Structured Finance & Securitisation

Contributing editor
Patrick D Dolan

2018

GETTING THE DEAL THROUGH

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Structured Finance & Securitisation 2018

Fourth edition

Getting the Deal Through is delighted to publish the fourth edition of *Structured Finance & Securitisation*, which is available in print, as an e-book, and online at www.gettingthedealthrough.com.

Getting the Deal Through provides international expert analysis in key areas of law, practice and regulation for corporate counsel, cross-border legal practitioners, and company directors and officers.

Throughout this edition, and following the unique **Getting the Deal Through** format, the same key questions are answered by leading practitioners in each of the jurisdictions featured. Our coverage this year includes new chapters on Luxembourg, Spain and Turkey.

Getting the Deal Through titles are published annually in print. Please ensure you are referring to the latest edition or to the online version at www.gettingthedealthrough.com.

Every effort has been made to cover all matters of concern to readers. However, specific legal advice should always be sought from experienced local advisers.

Getting the Deal Through gratefully acknowledges the efforts of all the contributors to this volume, who were chosen for their recognised expertise. We also extend special thanks to the contributing editor, Patrick D Dolan of Norton Rose Fulbright US LLP, for his continued assistance with this volume.

GETTING THE DEAL THROUGH

London
February 2018

Japan

Motohiro Yanagawa, Takashi Tsukioka and Yushi Hegawa

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General

1 What legislation governs securitisation in your jurisdiction? Has your jurisdiction enacted a specific securitisation law?

There is no legislation that specifically governs securitisation in Japan.

Rather, securitisation in Japan is governed by laws and regulations applicable to specific types of transactions such as the Civil Code (Law No. 89, 1896), the Trust Act (Law No. 108, 2006) and the Financial Instruments and Exchange Law (Law No. 25, 1948) (FIEL). That said, there is a law specifically dedicated to facilitating asset securitisation, which is the Act on the Securitisation of Assets (Law No. 105, 1998) (the Securitisation Act). This Act authorises the use of two types of vehicle specifically designed for securitisation, namely the specific purpose company (TMK) and the specific purpose trust (TMS), and provides for relevant regulations applicable to them. TMKs are frequently used as issuer vehicles for Japanese asset securitisation transactions. However, the use of those vehicles is not required and many securitisation transactions involve schemes that are not based on the Securitisation Act.

2 Does your jurisdiction define which types of transactions constitute securitisations?

There is no law that specifically defines which types of transactions constitute securitisations in Japan. The Securitisation Act broadly defines asset securitisation as follows:

- a series of acts wherein a TMK acquires assets with monies obtained through the issuance of securities or borrowings;
- or wherein a trustee holds assets in trust and issues trust beneficiary certificates representing interests in a TMS; and
- with monies obtained through the administration and disposition of such assets, performs payment obligations in relation to such securities, borrowings or trust beneficiary certificates, as the case may be.

Under the Securitisation Act, TMKs and TMSs are authorised to carry out transactions that are contemplated by the above definition.

3 How large is the market for securitisations in your jurisdiction?

According to a survey conducted jointly by the Japanese Bankers Association and the Japan Securities Dealers Association, there were 73 reported securitisation transactions with underlying assets located in Japan in the first half of 2017, and the aggregate issue price of the securities issued in relation to those transactions is approximately ¥2.3 trillion. As this number is based on information provided through voluntary reporting, the actual number of securitisation transactions that took place in that period might be much larger.

Regulation

4 Which body has responsibility for the regulation of securitisation?

As there is no Japanese legislation governing securitisation in general, there is no body with specific responsibility for the regulation of securitisation. Nevertheless, as securitisation typically involves securities and financial transactions, the Financial Services Agency of Japan (FSA) fulfils an important role in the context of securitisation regulation in general. Under the Securitisation Act, it is the prime minister who is primarily in charge of administrating a regulation framework for TMKs. However, this authority is delegated to the commissioner of the FSA who, in turn, has delegated this authority to the director generals of the local finance bureaux.

5 Must originators, servicers or issuers be licensed?

Even though many originators of securitisation transactions are licensed under regulations governing their specific businesses, to which the underlying assets relate (eg, an operator of a banking business is required to obtain a licence under the Banking Act (Law No. 59, 1981)), there is no licensing requirement specifically applicable to originators or issuers to conduct securitisation transactions in general. However, TMKs and trustees of TMSs are subject to a notification requirement under the Securitisation Act (see question 19). In general, servicers are also not subject to a licensing requirement. However, to engage in certain collection activities as a 'special servicer' will require a licence under the Servicer Act (see question 13).

