the freedom of establishment can be reduced to:

Does a national provision restrict a company incorporated in another member state from moving into the member state or from establishing a branch?

If this question is answered in the negative, the provision does not have to be further tested against the freedom of establishment.

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PwC Legal (Vietnam) Co., Ltd – New regulations on foreign loans

At a glance

The regulations on when and how foreign loans need to be registered in Vietnam have been revised by the State Bank of Vietnam.

A new Circular 03/2016 /TT-NHNN on foreign loans came into effect on 15 April 2016. This is a positive development in that the new Circular 03 replaces multiple older circulars and therefore consolidates the regulations on this topic into one place.

This article looks at the notable changes under the new Circular 03, which primarily focus on SBV registration and notification requirements, processes for documentation filing and requirements surrounding bank accounts.

In detail

Circular 03/2016/TT-NHNN

The State Bank of Vietnam has issued Circular 03/2016 /TT-NHNN on foreign loans. The new Circular will take effect from 15 April, and replace Circulars 09/2004/TT-NHNN and 25/2014/TT-NHNN, thereby consolidating the regulations on this issue.

Summary of Notable Changes under Circular 03

1. Changes to SBV registration requirements when importing goods on deferred payment terms

Importing goods on deferred payment terms no longer requires registration with the SBV. However, the opening and use of bank accounts and remittances out of Vietnam for such arrangements must still comply with the requirements of Circular 03, and concerned enterprises must periodically report to the SBV.

2. Availability of electronic and hard copy filing facilities

Loan registrations and quarterly reports can now be filed in hard copy or electronically. They can be posted to or submitted directly at the SBV or registered online through the SBV's website www.sbv.gov.vn or www.qlnh-sbv.cic.org.vn.

3. Additional documentation required for medium and long term foreign loans

With respect to the registration dossier for medium and long term foreign loans, in addition to the documents previously required in Circular 25, Circular 03 requires a number of new documents. For example, borrowers of short-term loans the term of which is extended beyond 1 year must now additionally submit an explanatory report on the satisfaction of conditions on use of the initial loan (together with documentary evidence) and a repayment plan for the extended loan.

4. Bank account requirements

A borrower which is not a foreign direct investment enterprise must open a bank account for the purposes of the foreign loan. Circular 03 provides regulations on the opening and use of such bank account. For FDI enterprises, their direct investment capital bank accounts should be used for this purpose.

5. Re-registration and notification requirements

Circular 03 retains the regulations in Circular 25 whereby, if the schedule of loan disbursement, repayment or interest payment changes by less than 10 days from the schedule already registered with the SBV, the borrower must only notify its bank, and does not need to register the changes with the SBV. However, if the schedule changes by more than 10 days, then re-registration with the SBV is required.

Circular 03 also sets out a number instances where only a written notification (rather than a formal registration) with the SBV is required, if certain details of an already registered loan change. Instances where mere notification suffices include change of address of the borrower within the province/city where the borrower is headquartered, change of trade names, etc..

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