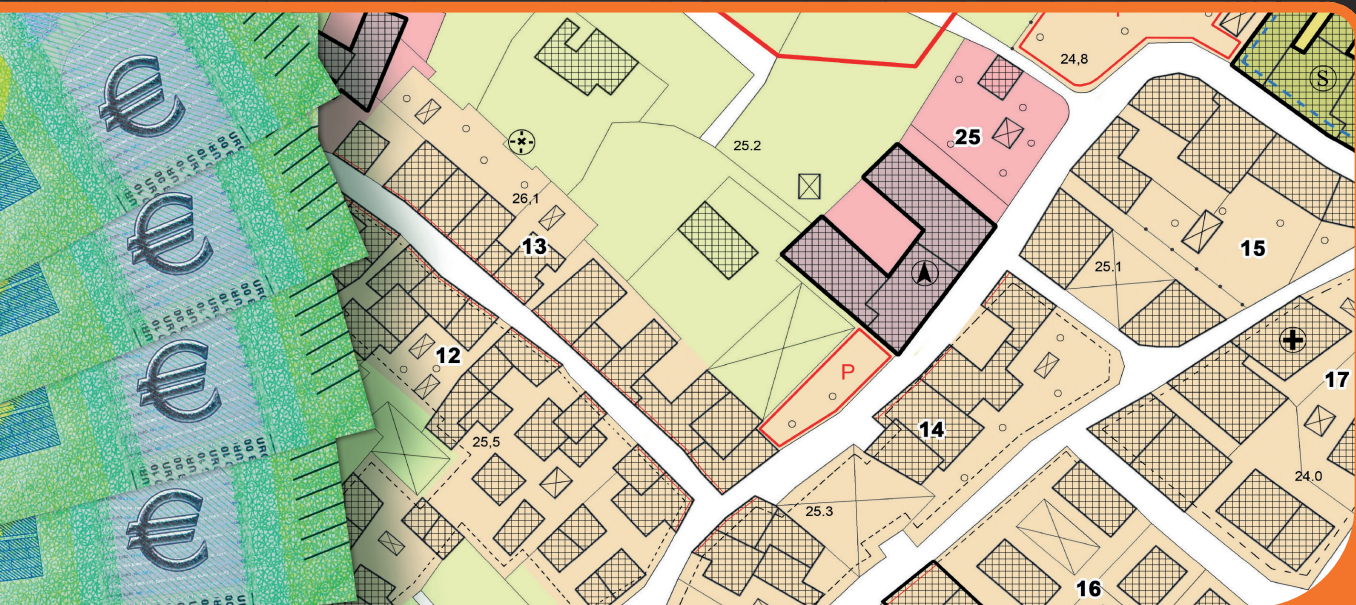


International Comparative Legal Guides



Practical cross-border insights into project finance

Project Finance 2022

11th Edition

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1 Overview

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

Following the nuclear power crisis caused by the Great East Japan Earthquake in 2011, the electricity industry has changed drastically. Renewable energy has drawn increasing attention as an alternative energy source. The Japanese government accelerated this trend by introducing the feed-in tariff in 2012. Although the focus is now shifting from photovoltaic to other power sources (such as onshore/offshore wind, geothermal and biomass), renewable energy projects remain one of the highlights of the Japanese project finance market. On the other hand, the suspension of operation of nuclear reactors has made the country more dependent on fossil fuels. However, the global trend of decarbonisation, in conjunction with the United Nations Sustainable Development Goals, has significantly discouraged the development of new thermal power plants. At the end of 2020, the Japanese government published the “Green Growth Strategies” and clarified its policy to increase renewable energy sources so that these constitute 50–60% of all electricity sources by 2050.

