ABA Section of International Law
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International M&A and Joint Ventures Committee Newsletter

March 2010

Spring Meeting
If you have not done so already, it is now time to register for the 2010 Spring Meeting that will be held April 13 -17 at the Grand Hyatt in New York City.

The Committee is sponsoring a number of programs at this upcoming Section Meeting. For the full program please see the Spring Meeting website: http://www.abanet.org/intlaw/spring2010/

Committee dinners will be held Wednesday evening at the Yale Club. We hope to see you all there.

Get Involved with your Committee!
The Committee leadership values and encourages your participation in activities of the Committee**.**

Newsletter Contributions
If you would like to contribute a Country Update for the next newsletter, please contact Kees Koetsier (kees.koetsier@nautadutilh.com). The next issue of the newsletter is planned for June 2010. The deadline for submissions is June 1, 2010.

Foreword

Dear Committee Members,

This is the first issue of our committee's newsletter for 2010, with Country Updates on Belgium, Brazil, Canada, China, India, New Zealand, South Korea and the UK.

Many thanks to all committee members that contributed to this newsletter. Hope to see you all in New York in April.

Kind regards,
Kees Koetsier

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Country update on Belgium

By Nicole van Ranst and Nicolas Claerhout, Marx van Ranst, Vermeersch & Partners, Brussels

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Obligation to disclose major shareholding within unlisted companies

In our contribution to ABA SIL's M&A and Joint Venture "Year in Review 2008" (Summer 2009), we already informed you about the first step in the abolition process of bearer securities. Until recently, Belgium was one of the very few countries that still allowed the issuance of bearer securities.

On 18 January 2010, with the same aim to prevent money laundering and financing of terrorism, the Belgian Chamber of Representative adopted a new act to amend the Belgian Corporate Code (Corp. Code)[1]. The new article 515bis Corp. Code requires any legal person or individual who, following the acquisition of voting securities, whether or not these securities represent a capital contribution, would be in the possession of such securities that represent 25% or more of the total voting rights in an unlisted limited liability company that issued bearer securities or dematerialized securities, to notify the issuing company thereof within 5 days after the acquisition. The same notification needs to occur within the same period when a subsequent sale of the concerned securities would entail that the shareholder's voting rights attached to such securities would drop again below 25% of the total voting rights.

The consequence of the mandatory disclosure is that no one can take part in the voting process at the general meeting with a number of votes superior to the number declared to be in their possession at least 20 days before the general meeting is due to take place (amended art. 545 Corp. Code). Furthermore, if the Board is aware that no disclosure has been made when it should have been done, it can delay the general meeting up to three weeks (amended art. 534 Corp. Code). The penalties for failure to disclose the shareholding can be set by the Commercial court, and might be (i) the suspension of all or part of the rights embedded in the shares for a maximum term of 1 year, (ii) the temporary suspension of the general meeting that has been convened, and even (iii) the forced sale of the concerned shares to a third party, not affiliated to the current shareholder.

New company form in Belgium

As one of the very last European countries, Belgium has introduced a new company form, a BVBA "light". On 12 January 2010, an act to amend the Belgian Corporate Code and to set the modalities of the 'Starter' Closed Limited Liability Company was approved by the Belgian Chamber of Representatives[2].

This type of company aims to (i) lower the burden for entrepreneurs forming start-ups whilst still providing them the benefit of limited liability, and (ii) compete with similar legal forms in other jurisdictions. The main features of the act are as follows: (i) the minimum share capital of the start-up limited liability company will amount to EUR 1; (ii) a business plan should be prepared and audited with a view to avoiding premature bankruptcy due to a lack of experience; and (iii) it is mandatory to increase the share capital within five years to bring it up to at least EUR 18,550 (i.e, the minimum share capital required for closed limited liability companies).

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[1] Act of 18 January 2010 to amend the Act of 11 January 1993 to prevent the use of the financial system for money laundering and financing of terrorism, and the Corporate Code (published in the *Official Belgian Gazette,* dated 26 January 2010).

[2] Act of 12 January 2010 to amend the Corporate Code and to set the modalities of the closed limited liability company 'Starter' (published in the *Official Belgian Gazette,* dated 26 January 2010)

New law on judicial administratorship (“gerechtelijk akkoord” / “concordat judiciaire”)
On 31 January 2009, a new Act on the Continuity of Enterprises has been approved by the Chamber of Representatives[3]. Under the former legislation, companies, creditors, financial institutions … approached the judicial administratorship as a kind of waiting phase for the bankruptcy of the company. By applying for a judicial administratorship, companies acknowledged openly to suffer from all sorts of problems, which had an negative impact of their image, hence on the manner in which they were regarded by suppliers and customers. Therefore, as the title of the new act already indicates, it is the legislator’s clear intention to offer a set of efficient tools to companies to address and recover from any issues they might have.