6 What will the regulator consider before granting, refusing or withdrawing authorisation?

As explained in question 5, there is no licensing requirement applicable to securitisation transactions in general. A local finance bureau will typically only check whether a filing document has been prepared in accordance with an appropriate format in relation to a notification submitted by a TMK.

7 What sanctions can the regulator impose?

As explained in question 5, there is no licensing requirement applicable to securitisation transactions in general. As for the notification requirement under the Securitisation Act, the failure to submit the required notification may result in imprisonment for up to three years, a fine of up to ¥3 million, or both.

8 What are the public disclosure requirements for issuance of a securitisation?

There is no public disclosure requirement applicable to issuance of securitisation instruments in general. Depending on the type of instrument issued for the transaction in question (ie, bonds, shares or trust beneficiary certificates) and the method of the offering (ie, public offering or private placement), the issuance may be subject to public disclosure requirements applicable to certain securities in accordance with the FIEL.

9 What are the ongoing public disclosure requirements following a securitisation issuance?

There is no ongoing public disclosure requirement following a securitisation issuance in general. Depending on the type of instrument issued for the transaction in question (ie, bonds, shares or trust beneficiary certificates) and the method of the offering (ie, public offering or private placement), the issuer may be subject to ongoing public disclosure requirements applicable to certain securities in accordance with the FIEL.

Eligibility

10 Outside licensing considerations, are there any restrictions on which entities can be originators?

In general, there are no restrictions on which entities can be originators as a matter of Japanese law. However, in practice, parties such as arrangers and rating agencies will closely scrutinise potential originator candidates to determine their qualifications in several respects including, among others, their ability to manage and service the underlying assets, the quality of the securitised assets and even their creditworthiness. Therefore, only entities that are deemed qualified by those parties may become originators for credit-rated transactions.

11 What types of receivables or other assets can be securitised?

In terms of the types of assets that can be securitised, there is no restriction under Japanese law specifically applicable to securitisation.

This is also the case for TMKs under the Securitisation Act, with limited exceptions, such as partnership interests, silent partnership interests and beneficial interests in a trust whose trust asset is cash. Types of receivables that are commonly securitised in practice include:

- receivables on loans secured by residential mortgages;
- credit card receivables;
- lease receivables;
- auto-loan receivables; and
- account receivables, which include promissory notes.

Real estate is another type of asset commonly securitised in Japan.

12 Are there any limitations on the classes of investors that can participate in an offering in a securitisation transaction?

There are no limitations on the classes of investors that can participate in an offering in a securitisation transaction. However, practically speaking, the securitisation structure is too complicated and the face-value amounts of the securitisation instruments are too large for retail investors, therefore, only institutional or relatively larger (and more sophisticated) investors are targeted for securitisation transactions.

13 Who may act as custodian, account bank and portfolio administrator or servicer for the securitised assets and the securities?

There is no regulation specifically applicable to securitisation transactions that identifies or describes the qualifications to serve as custodian, account bank and portfolio administrator, though an entity serving in any such capacity may be subject to generally applicable regulations, for example, an accounting bank should have a banking licence under the Banking Act. As for servicers in receivable securitisation transactions, a common structure is for the originator to serve as the primary servicer until:

- a servicer termination event occurs, in which case a backup servicer will succeed the originator as the primary servicer; or
- a securitised receivable becomes delinquent, in which case a 'special servicer', which is often a servicer licensed under the Act on Special Measures Concerning Claim Management and Collection Businesses (Law No. 126, 1998) (the Servicer Act), will succeed the originator and commence collection proceedings in relation to the receivable in question.

The arrangement of the second point above is necessary owing to the Japanese Attorney Act (Law No. 205, 1949), which prohibits members of the general public who are not licensed attorneys from providing legal services (the collection of delinquent receivables would fall into this category). Under the Securitisation Act, a TMK must entrust the securitised assets that it holds to a licensed trustee, which essentially entails a transfer of title to the trustee, unless the relevant asset is real estate, receivables and some other assets, in which case the TMK may retain the originator, or some other person with sufficient financial soundness and personnel capable of administrating and disposing of the securitised assets appropriately, as the administrator that will administer and dispose of the securitised asset. In the latter case, the administrator will be subject to various obligations such as segregation of securitised asset from its own assets and cooperation with document inspection requests from the TMK.