A substantial proportion of the existing Japanese social infrastructure was constructed during the 1960s and 1970s. To meet the need to restore or replace these facilities in the coming decades, the Japanese government is facilitating the use of public-private partnership (PPP) and private finance initiative (PFI) structures. We have seen quite a number of “concession” projects in various sectors, including: airports; toll roads; water services; facilities for the meetings, incentives, conferences and exhibitions (MICE) sector; and sports stadiums. Also, massive project financing is currently being arranged for a number of ongoing “integrated-resort” (casino) construction projects in Japan. This is another trend that market participants are focusing on.

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

In recent years, offshore wind projects have been gaining attention in Japan. Since the country is surrounded by water, it is considered to have huge potential for the development of offshore wind power projects in the midst of a growing need for decarbonisation and environmentally friendly sources of energy. In 2019, the Japanese government introduced new legislation to designate areas for the promotion of offshore wind projects and conduct public tendering to select operators for such designated areas. In early 2020, the first commercial offshore wind project in Japan, with a total capacity of approximately 140 MW and led

by Marubeni Corporation, reached financial close, with a total project cost of approximately JPY 100 billion. In the coming years, even bigger project financing is expected to be arranged for offshore wind projects in Japan. Recently, the Japanese government published its goal to develop offshore wind power plants with a production capacity of up to 30–45 GW by 2040.

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?

A “blanket lien” (i.e., a lien that gives a creditor the entitlement to take possession of any or all of the debtor’s property to cover a loan) is not available for bank loans in Japan. Therefore, it is necessary to individually attach security interests over each type of asset. Only with respect to movable assets and claims (e.g., trade receivables) is it legally possible to create security over current and future (after-acquired) assets that may change from time to time, to the extent that the scope of the security can be identified by location, type of asset, or underlying agreements.

A mortgage on a factory foundation (special statutory mortgage on facilities and land rights of plants) can be granted in favour of a bank. The reason for granting such a mortgage in project finance relates to the legal nature of some types of equipment. Specifically, it is unclear whether equipment directly and firmly attached to the land (e.g., mounting structure, fence, transmission line tower, and underground cable) are “fixtures”, which is real property, or “movables” under Japanese law. Thus, lenders are concerned about the risk that neither security on land rights nor security on movables covers such equipment. In contrast, it is clear that a mortgage over a factory foundation covers such equipment as long as the mortgage is registered.

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?

Among the forms of security available under Japanese law (i.e., mortgage, pledge and security assignment), a mortgage is typically used for real estate. A mortgage is perfected by registration at the legal affairs bureau with jurisdiction over the location of the property. The registration fee is 0.4% of the amount of the secured obligation. To reduce the upfront cost, some lenders permit the security provider to make a provisional registration only, on day one, which costs JPY 1,000 per property. Once the

mortgage is provisionally registered, the priority is reserved for the mortgage over subsequent competing parties, such as other mortgages. To upgrade from a provisional to a formal registration, documents (some of which must be provided by the security provider) must be submitted and registration fees (which are typically borne by the security provider or the borrower) must be paid.

Pledge and security assignment (also known as security by way of assignment or assignment for the purpose of security) can be used to constitute a security over movable properties. Subject properties can be individual properties or a pool of properties. The pool needs to be sufficiently identified by specifying the type of asset, location, and other necessary criteria. This method enables lenders to capture after-acquired movable properties as security.

To perfect a security assignment of movable property, actual or constructive delivery of the subject property (such as an occupant's manifestation of its intent to occupy the subject assets on behalf of the secured parties) is required. Alternatively, registration of the transfer will also perfect the security assignment. The registration fee is JPY 7,500 per filing, in addition to the professional fees of the judicial scrivener.

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?

Pledge and security assignment are the most typical forms of security for receivables. Future (after-acquired) receivables can be subject to a pledge or security assignment, provided that the target receivables are sufficiently identified.

Lenders can perfect the pledge or security assignment by giving notice to, or obtaining consent from, the obligor in written form with a notarised date certificate. Alternatively, registration of the pledge or transfer will also perfect the pledge or security assignment. In most cases, the registration fee is JPY 7,500 per filing, in addition to the professional fees of the judicial scrivener. The cost of a notarised date certificate is even lower.