The options provided under the new law can be applied without or with supervision of the courts. In the latter event, a company can ask for a period of judicial protection against its creditors to enable her either (i) to find an amicable agreement with a limited number of creditors, or (ii) to find an recovery plan with all creditors, or (iii) to transfer the company or its activities, either partially or either wholly, to third parties under supervision of the court.

The conditions to obtain a judicial protection are relatively simple, as one must proof that (a) the company’s continuity is threatened, and (b) the company has at least prospects that the company’s activities can be safeguarded in part of in whole.

As the act went very rapidly through the legislative process given the economical climate, already quite some case law and legal texts has been produced on the topic. Hence, future legislative action to amend and perfect the act might be expected.

Less formalities on reporting and documentation in the case of future mergers and divisions
On 16 September 2009, the European Parliament and the Council approved Directive 2009/109/EC[4]. The European legislator attempts to reduce the administrative burdens weighing on companies within the Community to the minimum needed in order to protect the interest of other stakeholders, as it is aware of the facts that company law imposes on companies numerous information obligations, some of which seemed outdated or excessive.

The Directive opens the opportunity for companies to use their websites in the framework of their duty of information, as they offer in certain cases, a worthy alternative to publication via the companies registers. Member states should also be able to designate those other websites which companies may use free of charge for such publication, such as the website of business associations or chambers of commerce. Member States should also be entitled to provide that the extensive reporting or information requirements relating to the merger or division of companies need not be complied with if all the shareholders of the companies involved in the merger or division agree that such compliance may be dispensed with. Such agreement by the shareholders should of course be without prejudice to the systems of protection of the interests of creditors of the companies involved and to rules aimed at ensuring the provision of necessary information to the employees of those companies and to public authorities, such as tax authorities. The obligation to draw up accounting statements will also be abolished where an issuer whose securities are admitted to trading on a regulated market published half-yearly financial reports. Furthermore, reporting requirement will be reduced for mergers between parent companies and their subsidiaries which have a reduced economic impact on shareholders and creditors (given the parent company’s holding in the

[3] Act of 31 January 2009 on the continuity of enterprises (published in the Official Belgian Gazette of 2 February 2009).
[4] Directive 2009/109/EC of the European Parliament and of the Council of 16 September 2009 amending Council Directives 77/91/EEC, 78/855/EEC and 82/891/EEC, and Directive 2005/56/EC as regards reporting and documentation requirements in the case of mergers and divisions (L. 259/14, *Official Journal of the European Union* dated 2 October 2009).

subsidiary amounts to 90% or more of the shares and other securities conferring the right to vote). The same will apply to certain divisions, in particular when companies are split into new companies that are owned by the shareholder in the proportion to their rights in the company being divided.

It follows from the Directive that member states have time to comply with this Directive and to bring into force the laws, regulation and administrative provisions to that effect by 30 June 2011.

Country update on Brazil

Country update on Brazil

By Alexandre L. Ribeiro do Valle and Carolina Pett G. Gonçalves, V,M&L sociedade de advogados, Sao Paulo, Brazil

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Besides the international financial crisis, Brazilian market has registered a considerable number of M&A transactions during 2009 and as the beginning of 2010 indicates will register a higher number this year with the consolidation of some administrative and judicial decisions relating to M&A transactions and also with several changes in the related legislation. In addition, the world cup and Olympic games are already in evidence and pushing investors to carefully look at the Brazilian Market.

Apart from the recently changes in the accounting system, introduced by law number 11638 that came into force last year, the main points that should be emphasized as recent changes into the Brazilian legal system are the following:

In force since 2005, law number 11.101 has completely amended the procedures for bankruptcy in Brazil, enabling companies with punctual financial difficulties to restructure its debts by negotiating different conditions with creditors or selling part of its assets. A recent decision from the Supreme Court issued in November 2009 puts an end to the discussion whether the buyer of such assets would be considered as tax and labor substitutes of said companies, by considering that in such circumstances the buyer shall not respond for the sellers' obligations. Such decision will certainly open more space for acquisition strategies.