14 Are there any special considerations for securitisations involving receivables with a public-sector element?

To date, it has been understood that securitisation of assets held by the public sector is difficult. However, it is viewed that this might be a promising new type of securitisation in the future after difficulties in relation to approvals, such as the Local Autonomy Act (Law No. 67, 1947) that requires an approval of local assembly for disposal of assets and any other procedures, are overcome. In fact, there is one financing transaction executed by a public-sector entity, which is wholly owned by a local government, that utilises such entity's receivables for securitisation. If similar transactions occur in the future, another asset class for investors may be realised.

Transactional issues

15 Which forms can special purpose vehicles take in a securitisation transaction?

As explained above, TMKs are special purpose vehicles (SPVs) frequently used in securitisation transactions. In addition to TMKs, a trust is also a vehicle that is commonly used in securitisation transactions. Typically, the originator, as the settlor, will entrust its asset by conveying it to a trustee and, in return, acquire beneficial interests in the trust. Thereafter, the settlor will sell such beneficial interest to investors and thereby raise funds. Alternatively, the originator may be able to sell the beneficial interests in the trust to a TMK. In this case, the TMK will issue securities to its investors and the proceeds from such issuance are paid to the originator as payment of the purchase price for the beneficial interest in the trust. Also, pursuant to an amendment to the Trust Act made in 2006, the use of a declaration of trust is available in Japan.

For securitisation of real estate, limited liability companies (GKs) are also frequently utilised as SPVs. Usually each investor enters into a silent partnership contract (TK) with the GK, under which the investor makes a contribution to the GK and the GK distributes the profits arising from the asset (in this case, real estate) that it acquires using the funds contributed by the investor. Further, a general incorporated association under the Act on General Incorporated Association and General Incorporated Foundations (Law No. 48, 2006) is typically used to create a bankruptcy-remote holding company of the SPVs.

16 What is involved in forming the different types of SPVs in your jurisdiction?

In determining which type of SPV should be utilised, parties take into consideration various factors. Cost is one of the most important factors. Generally, a vehicle that will require the involvement of a financial institution, for example, a trust for which a trust bank will need to be appointed to serve as its trustee, may be costlier than vehicles that do not require such involvement (eg, a GK). The nature of the investment, whether it is debt or equity, will also influence the type of vehicle to be used. Trusts and TKs are usually used for equity investments, whereas both debt and equity instruments can be issued by a TMK.

17 Is it possible to stipulate which jurisdiction's law applies to the assignment of receivables to the SPV?

Under Japanese conflict-of-law rules (the Act on General Rules for Application of Laws (Law No. 78, 2006)), the effect of an assignment of receivables, regarding the obligor and any third party, would be determined based on the law applicable to the assigned receivables. This means that even if the governing law of the receivables purchase agreement (RPA) is Japanese law, the effect of the assignment in relation to its obligor and any third party, such as matters related to perfection, under the RPA is determined based on the law governing the assigned receivables rather than the law governing the RPA.

18 May an SPV acquire new assets or transfer its assets after issuance of its securities? Under what conditions?

Generally speaking, a Japanese SPV can acquire new assets or transfer its assets after issuance of its securities. The conditions for the acquisition of new assets or transfer of assets are reflected in the relevant contracts and are not stipulated by law. Usually such conditions are set forth in the contracts after taking into consideration their potential effect on:

- the rating of the existing securities;
- the loan-to-value ratio;

- the debt service coverage ratio;
- the limited recourse structure;
- true sale-related concerns; and
- other factors that may affect the securities.

Where a TMK is used as an SPV and acquires new assets or transfers its assets, unless such acquisition or transfer is anticipated under its asset securitisation plan (this plan is to be attached to the TMK's business commencement notification, which is to be filed with the local finance bureau; see question 19), a change of the asset securitisation plan will need to be filed. This change may require the consent of interested persons, including all of the investors. Further, acquisition of additional parcels of real estate by a TMK is currently limited to certain cases, such as acquisition of real estate that is affiliated with the real estate already held by the TMK.

19 What are the registration requirements for a securitisation?

In general, no registration is required for securitisation, except for securitisations using a TMK or a TMS under the Securitisation Act and which require the submission to the local finance bureau of a prior notification of the business commencement notification or TMS notification, as the case may be. Documents such as the TMK's asset securitisation plan (ie, a document setting forth the basic particulars concerning the asset securitisation to be carried out by the TMK) are to be attached to this notification.