Receivables cannot be collateralised without obtaining the obligor's consent if the underlying contract has a transfer restriction clause.

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

Yes, security over cash deposits is usually included in a typical security package for project finance in Japan. The borrower's receivables from the depository bank can be pledged for the benefit of the lenders in the same way as other types of receivables. Such pledge is perfected by the written consent of the depository bank with a notarised date certificate.

A legal opinion on the validity and perfection of security interests over ordinary (not fixed-term) bank deposits is usually limited or not given at all. This is because of an old court decision which denied the validity of such security interests, although today's leading law professors are unanimously supportive of its validity and most practitioners share this view.

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?

Pledge is the most typical form of security for shares. The method for perfection depends on the type of shares. Unless the

issuer is a listed company, the share pledge is normally perfected by the delivery of the share certificates representing the pledged shares. If share certificates are not issued pursuant to the articles of incorporation of the issuer, then the share pledge is perfected by recording the pledge in the shareholder ledger.

Lenders usually request that the issuer amend its articles of incorporation to remove any obstacles to the enforcement of the share pledge.

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)?

See questions 2.2 and 2.3 above.

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?

Normally, the filing, notification or registration requirements will not involve a significant amount of time or expense. That said, the registration under a factory foundation scheme tends to be more costly and time-consuming than other security schemes, which is one reason the factory foundation scheme is not used in relatively small projects.

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.?

Granting a security interest over some assets (e.g., receivables and contractual rights or status) may require consent from a third party, but regulatory or similar consents are not required with respect to major assets which are normally included in the security package for project finance in Japan.

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?

Traditionally, it has been a generally accepted principle in Japan that security must be held by the creditors to whom secured obligations are owed by an obligor. Therefore, each lender is named as a secured party in most syndicated loan transactions in Japan, which can be quite burdensome when there is a transfer of loans or a collective enforcement of security interests.

In 2007, the Trust Act of Japan was amended and the concept of a security trust was introduced, but as a matter of practice, security trusts have not been frequently used to date due to the number of drawbacks to overcome. One hurdle is a substantial increase in transaction costs, which results from fees payable to a trust bank or a trust company acting as the trustee of a security trust and also from additional mortgage registration fees required for perfection of mortgages held by a security trust.

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?

A conceivable alternative option is the use of a parallel-debt structure, where a security agent holds security to secure parallel debts owed to it by the borrower, rather than to secure each lender's corresponding loan disbursed to the borrower. Although the concept of parallel debt is fairly novel to the Japanese legal community, it should theoretically be feasible to create a parallel-debt structure under Japanese law.

One potential drawback to the parallel-debt structure may be the need to carefully examine the credit risk of the security agent, which could materialise if a creditor of the security agent were to attempt to seize and collect all or part of the parallel debt, or where an insolvency trustee might seek to collect parallel debt in connection with a security agent's insolvency proceedings. That said, the use of a parallel-debt structure has been gradually expanding and it might possibly be established as a common option for collective security arrangements in the near future.

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 Japan, insolvency proceedings are complex and under the control of the court and a court-appointed administrator/supervisor. In a nutshell, the lender may not exercise its security rights freely if there are insolvency proceedings against the borrower/obligor. Therefore, in order to prevent the project company from being subject to insolvency proceedings, the lender usually requires major related parties (including: the project company; the equity holder of the project company; the engineering, procurement and construction (EPC) contractor; and the operation and maintenance (O&M) contractor) not to:

- (i) file any petition for the commencement of any insolvency proceedings with respect to the project company; or
- (ii) terminate major project agreements without the prior consent of the lender.

Thus, it is important to ensure that the step-in rights of a bank can be exercised before the commencement of any formal insolvency proceedings.