There is also a current expectation that a new antitrust law will be enacted during 2010. The bill of law 3.937/04 has being approved by the house of representatives and sent to the Senate for discussions and deliberation. Apart from the complete reorganization of the internal structure of the Antitrust Agency (CADE), the main changes to be introduced by the law rests on the requirement of prior approval of acts that could be considered prejudicial to competition. Actually, Brazil adopts an after submission system. If the bill is approved, the number of transactions submitted to approval is expected to decrease, since there will be a second trigger for the submission. With the prevailing laws, if any of the parties involved in the transactions has registered, in Brazil, an annual revenue greater than R$ 400,000,000.00 the transaction shall be submitted. With the proposed changes, in addition to such requirement, the transaction will only be submitted if the other party has registered an annual revenue greater than R$ 30,000,000.00.

Corporate governance issues are also on the highlights, and poison pills were on the top of the discussions in the last few months. Many companies have adopted regulations stating that shareholders voting for the exclusion or amendment of clauses relating to poison pills should be obliged to make public offers to the other shareholders, with the argument that Initial Public Offers in Brazil would not be possible if the former controller is not keep saved in the control of the company even after going public. After several discussions, Brazilian Stock Exchange Commission recently issued an instruction in the sense that there should be no penalties for shareholders voting for the change or exclusion of poison pills.

Country update on Canada

Joint Ventures and the *Competition Act's* New Conspiracy Offence

By Mark Katz & Jim Dinning, Davies Ward Phillips & Vineberg LLP, Toronto, Canada

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In March 2009, the Canadian Parliament passed legislation incorporating significant amendments to the *Competition Act* (the "Act"), including important changes to the Act's conspiracy offence.[5] The wording of the new conspiracy offence, which came into force on March 12, 2010, has raised questions about its potentially broad application, especially in relation to joint ventures and other legitimate collaborations between competitors.[6]

The new conspiracy offence establishes a *per se* criminal prohibition against agreements between competitors to fix prices, affect production or supply levels of a product, or allocate sales, customers or territories.[7] Maximum penalties under the new offence are 14 years imprisonment and a CDN$25 million fine per count, up from the previous maximums of five years and CDN$10 million per count. The new offence also contains several defences and exemptions. Most notably, it is not an offence if the impugned agreement is (i) "ancillary to" a broader or separate agreement that does not itself contravene the conspiracy provision, and (ii) is "directly related to and reasonably necessary for" giving effect to that broader or separate agreement.

Also as of March 12, 2010, all other agreements between competitors that have the effect of lessening or preventing competition substantially will now be dealt with under a new civil provision. The Competition Bureau ("Bureau") will be able to apply to the Competition Tribunal under this new provision for an order to remedy the effects of such agreements.

Various concerns have been raised about the new *per se* conspiracy offence, foremost among them that the offence may inadvertently criminalize joint ventures between competitors that involve coordination on pricing or other prohibited matters but that are entirely legitimate and even pro-competitive. Although one might presume that joint ventures of this kind should be protected under the ancillary restraints defence, the statute does not define the meaning of key concepts such as "ancillary to", "directly related to" and "reasonably necessary for". Accordingly, the scope of the defence will remain undefined until the courts are given the opportunity to consider and interpret it.

The Bureau has attempted to fill this void with the issuance of its *Competitor Collaboration Guidelines* (the "Guidelines"), which set out the Bureau's enforcement approach to the new criminal offence, including the ancillary restraints defence.[8] On the positive side, the Guidelines emphasize the Bureau's view that the new conspiracy offence is not intended to capture pro-competitive joint ventures and other legitimate collaborations between competitors. At the same time, it must be recognized that the Guidelines are not a binding statement of the law. Indeed, there have been several instances in which the Bureau departed from its enforcement guidelines in other areas when this suited its purposes. It also must be kept in mind that section 36 of the Act allows private parties to bring civil suits to recover for damages suffered as a result of conduct contrary to the Act's criminal provisions, including the conspiracy offence. Thus,

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[5] Bill C-10, Budget Implementation Act, 2009, 2d Sess. 40th Parl., 2009, *available at* http://www2.parl.gc.ca/content/hoc/Bills/402/Government/C-10/C-10_4/C-10_4.PDF.
[6] See, *e.g.*, Canadian Bar Association National Competition Law Section, Submissions on Draft Enforcement Guidelines on Competitor Collaboration (August 2009), *available at*: http://www.cba.org/CBA/submissions/pdf/09-47-eng.pdf.
[7] *Competition Act*, R.S.C. 1985, c. c-34, s. 45.
[8] Competition Bureau, Competitor Collaboration Guidelines (December 23, 2009), *available at*: http://competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/03177.html.

even if the Bureau is prepared to abide by its assurances in the Guidelines that joint ventures ought not be subject to criminal prosecution in Canada, it is entirely possible that civil plaintiffs (and the courts) will take a different view when it comes to damage claims or efforts to void agreements for illegality.