20 Must obligors be informed of the securitisation? How is notification effected?

Obligors need not be notified in order to carry out a securitisation. Rather, it is performed for the purpose of perfection of the receivables that are to be acquired.

There are three ways to perfect an assignment of receivables:

(i) by sending a written notice with a notarised date to the third-party obligor;
(ii) by obtaining a written consent with a notarised date from the third-party obligor; and
(iii) by registering the assignment with the competent legal affairs bureau pursuant to the Act concerning Special Exceptions to the Civil Code with respect to the Perfection of Assignment of Movables and Receivables (Law No. 104, 1998) (the Perfection Act).

In the case of method (iii), for an assignment to be able to be registered, the assignor must be a juridical person registered in Japan (ie, a Japanese corporation). No such limitation or restriction exists with respect to the assignee or obligor. Further, it should be noted that in Japan perfection of an assignment in relation to third parties, other than the obligor, is not sufficient to assert the assignment against the obligor. Methods (i) and (ii) would satisfy both requirements, but completion of the registration in accordance with the Perfection Act through method (iii) only relates to perfection in relation to third parties.

In order for the assignment to be perfected regarding the obligor, in addition to the registration provided in method (iii):

(a) the assignor or the assignee must send to the obligor a notice stating that the assignment has been made, and that such assignment has been registered, together with a certificate of registered matters issued by the competent legal affairs bureau; or
(b) the obligor must consent to the assignment and acknowledge the registration of such assignment.

In cases where method (iii) is used, which is often the case where receivable securitisation transactions are conducted on an undisclosed basis with regard to obligors, it is common that the procedures for perfection regarding the obligors in accordance with methods (a) and (b) will not be taken until certain events such as a default of the originator occurs.

21 What confidentiality and data protection measures are required to protect obligors in a securitisation? Is waiver of confidentiality possible?

The Act on the Protection of Personal Information (Law No. 57, 2003) (the Personal Information Protection Act) is the Japanese law that was enacted to protect the rights and interests of individuals while taking into consideration the usefulness of personal information, especially in light of the remarkable increase in the use of personal information with the development of our advanced information and communications society. Pursuant to the Personal Information Protection Act, a business operator handling personal information may not provide personal data to any third party without the prior consent of the affected individual, except in the following instances:

(i) where such provision of personal data is done pursuant to applicable laws and regulations;
(ii) where such provision of personal data is necessary for the protection of the life, body or property, and in situations where it is difficult to obtain the consent of the affected individual;
(iii) where such provision of personal data is necessary for improving public health, or promoting the sound growth of children and it is difficult to obtain the consent of the affected individual; and
(iv) where such provision of personal data is necessary to cooperate with a state organ, a local government, or an individual or a business operator entrusted to execute certain affairs prescribed by laws and regulations in situations where obtaining the consent of the affected individual is likely to impede the execution of such affairs.

In conjunction with the transfer of receivables, some personal data may need to be provided to the SPV. For practical reasons, it may not be feasible to obtain the consent of the affected individual.

For credit card receivables, auto-loan receivables and lease receivables, in order to facilitate securitisation, the originator usually insists on the inclusion of a provision in the underlying contract with the obligors, which acknowledges the obligor's consent to the provision of personal data in the case of an assignment (including, but not limited to, securitisation) of those receivables.

However, for assignments of receivables where the obligors' express consent to the provision of personal data is not obtained, further analysis is necessary to consider whether the provision of personal data in that situation may contravene the restriction imposed by the Personal Information Protection Act. Regarding this point, the current practical interpretation of the relevant law suggests that since a receivable is assignable in principle, the consent of the person to the provision of personal data can be assumed in the case of an assignment of receivables to the extent it will be necessary for the management and collection of such receivables by the assignee. In this situation, the exception in (ii) may apply, and therefore securitisation of receivables should be feasible.

22 Are there any rules regulating the relationship between credit rating agencies and issuers? What factors do ratings agencies focus on when rating securitised issuances?

Under the FIEL, credit rating agencies that satisfy certain conditions, such as the development of appropriate systems, can be registered. It is not mandatory for credit rating agencies to be registered in Japan. However, in cases where securities companies or other financial institutions conduct solicitations using a credit rating determined by an unregistered credit rating agency, they are required to explain to potential investors, among other things, that the 'rating is a rating by an unregistered credit rating agency'.