Step-in rights are commonly set out in a direct agreement with a material party to the project. Where step-in rights are given to a lender, the lender is allowed to remedy a default under a project document on behalf of the project company, and project parties cannot terminate the project documents while the step-in rights are being exercised.

It is common to set up an arrangement as part of a security package whereby a lender is given an option (*yoyaku kanketsuken*) to acquire, or cause a designated party to acquire, the contractual position of the project company. This option usually becomes exercisable upon the occurrence of certain credit or default events, before the commencement of the insolvency proceedings.

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

Regarding the enforcement of share pledges, foreign lenders are not allowed to acquire pledged shares over companies that conduct certain categories of business related to national security. Such categories include telecommunications, broadcasting, and aviation.

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 major statutory insolvency proceedings; namely, bankruptcy (*hasan*), civil rehabilitation (*minji saisei*), and corporate reorganisation (*kaisha kousei*). Bankruptcy results in the liquidation of the borrower's business, while the other two proceedings allow the debtor's business to continue once substantial changes have been made to its assets, liabilities and equity pursuant to a rehabilitation or reorganisation plan.

Generally, in the course of bankruptcy proceedings (*hasan*) and civil rehabilitation proceedings (*minji saisei*), security interests are outside the scope of the control or supervision of the court-appointed administrator/supervisor. The commencement of such proceedings does not affect any security interest in place over the debtor's property. Therefore, such security interests could be enforced even during the bankruptcy proceedings and civil rehabilitation proceedings.

On the other hand, if corporate reorganisation proceedings (*kaisha kousei*) are commenced, secured creditors will be required to suspend security enforcement (an automatic stay) and their claims may be subject to reduction in accordance with the reorganisation plan. In other words, the court-appointed administrator may reduce the amount covered by a certain security interest, if it approves such reduction. Therefore, under corporate reorganisation proceedings, security interests might not be enforced pursuant to the original terms and conditions thereof.

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?

In terms of priority among secured creditors, Japanese law allows transaction parties to create and perfect most types of security interests in different priorities for the benefit of multiple creditors pursuant to certain procedures provided in the Civil Code and other relevant regulations. In addition, the second-ranking secured creditors will typically be requested by the senior lenders to enter into an intercreditor agreement in which they covenant not to enforce their security interests without the approval of the first-ranking secured creditors.

On the other hand, unsecured loans are usually treated as general claims in Japanese insolvency proceedings, and are subordinated by law to the following two senior claims: common benefit claims (such as costs and expenses arising from insolvency proceedings and certain other types of claims having common benefit for creditors overall); and preferred general claims (such as wages for employees and certain tax claims). Also, general claims are satisfied in priority to certain subordinated derivative or incidental claims (such as accrued interest,

damages or penalties for contractual breach, and delinquent taxes arising after the commencement of insolvency proceedings) pursuant to the relevant insolvency laws.

One of the notable risk areas for lenders in statutory insolvency proceedings is the risk of avoidance. Where a security interest is created or perfected by an already insolvent debtor or a debtor who suspends payment of debts that are due and payable, the related security interest or perfection may be avoided if bankruptcy proceedings (*hasan*), civil rehabilitation proceedings (*minji saisei*) or corporate reorganisation proceedings (*kaisha kousei*) have commenced thereafter.

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

In the context of project finance, it should be noted that Japanese limited liability companies (*godo kaisha*, GK) cannot be the subject of corporate reorganisation proceedings (*kaisha kousei*), unlike ordinary stock companies (*kabushiki kaisha*, KK), which means that the lender to a GK can enforce its security interests outside of the insolvency proceedings commenced with respect to a GK. In practice, a GK is often used as a project company, especially in solar power projects in Japan.

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?

Under standard security documentation, a lender may choose to enforce a security interest created by a judicial (in-court) procedure or private (out-of-court) process. One of the problems with judicial enforcement is that the sale proceeds are likely to be substantially lower than would be realised through a private auction.