There are also difficulties with the Guidelines themselves. For example, the Guidelines state that a restraint is "ancillary" when it is functionally incidental or subordinate to the objective of some broader agreement.[9] This may be taking too narrow a view. While coordination on pricing or other matters may not always be the sole purpose of a joint venture, there may be examples of legitimate forms of collaboration where such forms of coordination are at the heart of the venture and not simply incidental or subordinate to the main purpose of the agreement.

Similarly, the Guidelines state that a restraint will not be considered "directly related to, and reasonably necessary for giving effect to" the objective of a joint venture agreement if the parties "could have achieved an equivalent or comparable arrangement through practical, significantly less restrictive means that were reasonably available to the parties at the time when the agreement was entered into". This means that the Bureau (and ultimately the courts) will be asked to second guess the joint venture parties and make judgments about the relative merits of various business strategies. This is not a simple task at the best of times, and may be made even more difficult by the fact that joint ventures often involve coordination at many levels, from research and development, through production to distribution, marketing and sales.

In short, the changes to Canada's conspiracy offence have opened up new uncertainties for joint ventures between competitors in Canada. Moreover, even if a joint venture is able to avoid both scrutiny and liability under the new criminal offence, it will still remain potentially subject to proceedings and remedies under the new civil provision governing anticompetitive agreements.

Country update op China

Foreign-invested Partnership – A New Structure of Joint Venture in China

By Hazel Ranran Yin (Visiting International Scholar), Crowell & Moring LLP
Washington DC, U.S.A.

Starting from March 1, 2010, foreign companies or individuals investing in China will have one more structuring option to team up with their Chinese partners: to establish a foreign-invested partnership (“FIP”). Before that, partnerships could only be established by domestic entities or individuals; foreign-invested enterprises (“FIEs”) generally shall take one of the four corporate forms, including the equity joint venture (“EJV”), the contractual joint venture (“CJV”), the wholly foreign owned enterprise (“WFOE”), and the foreign-invested company limited by shares.

This new form becomes available with the State Council’s promulgation of the *Administrative Measures for the Establishment of Partnerships by Foreign Enterprises or Individuals in China* (State Council Decree No. 567, the “Measures”) on December 2, 2009. Subsequently on January 29, 2010, the State Administration of Industry of Commerce (SAIC) issued the *Administrative Regulation on the Registration of Foreign-invested Partnerships* (SAIC Decree No. 47, the “Regulation”) to further clarify issues presented by the Measures.

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[9] *Ibid.*

Approval Procedure
The Measures and the Regulation represent a significant departure from the previous legal regimes regulating FIEs in terms of the approval procedure. Traditionally, to establish FIEs in China, the investors have to first apply to the Ministry of Commerce or its local counterparts ("MOFCOM") for foreign investment approval, and then apply to the SAIC or its local branches for issuance of the business license. Under the Measures and the Regulation, however, FIPs will only have to be registered with SAIC or its local branches. As an unprecedented move, MOFCOM will be only notified by SAIC after the registration is completed. Note that other approvals that are a prerequisite for conducting specific business in China shall still be required.

Foreign Investment Policies
Notwithstanding removal of MOFCOM approval, foreign investment by means of FIPs shall also abide by industrial policies for foreign investment, including the Guidance Catalog of Foreign-invested Industries (the latest version released in 2007). According to the Regulation, FIPs are not allowed to invest in prohibited industries, industries that are open only to CJVs and/or EJVs, industries where the Chinese party shall be the majority or controlling shareholder or industries where restrictions are imposed on the shareholding ratio by foreign investors, as specified in the Guidance Catalog. The applicant shall submit to SAIC an explanation of its compliance with these policies.