The independence of registered credit rating agencies is required under the FIEL. The FIEL also provides for regulations applicable to registered credit rating agencies covering, among other things, the following:

- quality control in the rating process, including measures to protect investors' interests in respect of the interests of the credit rating agency or other interested parties such as issuers and originators;
- prohibition of name lending;
- prohibition of the provision of ratings to closely related persons;
- prohibition of the concurrent provision of rating and consulting services;
- timely disclosure of information including rating determination policies; and
- periodic disclosure of information.

Therefore, a registered credit rating agency may be prohibited from providing a rating to a closely related issuer.

When rating securitised issuances, rating agencies mainly focus on cash flow analysis, bankruptcy-remoteness and operational risks of the transaction parties, taking into consideration quantitative and qualitative aspects of the structure and type of assets for each transaction.

23 What are the chief duties of directors and officers of SPVs? Must they be independent of the originator and owner of the SPV?

In cases where a joint stock company or a GK is used as an SPV, the Companies Act (Law No. 86, 2005) will apply.

With regard to joint stock companies, the relationship between the company and its directors is regulated by the provisions of the Civil Code addressing entrustment. Accordingly, a director has a duty to the company, to use the due care of a good manager (duty of due care) when performing the director's duties. In addition to this duty of due care, the Companies Act provides that directors of a joint stock company must comply with all laws and regulations and the company's articles of incorporation, as well as all resolutions adopted at general meetings of the company's shareholders, and that directors must perform their duties faithfully for the benefit of the company. This duty is generally called the 'fiduciary duty' of directors. There are also special provisions restricting or expanding the responsibilities of directors in certain situations or under certain circumstances, including but not limited to where competitive transactions or conflict of interest transactions exist.

With regard to GKs, members who manage a GK owe a duty of due care and a fiduciary duty to that GK. Such members are jointly and severally liable to the GK for any damage incurred by the GK that is caused by the non-performance of duties of the managing members. Unlike a joint stock company, the Company Act does not specifically provide an exemption from such liability. However, it is generally understood that a GK can grant an exemption from such liability, either in advance or after the fact, and the method for obtaining such exemption or conditions for the grant of such exemption may be set out in the GK's articles of incorporation.

In cases where a TMK is used as an SPV, the Securitisation Act will apply. The directors of the TMK owe a duty of due care and a fiduciary duty to that TMK. There are also special provisions restricting or expanding the responsibilities of directors in certain situations or under certain circumstances, including but not limited to, where competitive transactions or conflict of interest transactions exist. Further, if a third party sustains damages as a result of the wilful misconduct or gross negligence of directors of a joint stock corporation or a TMK or managing members of a GK in the performance of their duties, such directors or managing members will be jointly and severally liable to such third party for such damage.

There is no legal requirement for such directors or managing members to be independent of the originators or the owner of the SPV. However, it is usual practice for the SPV to appoint an independent director or managing member in order to secure the bankruptcy-remoteness of the SPV.

24 Are there regulations requiring originators and arrangers to retain some exposure to risk in a securitisation?

There is no regulation under Japanese law requiring originators or arrangers to retain some exposure to risk in a securitisation.

However, the Supervisory Guidelines and policies announced by the FSA provide that, in cases where financial institutions invest in securitised products, it is recommended that such investments be made only by those to which the originator retains some exposure to risk.

Notwithstanding the foregoing, it is usual for rating agencies to require that the originator be exposed to some risk in order to acquire a higher credit rating for the securitised product.

Security

25 What types of collateral/security are typically granted to investors in a securitisation in your jurisdiction?

Most transactions in Japan involving the securitisation of receivables are done without granting any collateral to the investors. Such deals are based on the understanding that:

- the SPV is a single-purpose entity;
- the management of assets and cash flow of the SPV is structurally controlled;
- the SPV will not enter into any unrelated transactions with third parties; and
- the SPV will not incur any unrelated debt.

On the other hand, in the case of securitisation of real estate, if the investment method is an asset-backed loan, collateral is usually granted in favour of the lender to secure the payment of such loans. Mortgages and pledges of real estate beneficial interests are typical types of collateral granted.

Regarding other types of securities, a security interest over receivables may be created either by way of a pledge or a security assignment.

A security interest over bank accounts and trust beneficial interests may be typically created by way of a pledge, and a security interest over movable assets is typically created by way of a security assignment.

If any collateral is created in order to secure payments of bonds, the Secured Bonds Trust Act (Law No. 52, 1905) will apply and a trust company will need to be appointed to manage such collateral for the benefit of bond holders. However, because the requirements and restrictions under the Secured Bonds Trust Act are stringent, inflexible and cumbersome, a grant of a security interest for bonds is rarely seen in the market.