However, in case of project finance, a lender is more keen on being able to replace the project sponsor by enforcing the security over all the assets held by the project company or the pledge over the shares of the project company, rather than to sell the individual collateral assets at higher prices.

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?

Generally, private restructuring processes are initiated by the borrower's lawyer and sometimes involve a third-party organisation specialising in private turnaround situations.

This type of process is chosen by a financially distressed debtor who would like to avoid the damage that would be caused by the public announcement of a commencement of statutory insolvency proceedings. Given the private nature of this process, the creditor's rights are not involuntarily impaired, and unanimous agreement among major creditors is required for the debtor to implement its restructuring plan.

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.

Generally, directors are liable to the company only when his or her action exceeds reasonable discretion for business judgment.

Also, directors are liable to third parties only when such third parties suffer any damage or loss arising from the wilful misconduct or gross negligence of the director.

6 Foreign Investment and Ownership Restrictions

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

Essentially, only *post facto* reporting is required under the Foreign Exchange and Foreign Trade Act (FEFTA) when a foreign investor acquires shares in a project company in Japan. However, when the project company is engaged in certain types of business, including electricity, gas, oil, telecommunications, water supply and transportation, the foreign investor who intends to acquire shares in such company is required to make a filing 30 days prior to the investment. When the filing is made, the government can order suspension of or change to the investment if it is perceived as a threat to national security. Also, there are some laws which provide an upper limit to the foreign ownership ratio in specific industries such as aviation and telecommunications.

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

There are no bilateral or international investment treaties that provide protection from such basic restrictions mentioned above.

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

The Expropriation of Land Act allows expropriation of land for public interest reasons, including roads, dams and railways. The landowner will be compensated for loss due to the expropriation. This Act applies to any land and there is no exceptional type of investment which 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 primary relevant governmental bodies are as follows:

- Energy projects: the Ministry of Economy, Trade and Industry (METI), especially the Agency for Natural Resources and Energy in METI.
- Concession projects for airports, toll roads and sewage: the Ministry of Land, Infrastructure, Transport and Tourism (MLIT).
- Concession projects for water: the Ministry of Health, Labour and Welfare (MHLW).

There are various other relevant authorities, including local governments, as well as different ministries of the central government depending on each project.

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?

Generally, there is no need to register or file financing or project documents with any governmental authority or comply with legal formalities in order for such documents to be valid and enforceable, except for certain types of long-term land lease agreements which need to be executed in the form of a notarised deed (*kosei shousho*).

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)?

A licence is not required in order to own land or pipelines, although various laws and regulations may be applicable to their acquisition and development, depending on the type of activity. For example, an oil pipeline business requires permission from METI and MLIT under the Oil Pipeline Business Act, which can be obtained by a foreign entity.

On the other hand, ownership of natural resources generally requires permission as follows:

- (i) To use river water, permission must be obtained from the central or local government under the River Act. Permission can be obtained by a foreign entity.
- (ii) Mining certain minerals requires a mining right under the Mining Act. Mining rights can only be acquired by Japanese nationals or Japanese corporations; however, foreign ownership of mining rights through a Japanese corporation is allowed under the Mining Act.

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

The major taxes and fees specifically applicable to the mining business are as follows (prospecting rights are the rights for exploratory digging, and digging rights are for commercial digging):

Tax/Fee	Item	Rate/Amount (JPY)
Mining Area Tax	Prospecting rights	200 (per 100 ares* <i>per annum</i>) *1 are = 100 sqm
	Digging rights	400 (per 100 ares <i>per annum</i>)
	Oil or combustible natural gas	2/3 of above
Mining Tax	—	1% of the price of mined minerals
Application Fee	Prospecting rights	71,800 (68,200 via online)
	Digging rights	112,600 (109,800 via online)
Registration Fee	Prospecting rights	90,000 (per mining area)
	Digging rights	180,000 (per mining area)

The export of natural resources is not subject to special restriction under the FEFTA.