Implication for Private Equity/Venture Capital Funds
When the Measures were released, there was hope as well as doubt as to whether foreign-invested PE/VC funds may take advantage of the FIP form. Unlike the common practice in U.S. where PE and VC firms usually take the form of a limited partnership, in China, since FIPs were not allowed under the Partnership Law, onshore funds may only take the corporate form or the so-called "non-legal person" form as prescribed by the Administrative Measures for Foreign-invested Venture Capital Enterprises (effective as of March 1, 2003, "FIVCE Measures"). Requirement under the FIVCE Measures for establishing a foreign-invested PE/VC fund is very high and the MOFCOM pre-approval is also a must.

The Regulation appears to have cleared the doubt by confirming that "provincial level SAIC is responsible for the registration of foreign-invested partnerships whose principal business is making investment". It does not suggest such FIPs shall be subject to pre-approval by MOFCOM or any other special requirement. Nevertheless, it remains to be seen to what extent can foreign-invested PE/VC funds employ this new model.

Conclusion
On March 1, 2010, the first FIP was reportedly established in Kunshan, Jiansu by a US company and a Chinese citizen with the total contribution of RMB12 million (USD1.7 million). Without doubt, this marks an important development of the Chinese foreign investment regime, a step towards further integration with the global market. With the simplified registration process and the expected "pass-through" tax treatment, FIPs may become yet another important vehicle for foreign investment. There are still uncertainties, however, such as the tax, foreign exchange, accounting and customs issues of FIPs, application of the rules to PE/VC funds, and the coordination between SAIC, MOFCOM and other government authorities. Interested investors therefore should keep a close look at further regulatory development in this area.

Recent developments

By Anand S. Dayal, Koura & Co. Advocates, New Delhi, India

Cap on royalty payments abolished

In a relaxation that is expected to provide a significant boost to the franchising of foreign brands in India, the Government has abolished the cap on payment of royalty (or lump sum fee) for transfer of technology and on payments for the use of foreign trademarks or brand names in India. Payment is now permissible without limit under the "automatic route". Under the automatic route, prior approval of the Government is not required; rather, certain post-transaction regulatory filings (details to be notified by the Government) are required.

Until the aforesaid relaxation, the following limits (caps) applied under the automatic route:

Type of Arrangement	Lump Sum	Royalty
Foreign technology transfer	$ 2 million	5% of domestic sales 8% of export sales
Trademark or brand name licensing (without technology transfer)		1% of domestic sales 2% of export sales

For payments exceeding the above caps, prior approval of the Government of India (Project Approval Board, Department of Industrial Policy and Promotion) was previously required. For the period 1991 to June 2009, the Government had granted 8062 approvals for technology collaborations. Note that different norms apply to the hotel sector.

ADR/GDRs - takeover code implication

ADR/GDRs which entitle the holder to voting rights in the underlying shares are now treated at par with domestic shares for purposes of the SEBI (Substantial Acquisition of Shares or Takeovers) Regulations, 1997 ("Takeover Code"). This means that a foreign investor who acquires ADRs/GDRs which entitle the investor to exercise the right to vote the underlying shares "in any manner whatsoever" will not be exempt from the open offer requirements of the Takeover Code. Accordingly, such ADR/GDR holders will now be required to make an open offer to the domestic shareholders of the company if the underlying shares of the ADR/GDRs held by the foreign shareholder exceed 15 percent of the issued shares. ADR/GDRs are overseas depository receipts issued to overseas investors against domestic shares issued by Indian companies.

The open offer is required within four working days of the acquisition of such ADR/GDRs. Previously, the open offer requirement applied only if and when the ADR/GDRs were converted into or exchanged for the underlying shares (not at the time the ADR/GDRs were acquired).

The above requirement was introduced in November 2009 by an amendment to the Takeover Code. Note that the amendment affects only ADR/GDRs wherein the voting rights are exercisable "by the holder". Often this is not the case, as the voting rights are typically held by the custodian bank that issues the depository receipts, not the ADR/GDR holder.

Country update on New Zealand

M&A and JV Activity

By David Quigg/John Horner/Asha Stewart,
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New Zealand: M&A and JV Activity
2009 saw a drop-off in New Zealand M&A activity as a result of the continued global economic turbulence, though the new year has seen increased interest on this front. Joint Ventures have been seen moving back into favour, as investors look to embrace opportunities while keeping exposure limited.