Alternatively, bonds issued by a TMK can be secured by a general lien pursuant to the Securitisation Act. In such a case, the appointment of a trust company is not required, although the rights and interests granted to the holders of a general lien are relatively weak.

26 How is the interest of investors in a securitisation in the underlying security perfected in your jurisdiction?

The method for creating and perfecting a security interest depends on the type of security interest and the type of assets subject to the security interest.

Mortgage

To perfect a mortgage against third parties, the mortgage must be registered with the competent legal affairs bureau.

Pledge or security assignment of receivables

There are three ways to perfect a pledge or assignment, as explained in question 20:

- to send a written notice with a notarised date to the third-party debtor;
- to obtain a written consent with a notarised date from the third-party debtor; and
- to register the pledge or assignment with the competent legal affairs bureau pursuant to the Perfection Act.

Pledge over bank accounts

To perfect a pledge over a bank account, written consent with a notarised date is typically obtained from the bank at which the account is maintained.

Pledge over trust beneficial interests

To perfect a pledge over trust beneficial interests, a written consent with a notarised date is typically obtained from the trustee.

27 How do investors enforce their security interest?

In general, enforcement of a security interest can be made through a judicial proceeding or private sale. The actual methods of enforcement may vary depending on the type of security and the arrangements specific to each transaction.

28 Is commingling risk relating to collections an issue in your jurisdiction?

In a Japanese securitisation deal, the originator is usually appointed by the SPV to serve as the servicer for continued collection and management of the receivables. Payments by obligors will continue to be made to the originator, and collections in respect of transferred receivables may be commingled with the originator's other funds such as collections in respect of non-transferred receivables. If the originator or any successor servicer appointed or provided for under the servicing agreement is declared bankrupt or is subject to corporate reorganisation or civil rehabilitation proceedings while holding collections in respect of the SPV's transferred receivables, it is likely that such collections would be treated as part of the originator's bankruptcy estate or the originator's estate subject to the corporate reorganisation or civil rehabilitation proceedings (or that of the relevant subsequent servicer), and

Update and trends

The long-awaited amendments to the Civil Code of Japan were finally approved by the Diet on 2 June 2017 and will become effective within three years. This is an epoch-making piece of legislation because the Civil Code of Japan has scarcely been amended in the 120 years since its initial enactment in 1896. The notable amendments are, inter alia, as follows:

(i) even in the event a creditor and debtor agree that the assignment of receivables is prohibited or limited (Assignment Limited Receivables), the assignment of such receivables may be valid, but the debtor may refuse to pay the receivables, or may claim the expiry of the receivables owing to payment to the assignor or other reasons, against the assignee who knew or did not, as a result of gross negligence, know of the agreement prohibiting or limiting the assignment of receivables;
(ii) it is statutorily confirmed that an assignment of future receivables will be valid even if such receivables have not yet been incurred upon such assignment;
(iii) standard terms and conditions of contract may be validly incorporated into the parties' agreement if certain requirements are satisfied;
(iv) the short-term statute of limitation applicable only to specific receivables, such as doctors' or attorneys' fees, food and drink charges owed to a restaurant or bar, etc, will be abolished and instead receivables will expire if they are not claimed within five years from the date a creditor knew that such receivables could be claimed, or if they are not claimed within 10 years from the date a creditor was able to claim such receivables;
(v) the statutorily applicable interest rate will be reduced from 5 per cent (fixed) to 3 per cent, and such interest rate will be revised according to the market interest rates from time to time;
(vi) an individual person's guaranty of business-related debts will be invalid unless such person's intention of guaranty is confirmed by a notarised document executed within one month prior to the execution of the guaranty agreement; and
(vii) the upper limit of the duration period for leasing will be changed from 20 years to 50 years.

Regarding the securitisation field, the amendments listed as items (i) and (ii) are especially important. Under the current law, the assignment of Assignment Limited Receivables is invalid unless the assignee does not know about the restriction, provided such lack of knowledge is not owing to such assignee's gross negligence. Therefore, current funding using Assignment Limited Receivables can be structured only by a declaration of trust structure or a participation structure. However, pursuant to the amendment listed at (i), it is expected that such amendment will help and facilitate companies in using their Assignment Limited Receivables as an asset for securitisation under an asset transfer structure. Further, under the present law, although there is no statutory provision to such effect, court precedents allow the assignment of future receivables. Statutory confirmation of the assignment of future receivables contributes to the stability of securitisation structures using future receivables.

not as funds owned by the SPV. In such a situation, it is likely that the SPV would not recover the full amount of such collections.