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

Know Your Customer (KYC) procedures, which are conducted by financial institutions, are required for foreign currency exchange under the FEFTA. Also, there may be *post facto* filing requirements under the FEFTA.

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?

Post facto filing under the FEFTA is required for overseas remittance exceeding JPY 30 million. Also, a withholding tax of 20.42% is basically imposed on dividends and interest paid to foreign investors or lenders, but tax treaties may reduce or exempt foreign investors or lenders from such withholding tax.

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

Yes. A company may establish and maintain onshore foreign currency accounts, and/or offshore accounts, but *post facto* filing with the tax office is required for offshore assets held by a tax resident exceeding 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?

The amount of the dividend may not exceed the “distributable amount” under the Companies Act, which is calculated based on the amount of surplus earnings. In addition, a loan agreement for project financing typically contains cash waterfall provisions with conditions and restrictions on distribution of dividends. Other than those, generally, there is no specific restriction on payment of dividends from a project company to its parent company, regardless of the place of incorporation of the parent company.

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?

The basic environmental policy of Japan is set out in the Basic Environment Act. In addition, various laws and local regulations may be applicable in respect of environmental, health and safety issues; in particular, whether an environmental impact assessment is required by law or local regulation would have a significant impact on the costs and schedule of the project. The primary relevant authorities in the central government are the Ministry of the Environment (MOE) for environmental issues and MHLW for health and safety issues, but the applicable laws and regulations may vary depending on location, and therefore it would be helpful to consult with the local government to identify applicable laws and regulations.

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

No. There is no specific legal restriction on procurement by a project company, to the extent that the company is privately owned.

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?

Foreign insurance companies are required to obtain an insurance business licence under the Insurance Business Act to provide insurance policies over project assets in Japan.

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

There is no specific restriction on the payment of insurance proceeds 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?

As long as the foreign person has the appropriate visa status under the Immigration Control and Refugee Recognition Act, he or she may be employed by a project company as a worker, technician, engineer or executive. The project company employing any foreign person is required to report such employment to the Public Employment Security Office.

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?

There are minimal restrictions on importing equipment, such as the prohibition on importing drugs, guns and explosives designated by the Customs Act or FEFTA. Import duties may be imposed depending on the type of goods.

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

Import duties vary depending on the type of assets, exporting country, and other circumstances. The relevant information is disclosed on the website of Japan Customs under the Ministry of Finance.

11 Force Majeure

11.1 Are *force majeure* exclusions available and enforceable?

Typical project agreements contain *force majeure* exclusions, which are generally enforceable under Japanese law.

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?

In Japan, domestic and cross-border bribery is prohibited. The Penal Code prohibits bribery of Japanese government officials, while the Unfair Competition Prevention Act prohibits bribery of foreign public officials.

On the other hand, private commercial bribery is not generally regulated other than by specific laws that regulate private commercial bribery under specific circumstances. For example, under Article 967 of the Companies Act, giving, offering or promising bribes to a director of the board or similar officer of a stock corporation in response to “unlawful solicitation” in connection with their duties is prohibited.

13 Applicable Law

13.1 What law typically governs project agreements?

For projects and assets located in Japan, project agreements are typically governed by Japanese law. However, it is generally possible for transaction parties to choose another governing law.

13.2 What law typically governs financing agreements?

For projects and assets located in Japan, financing agreements are typically governed by Japanese law. However, except for security agreements where the collateral is assets located in Japan or shares/equity interests of an entity incorporated under Japanese law, it is generally possible for transaction parties to choose another governing law.

13.3 What matters are typically governed by domestic law?

Please see questions 13.1 and 13.2 above.

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?

An agreement to submit to a foreign jurisdiction is generally valid and binding as long as such agreement is executed in writing. Also, a waiver of sovereign immunity is valid and binding subject to the conditions under the Immunity Act, which is based on the United Nations Convention on Jurisdictional Immunities of States and Their Property.