Review of the Overseas Investment Act 2005
Under current New Zealand law, in certain circumstances international mergers, acquisitions, or joint ventures may require consent from the New Zealand Overseas Investment Office where there is a New Zealand business operated by the "target". This can have an impact on the timing of the transaction, as consent applications can take some time to be processed.
On 17 March 2009, the new National government announced a review of the overseas investment rules. The review aimed to make foreign investment in New Zealand simpler and more attractive, while at the same time protecting sensitive land, assets, and resources.
On 23 July 2009, Minister of Finance Bill English announced changes to the Overseas Investment Procedure, by delegating greater decision-making powers to the Overseas Investment Office. The Overseas Investment is now able to decide all applications apart from those relating to rural sensitive land, or land adjoining waterways, without reference to the Minister. Where applications *are* to be decided by the Minister, the Overseas Investment Office is able to both give advice and make recommendations to the Minister in respect of that application.[10]
In addition, several types of transactions of a minor, technical or temporary nature have been exempted from the Act. Examples include some underwriting transactions and sales within a group of companies with shared ownership. These transactions result in little or no change to the overseas ownership of sensitive assets.
The Government is now looking to consider the second part of the review, aimed at simplifying the screening process, providing greater certainty, and reassessing the screening thresholds.

Takeovers: Guidance Notes available
The Takeovers Panel has recently issued Guidance Notes on the timing rules in the Takeovers Code and the application of the Code to joint holders or controllers of voting rights in a Code company. The

Guidance Notes are available on the Panel's website, www.takeovers.govt.nz. Please do not hesitate to contact the authors if you would like further information.

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[10] From the amended Ministerial Directive Letter dated 21 December 2009, available at: http://www.linz.govt.nz/overseas-investment/about-oio/news/2010/0112-amendment-ministerial-directive/index.aspx

2009 Merger & Acquisition in South Korea

By Mr. Hee-Chul Kang (co-head) and Mr. Ki-Young Kim (partner), Yulchon's corporate and finance group, Seoul, South Korea

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Major Trends for 2009.

The total market size for M&A transactions in Korea decreased in 2009. According to statistics released by the Korea Fair Trade Commission, only 413 merger review requests were filed. There were 550 in 2008, 857 in 2007, and 744 in 2006. Bloomberg reported slightly different, but still lower, numbers, namely 851 mergers (approximately USD 45 billion), which signifies a 2.74% reduction from the 2008 gross amount (or proceeds) and a 1.85% numerical reduction.

There were, however, some positive signs. M&A activities between affiliated firms increased in 2009. This trend was particularly strong in the communications sector. For example, KT merged with KTF, and LG Telecom merged with LG Dacom and LG PowerCom. Outside of the communications sector major mergers between affiliates included a merger between Hyundai Mobis and Hyundai Autonet and a merger between Samsung SDS and Samsung Networks. Other notable M&A transactions include KKR and Affinity's acquisition of Oriental Brewery Company and E-bay's acquisition of G-Market.

2009 M&A Related Legal Developments

2009 was notable because of several high-profile legislative efforts to stimulate mergers and acquisitions. Under the Capital Market Act, investors can now use a Special Purpose Acquisition Company ("SPAC") for the sole purpose of carrying out a merger or acquisition. An SPAC generates profits by using funds gathered from public investors to carry out a merger or acquisition.

On December 1, 2009, the Korean government also announced the impending introduction of a statutory based poison pill, which target companies would be able to use as a defensive measure against hostile takeovers. There has been, however, considerable opposition to this proposed amendment. Thus, it is not clear whether the amendment will actually occur in 2010.

Country update on Spain

By Albert Garrofé (NY) and Idoya Fernández (Madrid) Cuatrecasas, Gonçalves Pereira

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Remuneration of directors of listed companies

In April 2009, in view of the experience of recent years and that which has been acquired as a result of the financial crisis, the European Commission issued a new recommendation regarding the remuneration of directors of listed companies ("Recommendation 2009/385/EC"). In Spain, the reaction to Recommendation 2009/385/EC has consisted of:

- A proposal for the amendment of the Securities Exchange Act included in the Draft Bill for Sustainable Economy in order to elevate to the status of law the corporate governance recommendations on the transparency of compensation plans. Specifically, the mandatory compliance of the obligation to release and submit to the General Shareholders' Meeting, for consultative purposes, a report detailing the individual remuneration of the Directors and top executives shall be established as a legal regulation.

- The proposal to update the Combined Code on Corporate Governance that adopts, under the “comply or explain“ principle, the measures of the European Commission’s Recommendation. This proposal concerns the recommendations on the compensation structure for directors and the composition and functions of the Remuneration Committee.

It consists of legal regulations and corporate governance rules that are still being drawn up but which, in the future, shall increase the transparency of the remuneration of directors of listed companies.