In order to mitigate such risk, one or more of the following tactics is usually used:

- reduction of the time period during which the originator or the subsequent servicer actually holds the SPV's funds in its accounts;
- inclusion of a provision in the servicing agreement, providing the SPV with the right to terminate the appointment of the originator or the subsequent servicer in certain circumstances, including the petition for commencement of bankruptcy or corporate reorganisation proceedings in relation to the originator or subsequent servicer;
- establishment of an obligation requiring the originator to post a cash reserve or provide cash collateral;
- establishment of an obligation requiring the originator as servicer to pay to the SPV the scheduled collection amount prior to actual collection from obligors;
- use of separate accounts for the management of collected funds; and
- use of bank guarantees to secure the payment obligations of the originator or subsequent servicer.

Taxation

29 What are the primary tax considerations for originators in your jurisdiction?

Originators will, in general, recognise gains or losses arising from the transfer of the subject assets to the securitisation vehicle. There are no measures for deferral of recognition of gains or losses for originators that are practically feasible in typical securitisation deals.

If the securitisation vehicle is a trust, in general, the subject assets that are entrusted will be deemed sold, and the originators will recognise the gains or losses, when the trust beneficial interest representing the beneficial ownership of the subject assets is sold to third parties other than the originator. Accordingly, for example, if the trust beneficial interest is structured to have two-tier tranches of the preferred trust beneficial interest and the subordinated trust beneficial interest as a mechanism for credit enhancement, and if the originator retains the subordinated trust beneficial interest, then the subject assets represented by such subordinated trust beneficial interest are not deemed sold even if they were entrusted to the trust. It should be noted that, under Japanese tax laws, the tax consequences of such two-tier trust beneficial interest structure are not necessarily clear.

If the originators are Japanese corporations, such as Japanese banks, they are in general subject to Japanese corporate income taxation on the gains, at the effective rate, including national and local taxes, of 29 to 30 per cent (for Japanese corporations having stated capital of more than ¥100 million).

30 What are the primary tax considerations for issuers in your jurisdiction? What structures are used to avoid entity-level taxation of issuers?

The primary tax considerations for issuers are to avoid entity-level income taxation at the issuer because issuers are SPVs. In order to achieve this, there are many measures that are employed in practice so as to minimise the taxable net income of the issuer. If there is any taxable income, it is subject to Japanese corporate income taxation (see question 29).

If the issuer is a TMK or a listed real estate investment trust (J-REIT, which is technically not a trust but rather is an independent Japanese corporation):

- interest payable on the bonds or loans issued by the TMK or the J-REIT is deductible for its corporate income tax purposes; and
- dividends payable on the equity securities issued by the TMK or the J-REIT are also deductible for its corporate income tax purposes pursuant to certain special taxation measures if, in general, more than 90 per cent of the distributable profits are distributed as dividends to the investors.

If the issuer is a GK in the securitisation of real estate (see question 14):

- interest payable on the bonds or loans issued by the GK is deductible for its corporate income tax purposes; and
- profit distributions payable under a TK (ie, sort of an equity investment) are also deductible.

In addition, especially in the case of securitisation of real estate, minimising transactional taxes is important. Applicable major transactional taxes include real estate acquisition tax and registration and licence tax. These can be avoided or substantially reduced by the issuer acquiring the trust beneficial interest representing the beneficial ownership of the real estate, rather than acquiring the fee simple title to the real estate. Also, there are special taxation measures reducing the applicable transactional taxes if a TMK or a J-REIT acquires the fee simple title to the real estate for the purpose of securitisation.

31 What are the primary tax considerations for investors?

The primary tax considerations for investors are the Japanese withholding tax and the regular Japanese income taxation (on a net basis), to be imposed on the payment of the yields from the investment (eg, interest and dividends). The Japanese taxation on the investors substantially differs depending on the type of the instrument or securities issued, and the classification of the investors for Japanese tax purposes (ie, Japanese resident or not).

If the investor is a non-Japanese corporation having no permanent establishment in Japan for Japanese tax purposes, as a general rule, the investor will be subject to Japanese withholding tax:

- at the rate of 15.315 per cent on the interest payable on the bonds;
- at the rate of 15.315 per cent (if the shares are listed) or 20.42 per cent (if the shares are not listed) on the dividends payable on the shares or other equity securities;
- at the rate of 20.42 per cent on the profit distributions to be payable under the TK; and
- at the rate of 20.42 per cent on the interest payable on loans.