15 International Arbitration

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

Yes. Generally, the Arbitration Act provides that the following are required for an arbitration agreement to be valid and enforceable: (i) an arbitration agreement is about a civil dispute

(excluding disputes of divorce or dissolution of adoptive relation) which can be settled between the parties; (ii) an arbitration agreement is in writing; and (iii) it is possible to carry out arbitration proceedings under an arbitration agreement. In addition to the abovementioned requirements, the following items are considered to be required for an arbitration agreement to be valid and enforceable: (a) the parties have the power and authority to execute an arbitration agreement; and (b) there is a meeting of the minds with respect to the arbitration agreement, which must be valid and not invalidated (existence of an agreement).

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

Yes, Japan is a signatory to the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York Convention) and reserves the principle of reciprocity.

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

The Arbitration Act provides that the arbitration agreement should: (i) be about civil disputes (excluding disputes of divorce or dissolution of adoptive relation); (ii) involve private law matters that can be settled between the parties (excluding, e.g., criminal and administrative law matters and the validity of a registered patent); and (iii) not be about an individual labour dispute. Separate from the above, it is worth noting that the by-law of the Arbitration Act stipulates special rules regarding an arbitration agreement between a consumer and a business operator, which can be cancelled by the consumer.

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

No, disputes are not subject to such proceedings as a matter of mandatory rules.

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?

Generally, there is no call for political risk guarantees or insurance in Japan.

In PFI/PPP projects, it is common for a lender to enter into a direct agreement with the central or local government, where the lender is afforded an opportunity to be notified by, and discuss the project restructuring with, the government prior to the termination of the project agreement by the government.

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?

Dividends and interest paid to foreign entities by a Japanese entity are subject to withholding income tax at the rate of

20.42% (this may be reduced or exempted by treaty). Also, if the proceeds of a claim under a guarantee or security enforcement are treated as income from a domestic source, they will be subject to withholding income tax.

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?

Some tax treaties reduce or exempt certain persons from withholding tax, but there are no special incentives provided for project finance. Stamp duties will be imposed on certain types of agreements such as EPC contracts, land lease agreements, service agreements and loan agreements. For instance, in the case of loan agreements, the amount of stamp duty may vary depending on the principal amount of the loan (the maximum amount of stamp duty is 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?

Aside from the issues covered in the other questions and answers, one additional material consideration for equity investors would be the restriction on transfer of equity interests in a project company, which is typical under finance documents. Such transfer would require the prior consent of the lender, without much flexibility, even after construction is completed.

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, either in the form of corporate bonds or trust beneficial interests, are not common in the Japanese market to date. Project bonds are securities and subject to securities regulation under the Financial Instruments and Exchange Act of Japan. Public offering of securities is subject to a suite of filing and registration requirements.

Public offering of securities is not normally used for project financing except for certain listed infrastructure funds investing in a portfolio of renewable (especially, solar) projects.

Project bonds are usually issued through private placement for a limited number of institutional investors, such as insurance companies and pension funds.

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.

Islamic financing or *Shari'ah* law is not used for project finance in Japan and, therefore, there have not been many previous legal studies on the structuring of Islamic project financing in this jurisdiction. Under Islamic law principles, *Istina'a* may be used to provide funds for construction projects, but the agreement

between the financier and the project company under an *Istina'a* arrangement might be prohibited, since the Banking Act imposes strict restrictions on the scope of business of banks.

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?

There are no notable cases where *Shari'ah* law has been applied in Japan. The prevailing view under Japanese conflict-of-law rules is that the parties may select a certain law as the governing law

only if it is a law of a specific state – the parties may not select a non-state law as a governing law (e.g., *lex mercatoria*). Therefore, it is arguable that the parties may select *Shari'ah* as a governing law.

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?

No. An interest payment obligation in a loan agreement is valid and enforceable as long as the interest rate does not exceed the cap (15% to 20% *per annum*) under the Interest Rate Restriction Act.



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