Listed Public Limited Companies in Real Estate Market Investment

The Listed Public Limited Companies in Real Estate Market Investment (“SOCIMI” by their initials in Spanish), governed by Act 11/2009, are a new figure aimed at channelling investments in the real estate market with a view to boosting the rental market, increasing the competitiveness of the Spanish securities markets and revitalising the real estate market. It is a figure that is known as Real Estate Investment Trusts (REITs) in other legal systems.

The SOCIMI are listed public limited companies in a regulated market that must meet certain commercial, regulatory and tax requirements. Meeting these requirements allows them to take part in a special tax regime.

The commercial system of the SOCIMI companies is primarily centred on the following three requirements: activity limited to real estate activities, stock trading and mandatory dividend distribution. Their special tax regime is based on making the SOCIMI companies pay taxes on the revenue generated by the real estate investments, instead of placing this tax burden on the shareholder.

Circular of the Spanish Securities and Exchange Commission on material information

Circular 4/2009, of November 4, 2009, of the Spanish Securities and Exchange Commission describes the procedures and requirements for communicating material information, in line with section 82 of the Securities Act and Order EHA/ 1421/2009. Annex I to the Circular includes a list of examples that can be considered material facts. This list is for information purposes only and is not exhaustive.

European Court of Justice’s ruling: insider dealing

The European Court of Justice’s ruling of December 23, 2009, regarding the Spector Group versus Van Raemdonck case, clarifies the Market Abuse Directive on insider dealing (particularly, the expression “use of inside information” in Article 2(1)).

The Court held that, in a proper interpretation of Article 2(1) of the Market Abuse Directive, if a primary insider possessing inside information, acquires or disposes of, or tries to acquire or dispose of, for his own account or for the account of a third party, either directly or indirectly, the financial instruments to which that information relates, implies that that person has ‘used that information’ within the meaning of that provision, but without prejudice to the rights of the defence and, in particular, to the right to be able to rebut that presumption. The question whether that person has infringed the prohibition on insider dealing must be analysed in the light of the purpose of the directive: to protect the integrity of the financial markets and enhance investor confidence. This confidence is based, in particular, on the assurance that investors will be placed on an equal footing and protected from the misuse of inside information.

"Debt for Equity Swap -A "band aid" banking on economic recovery"

By Steve Wilson (Partner – Palo Alto, CA) & Catherine Williams (Senior Associate, London, UK), Osborne Clarke

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Converting debt to equity

In the current climate of debt heavy balance sheets, absence of liquidity and lack of new bank finance many companies are being forced to restructure. Beleaguered companies experiencing short term financial difficulties are considering ways to improve their working capital position, and reduce their gearing to attract new debt. Creditors are becoming increasingly concerned about levying high rates of interest with little hope of recouping their unsecured debt if the company enters into liquidation. Recognising that their debt is "under water" and ranks after senior secured and mezzanine debt, lenders are looking for an alternative to calling in their loans or winding up the company. Rather then forcing a company to service high rates of interest and risking insolvency, an investor holding unsecured debt may prefer the debt to be converted into a new class of equity (shares, warrants or options) to permit them to take control and revive the company, participating in any long term upturn.

A current trend

The UK and international market are experiencing small and large scale debt for equity swaps as creditors gamble on an upturn in the market. In the UK Foxtons, the troubled chain of estate agents backed by private equity house BC Partners approved a write off of debt of between £60-£90 million in exchange for a majority equity stake. Gala (the gambling group that also runs Coral) converted £540m mezzanine debt into new equity rather than sell out to their private equity owners Blackstone and Permira. Eurotunnel wrote off approximately 50% of its £6 billion debt in exchange for an equity stake of up to 87% issued to its senior creditor. The building society group West Bromwich, assisted by the Financial Services Authority ("FSA") and the UK Treasury, enabled bondholders holding £182.5m of subordinated debt to exchange their debt for "profit participating deferred shares" classed by the FSA and UK Treasury as Core Tier 1 capital (equity). In September last year Jessops approved a solvent restructuring rather than a pre pack administration. As a result HSBC converted its £34 million debt into 47% of the share capital of the Company.

What would lenders be seeking on conversion of their debt?

The lender will often request a quasi debt like equity (redeemable preference shares). If the Company is already in breach of existing financial covenants, they may insist on enhanced voting rights and replacing the board to exert as much control over the company as possible. This new class of share ranks ahead of the existing ordinary shares held by current shareholders, carries prior rights to dividends and, if the company were to go into liquidation, capital. These preference shares may be redeemable or convertible into ordinary shares on an exit.