Japanese taxation on foreign investors is finalised by such withholding tax, and there is no need to file a Japanese tax return. Tax treaties entered into between Japan and the country of tax residence of the investor may provide for exemption or a reduced rate with respect to such Japanese withholding tax. In addition, in the case of bonds, if the bonds are issued within Japan using the Japanese book-entry system, or issued outside Japan as Eurobonds, interest payable on such bonds may be exempt from Japanese withholding tax as special taxation measures, subject to compliance with certain procedural requirements.

Bankruptcy

32 How are SPVs made bankruptcy-remote?

The following methods are typically used to ensure the SPV's bankruptcy-remoteness; that is, the isolation of the SPV and its assets from the originator, the owner of the SPV or other relevant transaction parties in the event of a bankruptcy of the originator, the owner of the SPV or such other parties:

- structuring the transfer of assets to be a true sale and not a security transaction;
- ensuring that the transfer of assets from the originator to the SPV will not prejudice the interests of the originator's creditors, thereby reducing the risk that any assets so transferred will become subject to avoidance or revocation in the event the transfer is deemed to have been a fraudulent transfer;
- minimising any commingling risk;
- appointing independent directors for the SPV;
- structuring the owner of the SPV to be an independent bankruptcy-remote vehicle;
- prohibiting the SPV from engaging in any business other than the contemplated securitisation transaction, based on restrictions set forth in its articles of incorporation and other organisational documents;
- prohibiting the SPV from engaging in certain conduct, such as a merger with another entity or the hiring of employees; and
- causing the SPV and its directors or shareholders to waive its right to commence a bankruptcy proceeding, a civil rehabilitation proceeding, a corporate reorganisation proceeding or any other insolvency proceeding.

33 What factors would a court in your jurisdiction consider in making a determination of true sale of the underlying assets to the SPV (eg, absence of recourse for credit losses, arm's length)?

From a Japanese law perspective, 'true sale' means that the transfer of assets from the originator to the SPV will be regarded as a transfer of ownership of the assets and will not be recharacterised as an assignment for security purpose or a granting of any other security interest in such assets, even if a bankruptcy proceeding, a corporate reorganisation proceeding or some other insolvency proceeding is commenced with respect to the originator. If such recharacterisation takes place, the SPV's assets might be subject to the insolvency procedure in question.

It is critically important that a transfer of assets constitute a true sale in a case where a corporate reorganisation proceeding is commenced with respect to the originator, because the rights of secured creditors will be subject to such proceeding and payments to secured creditors will not be made until the court approves the reorganisation plan. On the other hand, under a bankruptcy or civil rehabilitation proceeding, secured creditors may have rights of exclusive preference and, in principal, the rights of secured creditors will not be substantially affected in such proceedings.

Currently, no statutory provision or published court precedent identifies factors that determine whether an assignment of assets is a true sale. However, the following factors are generally considered when determining whether an assignment of assets constitutes a true sale:

- the intention of the parties as indicated by the relevant contracts;
- whether the originator will retain any rights in or control of the assigned assets;
- whether there is any right or obligation by the originator to repurchase the assigned assets;
- whether the originator has any rights or interests in the cash-flow payments derived from the assigned assets;
- whether the transfer of the assigned assets is perfected;
- whether the originator warrants the ability of the obligors to make payments under obligations that relate to the assigned assets;
- whether the SPV will incur all losses and damages arising from defaults by obligors whose indebtedness is related to the assigned assets, and whether the originator will indemnify the SPV or its investors against such loss or damages;
- whether the purchase prices of the assigned assets are appropriate and determined based on the reasonable and fair value of the assigned assets; and
- whether the assigned assets are treated as absolute transfers in the originator's financial records and accounting books.

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34 What are the factors that a bankruptcy court would consider in deciding to consolidate the assets and liabilities of the originator and the SPV in your jurisdiction?

Currently, there is no such concept of consolidation in the Bankruptcy Law (Law No. 71, 1922), the Civil Rehabilitation Law (Law No. 225, 1999) or the Corporate Reorganisation Law (Law No. 154, 2002).

Therefore, if a bankruptcy, civil rehabilitation or corporate reorganisation proceeding is commenced with respect to the originator, the SPV and its assets should not be subject to such proceeding since there is no such concept of consolidation under the relevant laws. However, if the general theory of 'piercing the corporate veil' applies to the SPV, the SPV's status as a separate legal entity as distinguished from the originator is denied.

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