Warrants can be issued as an alternative to shares, offering many of the advantages of an equity holding including the chance to share in any improvement in the company's fortunes.

Various factors govern how much of an equity stake the lender is prepared to take in the Company. The lender may wish to avoid consolidating its accounts and therefore need to cap its percentage shareholding whilst the company may not wish to trigger change of control provisions. In the UK, investing (either alone or with connected parties through a lending syndicate) in more than 30% of the share capital of a listed company may trigger a mandatory offer to purchase the remaining equity of the company.

Consent issues
Existing shareholders will need to be persuaded that the dilution of their shareholding and relinquishment of their control over the Company is necessary to effect the restructuring and save the company from liquidation. Disgruntled shareholders may try to withhold their consent and the creditors may then insist on having a liquidator or administrator appointed to the borrower by way of scheme of arrangement, company voluntary arrangement or pre pack structure.
The bid by Citigroup to reduce the high debt exposure of EMI by converting debt to equity was rejected by Terra Firma the private equity and principal shareholder. Senior Lenders may also be required to provide consent. In the Gala proposal the mezzanine consortium were dependant upon the consent of the Royal Bank of Scotland and Lloyds Banking Group to agree to the restructuring.

Procedure
Once agreement has been reached on the amount of debt to be converted, the form of equity to be issued and the percentage shareholding, it is necessary to determine whether the Company has sufficient share capital for the purposes of the conversion whether the directors have authority to allot the relevant shares? The allotment of shares to creditors in consideration for the release of their debt (at least insofar as that debt is for a liquidated sum) constitutes an allotment for cash and accordingly under English law the shares must first be offered *pro rata* to existing shareholders unless pre emption provisions have been disapplied by the shareholders of the company. The rights attached to the new class of shares will be documented in revised articles of association and possibly a new or amended Shareholders Agreement. In the case where there are other senior creditors the Intercreditor Agreement will require amendments and a moratorium called on all existing debt whilst the restructuring takes place.

Tax issues
The release of debt may generate taxable income in the debtor company. The issue of equity in consideration for the release of debt may be treated as a payment, for UK tax purposes, of accrued interest on the debt converted, resulting in potential withholding obligations for the company, where actual interest cannot be paid gross and on a deemed receipt of interest by the creditor. The interest may be capitalised but 20% withheld to meet the potential withholding tax liability. The equity issued must be at market value. If the debt to be released exceeds the value of the equity to be issued this could give rise to a taxable gain for the Company. If the value of the equity exceeds the value of the debt this may give rise to a taxable gain for the lender receiving the equity. Valuation in the current market often causes concern as market value is often based on projections and debt is written down from face value if the lender is in breach or in financial difficulties.

Accounting Issues International Financial Reporting Interpretations Committee ("IFRIC")
IFRIC 19 (published in November 2009), examines the valuation of debt and equity ("Extinguishing Financial Liabilities with Equity Instruments"). IFRIC recognises that lenders may renegotiate the terms of loans to companies in financial difficulty, sell on their loans to other investors or accept equity in full or partial settlement of the debt. IFRIC are also concerned about the practical difficulties of entities measuring fair value of the equity issued and the financial liability if the company is in financial difficulty. The Committee concluded that the valuation of the equity is to be assessed at the fair value of the liability to be extinguished. Any difference between the carrying amount of the financial liability and the fair value of the equity instrument issued (or fair value of the liability extinguished if the fair value of the equity instrument cannot be reliably measured ie if the Company is in default) should be recognised as a gain or loss in profit or loss.

The Future

A debt to equity swap offers a short term financial solution for creditors and company alike. The current climate has seen many high profile debt to equity swaps which have prevented liquidation of the company. Encouraging this means of corporate restructuring the UK Government has launched the "Capital for Enterprise Fund" encouraging small companies with up to £50 million turnover to develop their business by selling debt in exchange for an equity stake in the business. The fund provides equity and/or mezzanine finance of between £250,000 and £2 million for companies in need of long term capital.

Critics of the debt to equity "band aid" have complained that if over time lenders cease to recognise any inherent long term value in the company they may look to liquidation as the only viable alternative to recoup their investment, having suffered the costs of the initial financial restructuring. No one disagrees however that the debt to equity model is a predominant feature of the current economic landscape and most anticipate a continual appetite in the market for this style of financial restructuring.